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# Trade and investment rules:
## Latin American perspectives

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This paper depicts the changing international landscape of investment rule-making from a Latin American perspective. It does so by looking first at the recent evolution of investment rules, pointing out differences and synergies between these closely intertwined processes and the role that Latin American countries have had in shaping them. Against the backdrop of repeated failures to develop a comprehensive set of investment disciplines at the multilateral level, the paper reviews the main arguments that have been recently advanced in favour of and against global rules for investment. The paper dissects the main reasons why investment fell off the negotiating agenda of the Doha Development Agenda of the World Trade Organization (WTO). It concludes with a number of policy lessons regarding the most optimal institutional settings in which to pursue various elements of investment rule-making and sketches a few forward-looking scenarios on investment rule-making at the multilateral level.

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# I
## Introduction

Investment rules governing cross-border investment flows usually consist of rules on treatment and protection of foreign direct investment (FDI), contributing to what is generally referred to as the "investment climate". Investment rules exist at the bilateral, regional and multilateral level. The question of how investment rules affect investment decisions has long generated heated policy debates. In general terms, a stable and transparent investment climate can be in the interests of investors when they were previously disadvantaged by unpredictable investment conditions. It is not clear whether this would lead to additional FDI or simply to more comfort for the investor. The predictability of the investment climate may be enhanced when domestic policies are enshrined or locked into international treaties. Much will also depend on existing practice. If treatment of existing investors is already good in practice, new rules will do little by way of generating new investment flows or a better investment climate, other than offering greater long-run security. Empirical evidence that addresses the effects of individual investment provisions on induced FDI remains scant, and results are largely indeterminate.

Against this background, host country governments have exhibited differing attitudes towards international investment rule-making. Latin American countries are probably among those that have shown the greatest activism. In the recent past, triggered in particular by the debt crisis of the 1980s, Latin American nations have recognized the importance of increased foreign investment flows into their economies. FDI can, at least partly, compensate for sources of capital that may otherwise become unavailable from international lenders in circumstances of heightened macro-economic turmoil. As a result, the region has witnessed a steady opening of investment regimes. Alongside domestic (or autonomous) investment regime liberalization, Latin American countries have engaged in a large number of international negotiations. Virtually all of them are today World Trade Organization (WTO) members, are party to one or more free trade other integration agreements, and are signatories of numerous bilateral investment treaties.[1]

This paper depicts the changing international landscape of investment rule-making from a Latin American perspective. Following the introduction, section II reviews the WTO disciplines. Section III looks at the scope and content of bilateral and regional agreements. Section IV provides an overview of the main arguments that have been advanced in favour of and against investment rule-making at the multilateral, bilateral and regional levels. Section V explores some of the reasons that investment fell off the negotiating agenda of the Doha Round. Section VI concludes by drawing policy lessons and sketches a number of forward-looking scenarios on investment rule-making at the multilateral level.

# II
## WTO disciplines

Multilateral rule-making on investment has a troubled history. The investment chapter of the 1948 Havana Charter was one of the main reasons for the downfall of the proposed International Trade Organization project. In the General Agreement on Tariffs and Trade (GATT) that survived, no further investment-related negotiations took place until the Uruguay Round negotiations in the mid-1980s.

☐ This is a revised version of the work contained in Sauvé (2006). The views expressed here are those of the author and do not necessarily reflect the views of the Organization.

[1] Brazil is one exception in this last respect, as it has signed numerous bilateral and regional investment treaties and agreements, including in the context of the MERCOSUR, but none have yet been ratified by its Congress.

Several other attempts at crafting a global investment regime would prove stillborn, including most spectacularly the proposed Multilateral Agreement on Investment (MAI) initiative launched within the Organisation for Economic Co-operation and Development (OECD) in the late 1990s. The MAI represented a major attempt at crafting a multilateral (if far from universal) regime for investment.

Finally, and most recently, efforts to include investment negotiations proper within the negotiating purview of the WTO have proven deeply contentious, contributing significantly to the derailing of the December 2003 ministerial meeting in Cancun. As part of the price for imparting forward momentum to the stalled Doha Development Agenda, WTO members agreed in July 2004 that foreign investment would (alongside two other so-called "Singapore Issues", i.e., trade and competition, and transparency in government procurement) be taken off the WTO negotiating table for the duration of the current Doha Development Agenda.

Accordingly, in terms of legally-binding multilateral rules, what survives the multiple initiatives of the past half-century are the rules that were agreed upon in the Uruguay Round of trade negotiations, concluded in 1994. Of these, the most important elements are the Agreement on Trade-Related Investment Measures (TRIMs), the Agreement on Subsidies and Countervailing Measures (ASCM), the General Agreement on Trade in Services (GATS), the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPs), and the Dispute Settlement Understanding (DSU).

The WTO has produced a rich harvest of investment-related provisions. This may come as a surprise in light of the determined attempt of many GATT members to eschew a meaningful discussion of investment matters at the outset of the Uruguay Round. That the Marrakesh Agreement establishing the WTO contains so many investment-related provisions, most notably in the TRIMs Agreement and, particularly in GATS, must be ascribed to the rapidly changing policy environment within which the Uruguay Round took place.

This fertile environment, characterized by a number of far-reaching changes in policy and rule-making approaches which gained currency in a growing number of developed and developing countries, was one the multilateral trading system was able to internalize (if only partially) by the time the Uruguay Round was completed. Among such changes are: (i) a growing recognition of the increasingly complementary relationship between trade and investment in a globalizing world economy; (ii) heightened awareness, particularly among developing countries, of the policy signalling benefits to be derived by credible commitments in the areas of trade, investment, and intellectual property protection; (iii) a greater appreciation of the key contribution of investment as the principle means of securing market access and enhancing the contestability of markets; and (iv) a significant worldwide push towards investment regime liberalization, often pursued on a unilateral basis and closely tied to efforts aimed at regulatory reform in key sectors (including energy, telecommunications, finance and transportation services).

While the Uruguay Round has set an important precedent by laying down markers with which to develop more comprehensive rules on investment, the limitations of existing provisions must also be borne in mind. For one, the TRIMs Agreement remains extremely limited in scope and is largely attuned to the concerns of an era of policy-making characterized more by suspicion of, and need to control, foreign investment than by keenness to compete for and attract such investment. WTO rules on investment remain unbalanced given the asymmetry of disciplines applying to performance requirements, the incidence of which tends to fall primarily on developing countries, as opposed to weak disciplines governing the distortive practice of investment incentives, the incidence of which tends to be greater among developed countries.

Moreover, while the GATS negotiations have brought out quite vividly the central importance of investment to trade in services and generated far more by way of commercial presence commitments than had been expected, their treatment of investment-related matters is embodied in provisions that display a number of architectural shortcomings. The latter lack definitional clarity, do not generate adequate transparency; generate limited pressures for liberalization; and afford weak and only indirect protection to investors.

Much, therefore, remains to be done to equip the multilateral trading system with a comprehensive panoply of investment disciplines, and it comes as no surprise that attempts would be made in the post-Uruguay Round era to address such shortcomings. Yet, despite the continued improvements in host country investment climates and policy regimes, attempts at crafting a comprehensive set of multilateral disciplines on investment have met with very limited success.

# III
# Scope and content of bilateral and regional agreements

## 1. Bilateral investment treaties

Starting in the 1960s, bilateral investment treaties (BITs) have become the most common international instrument dealing with investment protection issues. The number of such treaties has grown manifold, a trend that now engulfs countries at all levels of development. The number of signed BITs stands at some 2,300, although a smaller number (estimated at around 1700) is actually in force. The network of BITs grew significantly throughout the 1970s, prompted in large measure by a defensive impulse on the part of home (i.e., capital-exporting) country governments in the wake of the increasing number of expropriations and nationalizations, including in Latin America.

The trend accelerated again in the 1990s, albeit in a markedly changed policy (and ideological) environment, as host country (i.e., capital-importing) governments in developing countries and transition countries sought to exploit the putative signalling properties of BITs. The period saw a significant increase in treaties linking a wide range of countries along South-North lines, as well as, more recently, along South-South lines.

BITs are designed to protect, promote and facilitate foreign investment, and they constitute to date the most widely used instrument for these purposes. BITs have traditionally been negotiated between developing countries seeking to attract international investment and developed countries as the principal homes to foreign investors.

The content of BITs has become increasingly standardized over the years and has largely influenced rule-making at the regional level, particularly during the last fifteen years, though, as a consequence of the growth in the sheer number of BITs, the formulation of individual provisions remains rather varied.

There are notable differences between the provisions of BITs signed some decades ago and the more recent ones. A typical treaty's main provisions deal with the scope and definition of foreign investment; admission of investments; national and most-favoured-nation treatment; fair and equitable treatment; guarantees and compensation in respect of expropriation; guarantees of free transfer of funds and repatriation of capital and profits; and dispute-settlement provisions, both State-to-State and investor-to-State. The acceptability of investor-State arbitration was significantly advanced by the conclusion in 1965 of the Washington Convention, overturning the practice of sovereign immunity long embedded in the Calvo doctrine.

As noted earlier, perhaps the most relevant new development in international practice of the last few years is the frequency with which developing countries and countries in transition are concluding agreements with each other. In content terms, it bears noting that South-South practice does not depart significantly from the content of BITs concluded along North-South lines.

BITs remain primarily, if not exclusively, investment protection instruments. Over the years there has not been any significant change from their original objectives. It is thus still true that "a striking feature of BITs is the multiplicity of provisions they contain that are specifically designed to protect foreign investments, and the absence of provisions specifically designed to ensure economic growth and development" (Zampetti and Fredriksson, 2003).

## 2. Investment rules in regional integration agreements

The universe of regional instruments on investment does not reach the magnitude of the BIT phenomenon, but is still vast, diverse and growing. As such, regional agreements have also begun to create an intricate web of overlapping commitments. While BITs have a distinct focus on investment protection, regional integration agreements (RIAs), and interregional ones, are often geared towards investment regime liberalization even though many of them also address investment protection issues. In the case of European Union RIAs the focus on liberalization is particularly pronounced, as core investment protection issues are not within European Union competence and are generally addressed in BITs concluded by individual member States.

At the regional level, only a few instruments are entirely devoted to investment, such as the Andean Community's Decision 291 (adopted in 1991). However,

a growing number of regional trade agreements have in recent years embedded what are often comprehensive disciplines on investment. The North American Free Trade Agreement (NAFTA) and MERCOSUR Protocols are examples of this trend, albeit less comprehensively and still subject to ratification shortcomings.

The general aim of these agreements is to create a more favourable investment climate through liberalization measures, with a view to increasing the flow of investment within or between regions. As a result, the commonality of substantive rules is much less marked than in the case of BITs.

Latin American countries have been among the most active in pursuing such regional trade agreements, which, since NAFTA, typically include investment rules geared towards the twin pursuits of investment protection and liberalization.

Until recently, the United States and the European Union represented the region's most important partners, as hubs. However, there is now growing interest in Asia. In 2004, Mexico concluded the first free trade agreement (FTA) between Japan and a Latin American country.[2] Chile and China have just completed talks on an FTA; Panama has entered into an agreement with Taiwan Province of China; and China, Japan and the Republic of Korea are actively considering new integration agreements or other means of enhanced economic cooperation, including in the investment field, with Latin American partners.

### 3. Bilateral and regional advances in investment rule-making

Prior to the 1990s, relatively few investment-related provisions appeared in RIAs. Most such provisions were intended to protect property and were found in BITs. Investment-related provisions now commonly appear in RIAs in every region of the world and especially in those involving Latin American countries. Prior to the 1990s, and unlike BITs, which had historically tended to associate countries at very different levels of development, such as advanced capital-exporting nations and poorer host countries, RIAs were negotiated principally among States within the same region and at similar stages of economic development. RIAs now commonly link States in different regions of the world and often seek to integrate economies at very different stages of development.

The number of RIAs with investment-related provisions has increased dramatically since the 1990s. Although interregional agreements are becoming more common, the majority of RIAs that have been concluded by States in the Americas are with other States in the region. A large number of those States are party to at least one RIA, typically modelled after NAFTA. The CARICOM States, however, have not generally concluded RIAs outside of CARICOM.

Many investment-related provisions in RIAs address the same issues as their counterpart provisions in BITs and relate to compensation for expropriation and guaranteeing freedom of transfers. Although investment protection provisions in RIAs are often similar to those found in BITs, there appears to be greater substantive variance in the content of provisions between RIAs. One explanation may be that most countries, such as the United States, use a model negotiating text for their BITs, which tends to create uniformity across bilateral treaties. The participation of a greater number of States in the negotiation of a number of plurilateral RIAs, and the need to accommodate differing levels of commitment towards investment liberalization, has tended to require greater flexibility and thus more creativity in the drafting of legal provisions.

It remains true, however, that RIAs have in large measure codified pre-existing BIT practice in respect of investment protection issues. This is true even though RIAs have most recently been used to correct some of the perceived shortcomings of traditional BIT provisions, notably regarding investor-State arbitration over matters of indirect expropriation. In so doing, RIAs can arguably be said to fulfil their role as laboratories for experimenting (notably in light of evolving jurisprudence) with a number of rule-making advances that have proved to be obstacles to previous attempts at crafting multilateral investment disciplines, notably under the proposed OECD multilateral agreement on investment. Such advances, and the testing grounds that RIAs afford them, could facilitate the future adoption of similar multilateral disciplines in a WTO context.

The commonly found provisions in RIAs that go beyond traditional BITs are those that prohibit anticompetitive business practices, protect intellectual property rights, liberalize admission procedures and

[2] See the "Agreement between Japan and the United Mexican States for the strengthening of the Economic Partnership". The purposes of the Agreement are to promote freer cross-border flow of goods, persons, services and capital between Japan and Mexico. It also aims to promote a comprehensive economic partnership, which includes competition, improvement of business environment and bilateral cooperation in such fields as vocational education and training and support for small and medium-sized enterprises.

open up trade and investment in services, including in the form of commercial presence, which is akin to FDI. As in the case of BITs, issues related to taxation and investment incentives are generally absent from RIAs.

RIAs in the Americas have been heavily influenced by NAFTA, which contains an investment chapter modelled after the provisions of the BITs of the United States, though more elaborate in some respects. The same can also be said of the Mexico-Japan Economic Partnership Agreement. European RIAs, including those with Latin American partners, are chiefly concerned with liberalization (post-agreement market access), limiting anticompetitive practices, and protecting intellectual property. The European approach leaves investment protection to BITs concluded by European Union member States. Accordingly, RIAs involving the European Union, including those agreed with Latin American countries, do not feature provisions on investor-State dispute settlement.

The fact that RIAs tend to contain greater variation in legal provisions than is the case of BITs does not mean that RIAs are necessarily weaker agreements. Indeed, RIAs demonstrate that it is possible to achieve high-standard agreements outside the context of a BIT. Though it remains true that the strongest agreements tend to be bilateral in nature (reflecting in many instances power asymmetries between signatories), RIAs binding on multiple States and providing for high standards of investment protection and liberalization have been successfully concluded.

RIAs also tend to feature a larger number of provisions that take account of the special circumstances of developing countries than is the case under BITs. This is to be expected to some extent, given that some RIAs have only developing countries as parties. Finally, and as noted above, whether limited to developing countries or including countries at different stages of economic development, RIAs appear to offer greater scope than BITs for experimenting with different approaches to promoting international investment flows.

# IV

## Main arguments in investment rule-making debates: Bilateral, regional or multilateral approaches

The advantages and disadvantages of international investment agreements differ depending on whether such agreements are bilateral, regional or multilateral in scope. Advantages and disadvantages can also be viewed from different perspectives, such as those of the host versus home countries, and specifically with regard to the issues covered, the inclusion of development-related provisions, impacts on the regulatory sovereignty of host States, the impact on FDI flows, and relative bargaining power.

One of the main reasons for the popularity of BITs is the fact that they provide flexibility to the host country, affording it the possibility of screening and channelling FDI (as admission is generally subject to the domestic laws of the host country), while at the same time extending the necessary protection to foreign investors. However, BITs often involve countries at different levels of development, with unequal bargaining power and negotiating capabilities. Furthermore, available empirical evidence does not suggest a significant impact of BITs on investment flows.

Finally, investor-to-State dispute settlement mechanisms, which complement investment protection provisions, may give rise to high costs and liabilities for developing countries in addition to raising potentially controversial issues relating to the right to regulate in the public interest. The recent spate of litigation involving Argentina is an obvious case in point, as is the more general trend of heightened judicial activity observed since the late 1990s under BIT and RIA treaties.

At the regional level, while investment protection issues are often addressed, international investment agreements tend to have a broader focus, which includes the liberalization of restrictions to entry and establishment of FDI, followed by the reduction of discriminatory operational (post-entry) restrictions.

These elements are generally part of wide-ranging agreements addressing a host of other policy areas, from trade liberalization for both goods and services to intellectual property protection. As such, regional integration agreements may provide signatories with more space for trade-offs. However, the broader focus of these agreements, coupled with recourse to investor-to-State dispute settlement mechanisms, means that, like BITs, they are hardly immune from potential public policy controversies relating to investor-State arbitration, as experience under NAFTA has shown, notably in respect of litigation relating to the alleged confiscatory effects (e.g. indirect expropriation) of environmental or health regulations.

Even to a larger extent than BITs, regional instruments use all the panoply of traditional international law tools, such as exceptions, reservations, transition periods and the like, to ensure flexibility in obligations so as to cater to the different needs and capacities of parties at different levels of development. From the perspective of developing countries this, together with the growing recognition of the links between trade and investment flows, may explain why investment rules are increasingly found in RIAs, which had initially been concerned primarily with trade issues.

As RIAs addressing investment issues and BITs have multiplied in number, they have also created an intricate web of overlapping commitments. This is one of the main arguments cited in favour of creating a common, multilaterally-agreed, framework for investment that, in the words of the WTO Doha Ministerial declaration, would "secure transparent, stable and predictable conditions for long-term cross-border investment, particularly foreign direct investment" (WTO, 2001).

Proponents of a unified WTO compact on investment have argued that a new multilateral framework of rules could ensure autonomous as well as bilaterally- and regionally-negotiated liberalization and extend the benefits of such openness on a most favoured nation (MFN) basis, preventing possible policy reversals where liberalization measures have yet to be consolidated.

The counter-argument that has been voiced recalls that a multilayered set of investment rules already exists under BITs and regional instruments, and also at the multilateral level, especially under the WTO Agreement on Trade-Related Investment Measures (the "TRIMs Agreement") and the General Agreement on Trade in Services (GATS).

Existing rules may be far from perfect, but it has generally proven difficult for the "friends" of investment at the WTO to advance proposals suggesting that a clearly superior set of rules could be agreed upon in a WTO framework. Furthermore, the complexity of overlapping investment rules and regulations will likely persist, unless BITs and investment rules in regional instruments are superseded by a multilateral agreement.

At the same time, it remains the case that in the current WTO system an imbalance exists between the treatment enjoyed by investors in service sectors, which is already covered to some extent by GATS rules, and treatment enjoyed by all other investors, to which only the TRIMs Agreement may be deemed to apply in a direct manner.

From a development perspective, the question of the appropriate rule-making 'level' —bilateral, regional or multilateral— cannot be separated from an examination of the actual or potential content of investment rules and commitments. All international investment agreements are instruments of cooperation between countries that are entered into voluntarily. Furthermore, like all treaties, international investment agreements as such are neutral instruments: what determines their impact on the development prospects or regulatory sovereignty of countries is their content, and so far the development-specific content of such agreements at all levels has been rather modest. There is, accordingly, considerable scope for increasing the attention paid to development issues in international rule-making on investment.

This is particularly true in light of the power and negotiating capacity asymmetries that typically characterize multi-issue negotiations where a single undertaking prevails at the end and where great care needs to be exercised in ensuring that the interests of developing countries are properly addressed or preserved.

At the same time, negotiations at the multilateral level offer developing countries greater leverage than do regional or bilateral negotiations, since they are able to advance common ideas on substantive issues of importance to them. Moreover, the multilateral level could allow all developing countries, if adequate capacity-building efforts were put in place, to meaningfully participate in the design of new rules, which are otherwise going to be increasingly shaped by a restricted number of key countries participating in bilateral or regional initiatives.

In this regard, it is important that all international investment agreements are shaped so as to allow enough policy autonomy and flexibility. More specifically, the legal obligations entered into should not unduly limit the sovereign right to regulate in the public interest.

RIAs (more than BITs) have in recent years gone some way towards clarifying (and generally circumscribing the scope of) a number of investment protection-related provisions that could be deemed to unduly impair the regulatory autonomy of host States.

The quest for policy autonomy on the part of developing countries extends beyond protection matters to issues of admission and treatment, including support (subsidies and incentives) for domestic industries and performance requirements. While there seems to be an unambiguous collective preference for regulatory inaction on the issue of investment-related subsidies (i.e. investment incentives), the question of discipline on performance requirements has revealed an interesting paradox. Though the latter featured prominently in the Uruguay Round's implementation debate (as did the widespread perception of the Round's inequitable treatment of developing countries), it has generated little resistance in the context of RIAs, the great majority of which proscribe a more exhaustive list of measures than that mentioned in the TRIMs Agreement.

# V

# Anatomy of failure: investment and the Doha development agenda

At the fourth WTO Ministerial Conference, held in Doha, Qatar, in November 2001, WTO members agreed to launch negotiations on foreign investment after the fifth session of the Ministerial Conference "on the basis of a decision to be taken, by explicit consensus, at that Session on modalities of negotiations" (WTO, 2001). The decision identified a number of subjects that would be the focus of further work in the Working Group on the Relationship between Trade and Investment (WGTI) until the fifth Ministerial Conference and defined certain basic considerations that would need to be taken into account in negotiations on the envisaged multilateral framework.

While the work of the WGTI is widely seen to have been highly pedagogical in character and resulted in an unprecedented level of technical assistance and capacity-building being directed towards the investment policy field, it also proved highly contentious. Indeed, of the four "Singapore Issues" discussed by WTO members since 1996 (investment, trade and competition, trade facilitation and transparency in government procurement), investment was the subject matter most centrally involved in derailing the September 2003 WTO Ministerial Meeting held in Cancun.

The impasse surrounding investment and its treatment in the WTO system was ultimately resolved by the WTO General Council's July 2004 decision to confine Singapore Issue discussions under the Doha Development Agenda (DDA) solely to the subject of trade facilitation. The most immediate fallout from the failed WTO initiative will be to shift the focus of key rule-making initiatives on investment back to the bilateral and regional levels. These will take the form of BITs or RIAs featuring the extensive array of investment protection and liberalization provisions reviewed in this paper. For countries in the Americas, this entails essentially bilateral agreements insofar as prospects for a hemispheric integration agreement, such as the proposed Free Trade Area of the Americas (FTAA), no longer seem to hold the promise they once did.

Progress on making investment rules may well be more feasible at the bilateral and regional levels. This is so for at least two important reasons: first, the fact that such negotiations, particularly bilateral ones, are characterized by significant asymmetries of economic and political power between capital-exporting and capital-importing countries. A second reason is that BITs and RIAs typically start with a blank page and do not confront the delicate task of reopening existing rules, commitments and the balance of concessions that would inevitably complicate any attempt at fitting new investment rules alongside existing ones in the WTO context.

Discussions on investment at the WTO have highlighted a strange paradox: fierce resistance at the multilateral level by a number of developing countries on a subject towards which their unilateral, bilateral or regional policy stances have been starkly different

(and considerably more accommodating). Indeed, the burgeoning network of treaties, principally at the bilateral level, reflects a growing willingness and ability on the part of developing countries to codify existing legal frameworks for international investment at the country level, in part because of the strongly unilateral character of recent liberalization decisions.

The failure of WTO members to reach agreement on negotiating modalities for investment under the DDA must be assessed against the backdrop of the value added, coherence and negotiating incentives implicit in the proposals of its WTO advocates as opposed to the respective merits of BITs and RIAs. To put it simply, what purpose should a multilateral set of investment rules serve? Should, and can, it aim to go beyond what already exists at the bilateral and regional levels? And is such a body of rules worth having (and "paying for" in negotiating terms) if its content proves to be less than a BIT or RIA, as seems most likely given the considerably greater economic and political diversity of WTO membership and the recent reassertion by many developing countries of the need for greater policy space?[3]

On all the above grounds, and as the July 2004 decision of the WTO General Council recently confirmed, what was on offer in the investment area oddly failed to garner widespread support among WTO members. Such a conclusion can be reached when one looks at DDA proposals on investment through the prism of the four core components of investment rule-making: (1) protection; (2) liberalization; (3) distortions; and (4) good governance.

### 1. Investment protection

The WTO is arguably not the optimal setting in which to tackle matters of investment protection. WTO members appear to concur with this viewpoint to the extent that the issue of investment protection has never been a core agenda item in WGTI discussions. One major reason for this is that one of the distinguishing features of BITs or RIAs featuring comprehensive investment disciplines (recourse to investor-State dispute settlement procedures, to which investors naturally attach considerable importance) is for all intents and purposes not conceivable in a WTO setting. Indeed, the precedent —both legal and, perhaps more importantly, political— that such an instrument would create would likely fuel strong demands for private party recourse to dispute settlement in areas outside of investment, such as the environment, labour and human rights. This is something the diverse and polarized WTO membership appears most unlikely to support.

### 2. Investment liberalization

The WTO is on decidedly firmer ground as regards the core investment liberalization agenda. However, here again, one needs to consider two important facts to which proponents of a WTO agreement appear to have paid insufficient attention. First is the fact that some two-thirds of aggregate annual FDI flows are today directed towards service industries. Second, and perhaps more important from the perspective of the value added of any new WTO investment rule-making initiative, is that some four fifths of impediments to cross-border FDI are also found in service industries.

The predominance of services as the principal locus of investment restrictions, and thus of investment regime liberalization, stands out vividly, with the share of non-conforming measures in services ranging from 76.9 percent in the case of Canada and the United States, to 81.6 per cent in the study's Latin American sample countries (Argentina, Bolivarian Republic of Venezuela, Brazil, Colombia, Chile and Mexico), with a high of 94.1 percent in the case of transition economies such as the Czech Republic, Hungary and Poland.

### 3. Investment distortions

As regards collective action responses to investment-distorting measures, which tend to affect FDI in manufacturing more than in services, it is important to distinguish three sub-categories of policy measures. A first category consists of performance requirements, for which a comprehensive ban already exists under the "TRIMs Agreement" and whose scope arguably exceeds the limited subset of measures depicted in the agreement's illustrative list of prohibited measures. The main challenge in a multilateral context would be to incorporate the "TRIMs Agreement" by reference in any new WTO investment instrument and to consider its possible extension to investment in services, something a number of RIAs have done. As noted earlier, given the salience of the TRIMs Agreement in

[3] As noted above, the quest for policy space in the investment field is itself paradoxical as it has arisen mostly in the context of WTO negotiations and against the backdrop of the implementation debate burden flowing from the Uruguay Round. Meanwhile, developing countries would appear to have been willingly ceding policy space under BITs (a growing number of which are concluded among themselves) and RIAs.

the contentious WTO debate over the implementation burdens flowing from Uruguay Round agreements, such expanded scope cannot be taken for granted, even as recent research has begun to document the prevalence of TRIM-like measures in services (Sauvé, Molinuevo and Tuerk, 2006).

A second core element of the distortion agenda relates to investment incentives, which have been in use increasingly in recent years in all regions of the world and now in a growing number of developing countries. However desirable, not least on equity and coherence grounds, the coverage of investment incentives —the granting of which are often closely related to the imposition of performance requirements— would likely prove daunting in a WTO context if one is to judge by past failures and the revealed policy preference of host country governments for legal inaction in this area.

What is more, the question arises of the most appropriate level at which to tackle such sources of distortions (such as regional or multilateral agreements), given the likely greater regional incidence of locational competition between host countries. There has indeed been intense competition among developed and developing countries (but significantly less so between the two groups) in trying to attract FDI by using investment incentives. Central governments —and subnational ones in federal countries— make great use of these instruments, particularly in developed countries.

A third cluster of distortion-related challenges relates not so much to investment measures but to trade policy measures, and involves a range of practices that distort investment decisions away from the equilibrium that would prevail in their absence. Perhaps the best example of such investment-related trade measures is the discriminatory, sector-specific rules of origin found in many free trade agreements. Many such rules targeted Japanese investors in the past, notably in the automobile sector, with significant trade- and investment-distorting consequences. Such measures are also prevalent in the textiles and clothing sector, and indeed in many host-country sectors fearful of delocalization and structural competitive weaknesses in domestic industries.[4]

### 4. Good governance

Of all the issues linked to what one might call the "good governance" agenda in the investment field, those relating to transparency are arguably the only ones that could reasonably easily be anchored within a WTO investment agreement. Here again, however, one would need to reflect on the implications for effectiveness and development of recourse to dispute settlement and the attendant threat of trade or investment sanctions as a means of enforcing such positive prescriptions.

For all other issues relating to good governance —spanning subjects as diverse as the fight against corruption, the promotion of home country measures, the advancement of corporate social responsibility, and best practices in investment promotion— legally binding and enforceable legal responses, a fortiori in the WTO, appear ill-suited to the task and unlikely to command much support from the investment community.

# VI
## Conclusion: advancing forward-looking scenarios on investment

The quest for a global, multilateral, WTO-anchored, agreement will nonetheless likely be kept in mind and influence the actions of those countries that continue to believe in the desirability of such a rule-making approach. Without prejudging what the future might hold, this paper concludes with a few possible forward-looking scenarios. As it happens, several of the policy interrogations that will determine the final shape and content of a possible future WTO multilateral framework on investment (MFI) are questions that WTO members can also reflect upon and address in the context of their ongoing BIT and, especially, ria negotiations.

Should WTO members one day decide to take up negotiations towards a comprehensive agreement on

[4] Other significant IRTMs include tariff peaks and tariff escalation, as well the anticompetitive practices made possible under national anti-dumping regimes.

investment, they would need to determine the scope of that agreement and to address a number of core components. The substantive scope consists of the disciplines of the agreement, including the definition of key terms such as investments and investors (that is, in which investments and investors would benefit from the agreement). Countries would need to assess the impact of these definitions on the provisions of the agreement and an eventual liberalization process. Should the definition of investment include FDI, portfolio investment, real estate and intangible assets? Should it be broad enough to allow for the inclusion of new forms of investment, while providing for the definition of what is not an investment (in order to exclude short-term capital flows)? Should it extend to the pre- and post-establishment phase of an investment or could disciplines follow a variable geometry approach, with a broader definition applying to investment protection matters and a more circumscribed definition (for instance, limited to FDI flows only) adopted for purposes of investment liberalization?

Should an eventual investment agreement also apply to commitments made under the GATS in regard to commercial presence and under the "TRIMs Agreement" in respect of performance requirements? While the definition of commercial presence under article XXVIII of GATS is narrower than that typically found in BITs or in RIAs featuring comprehensive investment disciplines, it does cover pre- and post-establishment investment issues.

Basic provisions on national treatment and MFN are another key element of any prospective multilateral agreement on investment. WTO members would need to decide whether to apply the MFN and national treatment provisions across the board to all members and sectors (subject to negative list reservations), or to adopt the GATS approach, that is, to have an all-encompassing MFN provision with temporary exemptions and a conditional national treatment and market access standard, which would apply only to sectors and sub-sectors in which members would voluntarily schedule commitments. The choice of negative or hybrid list approaches to liberalization can have far-reaching implications for future regulatory conduct and the attractiveness of investment rules for many developing-country governments.

WTO members would thus need to assess whether a WTO Agreement on Investment would include commitments to investment liberalization in both goods and services, raising complex questions of an architectural overhaul and the treatment of acquired rights (and the attendant balance of benefits) flowing from current agreements.

Another relevant question (including at the bilateral and regional level) is whether the liberalization commitments made by WTO members should reflect the regulatory status quo. Securing such an outcome would entail a potentially significant departure from a long-standing tradition in goods trade under the GATT (for tariff negotiations) that was extended to services under the GATS in the Uruguay Round, whereby countries have traditionally maintained (and exercised) the right to bind less than the status quo.

Any comprehensive investment agreement would also need to address the issue of performance requirements, resulting most likely in the incorporation by reference of disciplines found under the "TRIMs Agreement". The question of whether such disciplines should be extended to services would need to be addressed, and would no doubt prove contentious given the recent focus on preserving policy space and the fact that service industries are still nascent in many developing countries.

However desirable, not least on equity and coherence grounds, disciplines on the granting of investment incentives would likely prove more contentious in a WTO setting if one is to judge by past failures and revealed policy preferences in this area. As noted earlier, provisions on investment incentives could nonetheless address issues related to their scope, codification, and the prohibition of (or encouragement to refrain from) some types of incentives. The principles of transparency and non-discrimination (national treatment and MFN treatment) should ideally apply to such practices, though progress is likely to prove difficult for obvious political reasons in important host countries.

An alternative scenario would be to expand the current WTO investment framework without negotiating a comprehensive agreement on investment. Several options are possible in this regard. Given that the bulk of investment restrictions arise in service sectors, WTO members could focus on investment liberalization in the GATS and ensure that commitments reflect more closely the investment regime in place in each member country (that is, encourage or mandate the scheduling of status quo commitments for mode 3 trade).[5] The latter issue

[5] The WTO defines a number of modalities for the provision of services in international trade. These include *Mode 1*, cross-border trade, where the service provider crosses the border in order to

is one that WTO members could require or encourage their BIT or RIA partners to uphold in agreements where a GATS-like, hybrid, approach to scheduling is adopted. Recent examples include RIAs signed by Japan with a number of countries in south-east Asia.[6]

WTO members could also elect to develop complementary disciplines on investment in goods, to address the market access component of an investment agreement that is currently missing under existing WTO disciplines. This was essentially what proponents of investment in the Doha Round had been arguing for, with decidedly poor results. Such an approach would need to be complemented by efforts at extending to services the disciplines found under the "TRIMs Agreement", another arduous task given the prominence of the post-Uruguay Round "TRIMs Agreement" implementation debate in WTO. As well, more explicit multilateral disciplines on investment incentives promoting transparency (and possibly non-discrimination, including on a voluntary, but MFN, basis) could be added to the Agreement on Subsidies and Countervailing Measures and once more possibly extended, in whole or in part, to investment in services.

Another scenario would be for WTO members to negotiate a multilateral agreement on investment, which would be comprehensive in nature, covering both investment protection and liberalization, and whose benefits would either extend solely to signatories or be concluded and applied on an MFN basis once an acceptable critical mass of cross-border investment activity had been met (as is the case of the WTO Information Technology Agreement). The European Commission floated the idea of a plurilateral approach for a short while in December 2000, but there were generally few takers, as the establishment of new plurilateral disciplines under the WTO requires the explicit consensus of all member countries, a situation that never prevailed on the Singapore Issues in general and on investment matters in particular.

A final forward-looking scenario, which WTO members can also seek to pursue at the bilateral and regional levels, would involve a negotiating quid pro quo to be envisaged as linking the movement of capital (investment) to that of labour (people).

Such a factor-movement-based negotiating bargain would respond to a thematic area —the temporary mobility of skilled and semi-skilled workers— that is high on the list of export priorities of a large (and growing) number of developing countries. Worker remittances are, after FDI, the second largest source of external finance in developing countries, and such flows dwarf FDI in many of them, particularly poorer ones that tend to attract little by way of FDI inflows. Furthermore, a capital-labour quid pro quo would also address the paucity of qualified workers that is becoming acute in a number of ageing societies. This challenge is particularly important in the case of developed countries, given prevailing demographic trends.

There is little doubt that the politics of labour movement are harder to contend with than those relating to capital mobility, a reality that is equally prevalent in developing countries. Still, despite these challenges and the genuine public policy concerns they give rise to, scope exists for countries to explore in an imaginative way the factor mobility linkages that could be exploited in RIAs (today) and the WTO (tomorrow).

For this to occur, WTO members could mould their RIAs on the tripartite architecture first used in NAFTA and found in a number of subsequent RIAs (particularly prominent in Latin America) that feature a complementary set of disciplines on: (i) cross-border trade in services (modes 1 and 2 of GATS); (ii) generic (horizontal) disciplines on investment applicable to goods and services in an undifferentiated manner; and (iii) generic disciplines on the temporary entry of business people.

Pursuing a capital-labour mobility agenda is arguably easier to contemplate at the bilateral and regional level than in a WTO setting, as negotiators in Geneva would inevitably need to contend with fitting any new investment disciplines into existing agreements, reopen the delicate balance of concessions embedded in them and possibly review the architecture of the WTO family of agreements. This is most clearly the case of the GATS, whose scope would need to be reduced to dealing exclusively with cross-border trade in services (modes 1 and 2) in order for new horizontal agreements to be pursued in the areas of investment (in goods and services) and the movement of people (across all sectors).

provide it. In *Mode 2* it is the service consumer who crosses the border. *Mode 3* involves a permanent commercial presence of the service supplier by means of an investment, and *Mode 4* involves transitory migration by natural persons working in a service enterprise in one country in order to provide the service in another.

[6] Recent Japanese FTAs feature a dual innovation: (i) an obligation to bind the regulatory status quo in investment commitments while keeping with a GATS-type voluntary approach to scheduling sectors in which commitments are made; and (ii) the publication for transparency purposes of non-binding lists of non-conforming measures affecting trade and investment in services.

As this paper has tried to show, the reasons for the current impasse on investment at the WTO are numerous. They involve a complex interplay of procedural, tactical and substantive concerns and involve a paradoxical quest for policy space in multilateral discussions at the same time that such space continues to be ceded in the context of unilateral, bilateral or regional policy initiatives.

That impasse provides a good opportunity for a thorough and much-needed rethinking of the objectives that negotiations on investment should pursue, including, at the regional and bilateral levels, the value added that any renewed attempt at placing investment on the WTO agenda can hope to achieve, and the parameters within which such discussions should be conducted if they are to balance the interests of home and host countries alike.

*(Original: English)*

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