International Negotiations on Investment Liberalisation

SPEAKING NOTES

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Some Broad Underpinning Factors

- To set the scene, so-to-speak, I would like to outline several broad factors underpinning the environment for international negotiations on investment liberalisation.
- *First*, I think there probably is almost universal agreement that foreign direct investment, like trade, is an engine of economic growth, employment and rising living standards, in both developed and developing countries.
  - Increased foreign direct investment flows have been an important factor for the increase in living standards since the Second World War.
- *Secondly*, it is a fact of life that all countries have restrictions on foreign direct investment, with varying degrees of openness and transparency.
  - While there are many factors that influence cross-border investment, it is clear that a transparent and stable foreign investment policy is a positive force for attracting investment.
- The *third* underpinning factor I would like to mention is that international negotiations on investment liberalisation have been going on for some decades.
  - Moreover, those negotiations have in fact produced a multitude of agreements that are designed to facilitate foreign investment.
    - Some also actually impose disciplines on countries in relation to their foreign investment policies.

Existing Agreements

- These agreements apply to both bilateral relationships and regional groupings, as well as through international organisations.
  - The nature of the disciplines contained in these agreements varies enormously: from aspirational and voluntary out to specific obligations prohibiting measures that would tighten a policy restriction and obligations for liberalisation.
  - I will mention just a few, but with an Australian focus.
- Around the world there is a large bowl of spaghetti of *bilateral investment agreements.* Australia has signed bilateral investment promotion and protection agreements (IPPAs) with over 20 countries and is currently negotiating further agreements with several additional countries.
  - These agreements, based on a model IPPA, essentially have the basic objective of promoting investment flows, rather than actually being mechanisms for investment liberalisation.
- A key *regional agreement* involving Australia is the APEC agreement reached in Bogor in 1994, under which industrial economies are to achieve the goal of free and open trade and investment no later than 2010, and the developing economies no later than 2020.
  - While there perhaps is some degree of 'softness' about this objective, in terms of what actually is the definition of 'free and open trade and investment', it nevertheless clearly represents a significant example of international negotiations (and commitments) for investment liberalisation.
  - Achieving the Bogor declaration is being pursued through Individual Action Plans and peer reviews in APEC's Investment Experts Group.
- For quite some years, *OECD member countries* have had agreements that impose disciplines on their foreign investment policies. I will briefly outline three.
  - First, the *Code of Liberalisation of Capital Movements and the Code of Liberalisation of Current Invisible Operations* constitute legally binding rules, stipulating progressive, non-discriminatory liberalisation of capital movements, the right of establishment and current invisible transactions (mostly services). All non-conforming measures must be listed in country reservations against the Codes. The Codes are implemented through policy reviews and country examinations, relying on 'peer pressure' to encourage unilateral rather than negotiated liberalisation.

- The Codes were initially adopted in 1961 but have since been revised and expanded in scope. Important recent additions were the right of establishment (1986) and cross-border financial services (1992). New work to promote liberalisation of insurance services and professional services has been launched. For most member countries, remaining reservations against the Code obligations relate to foreign direct investment, the purchase of real estate by non-residents and the prohibitions of certain types of securities operations.

– Secondly, there is the 1976 *Declaration by the Governments of the OECD member countries on International Investment of Multinational Enterprises*. This Declaration constitutes an aspirational objective of improving the investment climate and encouraging the positive contribution multinational enterprises can make to economic and social progress.

  - All 30 OECD member countries, and seven non-member countries (Argentina, Brazil, Chile, Estonia, Israel, Lithuania and Slovenia) have subscribed to the Declaration.

– Thirdly, there is the Convention on Combating Bribery of Foreign Officials in International Business Transactions. Under this convention it is a crime to offer or give a bribe to a foreign public official in order to obtain or retain international business deals.

  - A related text effectively puts an end to the practice according tax deductibility for bribe payments made to foreign officials.
  - The Convention has been signed by all OECD members and by several non-members.

- Between 1995 and 1998 OECD members and several non-OECD participants met to negotiate a *multilateral agreement on investment*, the so-called MAI, with the objective of providing a transparent, effective and comprehensive framework for international investment.

  – These negotiations which were launched in May 1995 collapsed in late-1998.

  – The MAI negotiations involved a very ambitious and complex set of proposals.

    - No presentation on international negotiations on investment liberalisation would be complete without some reference to the MAI;
    - and I propose to talk more about it shortly.

WTO: Doha Declaration

- Action on international negotiations on investment liberalisation more recently has been moved noticeably away from the OECD to the WTO.
  - As all here today would know, the WTO's Doha Declaration in November 2001 launching a new round of trade negotiations, included a section on 'trade and investment'.
    - This is a rather tortuously-worded and carefully constrained agreement for work on investment to continue in the Working Group on the Relationship Between Trade and Investment, as input into the objective of including to some extent investment in the new trade round.
    - The cautious nature of this formulation is not surprising, given the history of international negotiations on investment liberalisation, especially the MAI.
    - An important point to note here is the fact that increasing the number and diversity of countries involved from the 30 or so in the OECD sponsored negotiations to a much larger and more diverse WTO based participation of well over 100, increases significantly the complexity and difficulty of the negotiations.
- While I have no involvement in the work of the WTO's Working Group on the Relationship Between Trade and Investment, it seems to me that there is little if not no chance whatsoever of the WTO forum reaching agreement on an international framework for investment that would be any where near the ambitious shape of that proposed for the now-defunct OECD's MAI.
  - I hasten to add, that I suspect that there would be very few indeed who would in fact have that aspiration.

Basic Characteristics

- A key objective of all international agreements on investment is to ensure that the actual policy restrictions being applied are clearly known ie, the *transparency* objective.
- Other standard and important components include:
  - *'most favoured nation'* application ie, treating all foreigners the same;
  - undertakings about *expropriation/nationalisation* (including the nature of compensation);'
  - *dispute resolution mechanisms*;

- *standstill* obligations ie, a listing of those restrictions that will not be made more restrictive in the future; and sometimes
- *rollback* obligations ie, undertakings to actually liberalise existing restrictions in the future.

MAI

- This now brings me back to the OECD's MAI, the objective of which was to achieve a comprehensive multilateral framework for investment, with high standards of liberalisation and investment protection, with effective dispute settlement procedures, which would be open also to non-members.
  - The MAI story is a very complex one. It is also one that contains valuable lessons for international negotiations on investment liberalisation.
  - In outlining today the MAI experiences, I should caution that I will be running the risk of over-simplifying events, in addition to committing 'sins of omission'.
- In the lead-up to the launch of the negotiations by the OECD, Australia was in the small group of countries a little reluctant to join this consensus.
  - This did not reflect any 'in principle' objection.
  - Rather, there was a concern that there had been insufficient preparatory work on key issues to move to actual negotiations for an international agreement with treaty status.
- The MAI had its origins mainly in the perceived need not only to collate into a single agreement the range of existing agreements, but also to widen the scope of international obligations in relation to foreign investment.
  - Many were of the view that reaching agreement within the OECD membership on a high quality and comprehensive agreement was achievable, given the existing commitments and the reasonable homogeneity of the membership in relation to their attitude to foreign investment.
  - However, a cynic might also suspect that the MAI's origins were also in part sourced to the objective of some for the OECD to carve out a bigger international role.
- A key if not crucial characteristic of the MAI was that it was to have a 'tops down approach'.
  - In brief terms, this very ambitious approach meant that everything was to be covered, unless specifically excluded and that full 'national treatment' would

be given to foreign investors in all cases (ie, with no discrimination against foreigners) unless specifically exempted.

- Over the three years of negotiation a text of sorts with this scope emerged.
  - However, as you would expect, many parts had two or more variations, offered up by different countries.
    - Hence, a document with 145 pages.
- It was this document that generated significant concerns. There were strong objections and criticisms, along the lines that the proposed obligations represented fundamental and extensive erosion of national sovereignty.
  - And, in addition, there was the criticism that this proposed erosion had not been subjected to sufficient parliamentary and public scrutiny.
- The ensuing debate on this aspect of the MAI tended to overlook the so called 'other half' of the proposed treaty's documentation, namely, the reservations each proposed signatory would/could take out against various obligations of the 'first half' of the MAI.
  - In fact, the aggregate country reservations on the table at the time of the demise of the negotiations, though still incomplete, were much greater than the actual text of the obligations themselves.
- Australia's approach to the MAI negotiations included the position that a reservation would be lodged against any obligation of the proposed treaty that conflicted with Australia's then applying foreign investment policy.
  - Australia's draft proposed reservations were published.
  - However, these reservations, as was the case for the reservations proposed by many others, had yet to be subjected to examination by others.
    - I suspect that at least some reservations for all countries in the negotiations would have been subjected to a challenge of sorts.

Environment Protection and Labour Standards

- From an early date in the negotiations, several became strong proponents of including provisions in relation to the protection of environment and labour standards.
  - These essentially were encompassed by a proposed obligation along the lines that precluded encouraging investment by lowering environment protection and labour standards.

- As is well known, including these types of obligations was being pushed very hard by a range of non-government organisations and some political parties in some countries.
    - Many NGO proponents felt that, in circumstances of governments sacrificing some sovereignty to give more certainty to multinational corporations, there also needed to be obligations that constrained behaviour that could damage environment protection and labour standards.
- As you would appreciate, these proposals generated very frank debate within the negotiations, not only about how to fill in the detail to make them deliverable, but also as to whether to have them at all.

- This issue, ie the possible inclusion of obligations in relation to environmental and labour standards, inevitably will loom large in any international negotiation on investment liberalisation, in the future.
    - It will be very difficult for agreement to be reached.

Dispute Settlement

- The proposed MAI provisions in relation to *dispute settlement* were also far from agreed at the time negotiations collapsed.
- Some were pushing for a significantly enhanced system, relative to current arrangements.
    - For example, there were proposals for international expert tribunals and for State-investor disputes, as well as State-State disputes, to be covered.
- Those supporting enhancement probably had an eye to needing to protect investments by their residents in developing countries with less than robust legal systems.
- Those reluctant about enhancement were probably concerned about the erosion of their own sovereignty and in any case tended to put weight on the point that the vast bulk of foreign investment flows were from and to the developed (OECD) economies that have sufficiently robust legal systems and accountable foreign investment policies that do not need supplementation in relation to dispute settlement.

Two Australian Issues

- Naturally, all of the issues I have mentioned so far were also issues for Australia.

  - However, there are two others that I would also like to flag, while not unique to Australia, were of particular interest to us.
- Members of the European Union were particularly keen to ensure that the MAI obligations applied to *all levels of government*.
  - They were particularly concerned about the range of restrictions that impacted discriminately on foreign investors that the 50 state governments in the US had.
- Australia, as a Federation, was caught up in this push (as were some others eg, Canada).
- This means that Australia, when participating in future international negotiations on investment liberalisation, will surely need to liaise closely with the State and Territory Governments.
  - The existing Treaty making processes, which include State and Territory consultation, actually provide a mechanism to cover 'all levels of government'.
- The second Australia-specific issue I would like to mention is in relation to the *screening system* that underpins Australia's foreign investment policy.
  - Under the screening system, certain categories of investment are subject to the 'contrary to the national interest' test.
  - This test, with the onus on the government to find a reason to reject a proposal, has a discretionary element to it.
- This discretionary aspect has been criticised by others in the past. They would like it removed.
  - It is likely that this will be the case in future international negotiations on investment liberalisation.
- Australia also had a concern in the MAI negotiations that the proposal to apply the dispute resolution processes to the pre-establishment stage would mean that decisions under the screening system would be subject to challenge.
- In this regard, I mention as a footnote that, at the time the MAI negotiations were launched, Australia in fact had noted that what some countries seemed to have in mind for the Agreement could cause difficulty for Australia in regard to binding of State Governments and the removal of foreign investment screening processes.

Reasons for MAI Failure

- The reasons for the MAI negotiations to break down were complex, various and inter-related. If I had to make a list, I would probably include the following, some of which I have alluded to already:
  - Insufficient preparatory work on some key issues prior to moving to actual negotiations;
  - an overly-ambitious coverage for the agreement;
  - deficient communication to others by OECD member countries and the OECD as to the nature and shape of the proposed agreement, that is, that it contained not only obligations, but also scope for country reservations;
  - deficient consultation processes more generally with interested parties by the OECD member countries and the OECD;
  - to some extent, some misrepresentation of the proposed MAI in the international debate by some interested parties;
  - some possible disconnections between some negotiators and their home authorities (with the tendency for some to possibly push proposals in advance of obtaining Ministerial endorsement);
  - declining interest from the international business sector when the perception developed that the MAI was more about codifying existing systems of foreign investment policy and less about actually achieving liberalisation; and
  - an erosion to some extent of the initial positive negotiating environment.
- I think it reasonable to conclude that a listing of this kind would contain some useful lessons in relation to the undertaking of future negotiations on investment rules.

Conclusion

- I hope I have given you some sort of feel for the issues confronting international negotiations for investment liberalisation.
- I would be pleased to respond to questions.