



**United Nations
Conference
on Trade and
Development**

Distr.
GENERAL

TD/B/COM.2/48
TD/B/COM.2/EM.12/3
4 December 2002

Original: ENGLISH

TRADE AND DEVELOPMENT BOARD
Commission on Investment, Technology and
Related Financial Issues
Expert Meeting on the Development Dimension of FDI:
Policies to Enhance the Role of FDI in Support of
the Competitiveness of the Enterprise Sector and
the Economic Performance of Host Economies,
Taking into Account the Trade/Investment Interface,
in the National and International Context
Geneva, 6–8 November 2002

**REPORT OF THE EXPERT MEETING ON THE DEVELOPMENT DIMENSION OF
FDI: POLICIES TO ENHANCE THE ROLE OF FDI IN SUPPORT OF THE
COMPETITIVENESS OF THE ENTERPRISE SECTOR AND THE ECONOMIC
PERFORMANCE OF HOST ECONOMIES, TAKING INTO ACCOUNT THE
TRADE/INVESTMENT INTERFACE, IN THE NATIONAL AND INTERNATIONAL
CONTEXT**

Held at the Palais des Nations, Geneva
from 6 to 8 November 2002

CONTENTS

<i>Chapter</i>	<i>Page</i>
I. Chairperson's summary.....	2
II. Organizational matters.....	8
<i>Annex</i>	
Attendance	10

Chapter I

CHAIRPERSON'S SUMMARY

1. In accordance with the agenda of the meeting, the discussions focused on three main areas: the role of host country policy measures; the role of home country measures; and the right to regulate and safeguards.

2. Experts noted that inflows of foreign direct investment (FDI) could bring important benefits to the recipient economies in the form of capital inflows, technology spillovers, human capital formation, international trade integration, enhancement of enterprise development and good governance. However, it was also noted that such benefits were not automatic. In addition, some experts observed that FDI could have negative effects in such areas as market structure and balance of payments, and could lead to crowding out of domestic enterprises, as well as other social impacts. Government policies were therefore needed to enhance benefits and minimize negative effects.

3. When considering what host country policies could effectively help developing countries and economies in transition to attract FDI and benefit from it, experts noted that a wide range of host country policy measures were implemented, for example to:

- Create a sound and stable macroeconomic and political environment, including a transparent and predictable business environment;
- Develop physical and technical infrastructure, and promote clusters;
- Develop human resources;
- Develop domestic enterprise capabilities (notably small and medium-sized enterprises);
- Address environmental and social concerns;
- Adopt competition laws and reduce restrictive business practices;
- Influence the behaviour of investors by offering investment incentives and by imposing performance requirements (often in combination);
- Create larger markets through regional and bilateral cooperation;
- Protect investment, including intellectual property rights.

4. Experts noted that the policy mix had to be adapted to the special circumstances prevailing in different countries and might have to evolve over time. Factors influencing this mix were level of development, market size, domestic capabilities and existing levels of FDI. Globalization offered better opportunities for small economies to compete for export-oriented FDI, but it also implied more competition between countries. Thus, it was becoming increasingly important for countries to consider what the best policy approach was for attracting and benefiting from FDI in accordance with their development objectives. Even at an early stage of their development, countries needed to attach importance not just to the size of FDI, but also to its qualitative aspects.

5. Specifically with regard to incentives, experts noted that they were widely used and were often necessary for attracting FDI and achieving development objectives. Some experts suggested that incentives might be useful for attracting a critical mass of FDI, with possible agglomeration effects. However, views on the effectiveness of incentives varied. Countries needed to take the benefits and costs of incentives carefully into account. In particular, it was stressed that in order to benefit from FDI attracted in part by the provision of investment incentives, host countries needed to pay attention to the strengthening of domestic capabilities. Without a minimum level of absorptive capacity in host countries, the scope for positive externalities and linkages to domestic enterprises was limited. In this context, some experts made the point that countries might consider offering investment incentives in a non-discriminatory way, without distinguishing between foreign and local companies, and making incentives part of the overall industrial policy.

6. On the issue of performance requirements there was a divergence of views about the effectiveness of these measures. It was noted that almost all countries – both developed and developing countries – had had recourse to such requirements at some stage of their development. Specific objectives mentioned for the use of performance requirements included:

- Deepening and broadening of the industrial base;
- Generation of employment opportunities;
- Linkage promotion;
- Export generation and performance;
- Trade balancing;
- Regional development promotion;
- Technology transfer;
- Avoidance of restrictive business practices;
- Various non-economic objectives, such as political independence and distribution of political power.

7. In general, performance requirements were often used to address market or policy failures. Some experts stressed the importance of information asymmetry as an argument to justify the use of such requirements. Others expressed the strong view that the determination of development priorities should be left to host countries, which should therefore have the right to impose performance requirements in order to achieve their development objectives. Some experts noted that while there might be a role for performance requirements in the context of attracting and benefiting from FDI, the implementation and monitoring of them might entail costs and require major efforts to gather relevant information as well as to clearly define the key objectives of the measures. Some expressed the view that countries imposing too stringent performance requirements might reduce the opportunities to link up with the international production networks of transnational corporations (TNCs).

8. The use of some performance requirements had been disciplined by the World Trade Organization's Agreement on Trade-Related Investment Measures. As to whether countries

could benefit from making the use of performance requirements more restrictive or less restrictive, experts were unable to reach a consensus. Some experts were of the opinion that it should be left to each Government – as an expression of Governments’ right to regulate – to decide whether it wanted to use performance requirements, whereas others argued that further international disciplining would be in the interest of all countries.

9. The incidence of performance requirements in both developed and developing countries had declined over time for various reasons. It was noted by some experts that the policy mix had changed and that Governments, particularly in developed countries, were relying increasingly on other measures, such as anti-dumping and countervailing measures and strategic trade and investment policies, to achieve similar objectives. Some experts suggested that this policy change might warrant further attention.

10. On the issue of home country measures (HCMs), experts noted that this was an often overlooked aspect of FDI’s triangular relationship, which involved TNCs, host countries and home countries. Nonetheless, HCMs could play an important role in influencing the direction, magnitude and quality of FDI flowing to developing countries, as well as the benefits that could be derived from such investment. HCMs undertaken were typically voluntary in nature and were not bound by international agreements. There were important exceptions, however, and special reference was made to the Agreement on the Trade-Related Aspects of Intellectual Property Rights, the Lomé Conventions and the Cotonou Agreement.

11. Experts noted that HCMs were used primarily by developed countries, but more recently, also by some developing countries. Reflecting their objectives, HCMs could be classified into different categories:

- Policy declarations;
- Information and contact facilitation;
- Technology transfer measures;
- Financial and fiscal incentives;
- Investment insurance;
- Market access regulations;
- Development of infrastructure and judicial frameworks.

12. There was no consensus among experts with regard to the effectiveness and efficiency of the various measures. Several experts remarked that there was a need for careful assessment in this regard. More analysis of how HCMs at the national, regional and multilateral levels complemented or disrupted one another was called for. Some experts stressed that HCMs were generally undertaken not only with the interest of host countries in mind, but also with a view to supporting home countries’ own interests. This might constitute a problem as regards maximizing the development benefits for host countries.

13. It was suggested that greater attention to the role of HCMs might be appropriate in future investment agreements. Exploring ways to introduce greater consideration of developing country interests in the design and implementation of relevant HCMs could also

be a beneficial avenue to consider for enhancing the developmental dimension of FDI. Finally, several experts observed that it was important to take into account the interlinkages between official development assistance (ODA) and FDI. For example, ODA played an important role in financing investment (e.g. in infrastructure and human resource development) that might be needed in order to create an environment conducive to FDI, but it might be difficult to raise private capital for that.

14. In the context of the balance between investors' rights and obligations in international investment, experts recognized that there were many different ways to address issues related to corporate social responsibility (CSR). A key distinction could be made between binding rules and voluntary codes, and another could be made between initiatives at the national and international levels respectively. The issue of linkages between CSR initiatives and the trade and investment system could be further analysed.

15. At the international level, a large number of initiatives had already been agreed upon. Some were universal in nature and applied to all firms (such as the International Labour Organization's Tripartite Declaration and the Guidelines for Multinational Enterprises issued by the Organisation for Economic Co-operation and Development), whereas others related to specific industries or activities. In addition, many large companies had established internal rules and codes of conduct in this area.

16. Views diverged with regard to what kind of approach was most effective for ensuring that CSR issues were adequately addressed in the context of FDI. Some experts favoured binding rules rather than self-regulation and voluntary codes as a means of minimizing the risk of a "race to the bottom" in the area of environmental and social standards, and because of the generally weak enforcement in host countries. Other experts argued that legally binding rules tended to be agreed upon at a lower common level of standards and might infringe the sovereign right of countries to regulate in their own interest. Some experts perceived the risk that CSR commitments might adversely affect the ability of developing countries to exploit their comparative advantages. Also, experts discussed the potential liability of parent companies for the actions of their affiliates. Procedural difficulties were also raised in this context.

17. The challenge was to balance the promotion and protection of liberalized market conditions for investors with Governments' need to pursue development policies. Social responsibility standards must be applied with sensitivity to the realities of local conditions in developing countries and should not be used for protectionist purposes. It was also important that corporations operate in a regulatory framework – at the national and international levels – that was conducive to sustainable development and that did not provide incentives for mismanagement of the environment or social abuse.

18. It was suggested by some experts that standards for corporate responsibility should go beyond environmental and social protection and include such considerations as transfer of technology, linkages with domestic enterprises, human resources development, export promotion, consumer protection, and accounting and reporting standards.

19. On the right to regulate, the Meeting reviewed different concepts and interpretations in the context of liberalization and globalization. Experts recognized that international agreements might limit the sovereign autonomy of the parties. Some of these limitations might affect the ability of government to use regulation, including economic, social, environmental and administrative regulation. The tension between the need for Governments to regulate and existing international obligations was central to the question of preserving the national policy space for Governments to pursue their development objectives.

20. Experts reviewed the various ways in which the issue of the right to regulate had been addressed so far both in the trade area (especially in agreements such as the General Agreement on Tariffs and Trade (GATT), the General Agreement on Trade in Services (GATS), the Agreement on the Application of Sanitary and Phytosanitary Measures (SPS) and the Agreement on Technical Barriers to Trade (TBT)) and in the investment context, particularly in bilateral investment treaties and in regional agreements such as the North American Free Trade Agreement (NAFTA). Experts agreed that in view of the difference between the impact of investment and that of trade, it was not always possible to transpose concepts and provisions that had been developed in the area of trade to the broader area of investment. In particular, the determination of development priorities should be left to host countries themselves, and the right balance should be struck between protection of investors and promotion of development. Standards for treatment of investors should be applied in such a way as to provide enough policy space for host Governments. In this regard, some experts recommended that consideration be given to the application of exceptions to take into account development concerns and to the adoption of safeguards in case of injury to the domestic enterprise sector (e.g. crowding out, balance-of-payments considerations and modifications of concessions). Some experts also suggested that the right to regulate be applied to the definition of investment by leaving out portfolio investment and to the conditions for entry and operation.

21. Experts also devoted attention to the issue of expropriation and regulatory takings. They recognized that expropriation provisions were essential to many investment treaties that aimed at protection of investment rather than liberalization of investment flows. Formulations in recent agreements covered not only direct takings but also anything tantamount to a taking, and entailed a requirement for full compensation. Experts also discussed issues related to litigation cases concerning this matter. Questions arose as to whether regulatory taking to protect the environment or other areas such as health, morals or human rights would also be subject to the payment of compensation. Some experts did not consider the concept or recent practice with respect to expropriation standards to be problematic.

22. Experts reviewed in some detail how the GATS dealt with the right to regulate, in particular by devoting attention to the interface between market access and national treatment commitments and the operation of Article VI on domestic regulation. Many service sectors were highly regulated in order to protect consumers and the environment; in the financial services sector, this regulation was to ensure a country's financial stability. Governments were cautious when agreeing to make themselves subject to common rules. Such caution was reflected in the provisions of the GATS, which upheld the fundamental right of a

Government to regulate in order to pursue national policy objectives. Experts noted therefore that the experience of the GATS, in particular with regard to the commercial presence mode of service supply, which was akin in many respects to FDI, could provide a valuable insight into how to design workable provisions to safeguard the right to regulate in the context of investment agreements.

Chapter II

ORGANIZATIONAL MATTERS

A. Convening of the Expert Meeting

23. The Expert Meeting on the Development Dimension of FDI: Policies to Enhance the Role of FDI in Support of the Competitiveness of the Enterprise Sector and the Economic Performance of Host Economies, Taking into Account the Trade/Investment Interface, in the National and International Context was held at the Palais des Nations, Geneva, from 6 to 8 November 2002.

B. Election of officers

(Agenda item 1)

24. At its opening meeting, the Expert Meeting elected the following officers to serve on its bureau:

Chairperson: Mr. Jukka Nystén (Finland)

Vice-Chairperson-cum-Rapporteur: Mrs. Pramila Raghavendran (India)

C. Adoption of the agenda

(Agenda item 2)

25. At the same meeting, the Expert Meeting adopted the provisional agenda circulated in document TD/B/COM.2/EM.12/1. The agenda for the Meeting was thus as follows:

1. Election of officers
2. Adoption of the agenda
3. The development dimension of FDI: Policies to enhance the role of FDI in support of the competitiveness of the enterprise sector and the economic performance of host economies, taking into account the trade/investment interface, in the national and international context
4. Adoption of the report of the Meeting

D. Documentation

26. For its consideration of the substantive agenda item, the Expert Meeting had before it a note by the UNCTAD secretariat entitled “The development dimension of foreign direct investment: Policies to enhance the role of FDI, in the national and international context – Policy issues to consider” (TD/B/COM.2/EM.12/2).

E. Adoption of the report of the Meeting

(Agenda item 4)

27. At its closing meeting, the Expert Meeting authorized the Rapporteur to prepare the final report of the Meeting under the authority of the Chairperson.

Annex

ATTENDANCE *

1. Experts from the following States members of UNCTAD attended the Meeting:

Angola	Iran (Islamic Republic of)
Austria	Italy
Bangladesh	Jamaica
Benin	Japan
Bosnia and Herzegovina	Jordan
Brazil	Kenya
Brunei Darussalam	Latvia
Burkina Faso	Lesotho
Burundi	Lithuania
Canada	Madagascar
Chad	Malaysia
China	Mauritania
Colombia	Mauritius
Comoros	Mexico
Congo	Mongolia
Cuba	Morocco
Czech Republic	Mozambique
Democratic People's Republic of Korea	Netherlands
Democratic Republic of the Congo	Nicaragua
Ecuador	Niger
Egypt	Oman
Equatorial Guinea	Pakistan
Estonia	Papua New Guinea
Ethiopia	Peru
Finland	Philippines
France	Russian Federation
Gabon	Solomon Islands
Georgia	Saudi Arabia
Germany	Senegal
Grenada	Slovakia
Guinea	Sri Lanka
Guinea-Bissau	Sweden
India	Switzerland
	Syrian Arab Republic

* For the list of participants, see TD/B/COM.2/EM.12/INF.1.

Thailand	and Northern Ireland
Tonga	United Republic of Tanzania
Tunisia	United States of America
Turkey	Zimbabwe
United Kingdom of Great Britain	

2. The following intergovernmental organizations were represented at the Meeting:

Common Market for Eastern and Southern Africa
European Community
European Free Trade Association
Organisation for Economic Co-operation and Development

3. The following specialized agencies and related organization were represented at the Meeting:

International Labour Organization
United Nations Industrial Development Organization
World Trade Organization

4. The following non-governmental organizations were represented at the Meeting:

General Category

Center for International Environmental Law
International Centre for Trade and Sustainable Development
International Confederation of Free Trade Unions
Oxfam International
South Centre

5. The following panellists/resource persons attended the Meeting:

Mr. Kwasi Abeasi, Chief Executive, Investment Promotion Centre, Ghana
Prof. Vudayagi Balasubramanyam, Lancaster University, United Kingdom
Dr. Sanoussi Bilal, European Centre for Development Policy Management
Mr. Hugo Cayrús Maurín, Minister Counsellor, Permanent Mission of Uruguay to the WTO, Geneva
Prof. Argyrios A. Fatouros, Consultant, Greece
Mr. Danny Graymore, Global Advocacy Christian Aid, United Kingdom
Prof. Yao Su Hu, Academic Vice-President, HK Shue Yan College, Braemar Hill, Hong Kong (China)
Mr. Robert Jacobson, Unilever, Netherlands
Prof. John Kline, Georgetown University, Washington, DC

Prof. Ari Kokko, Stockholm School of Economics

Dr. Nagesh Kumar, Research and Information System for the Non-Aligned and Other
Developing Countries, New Delhi

Dr. Howard Mann, International Institute for Sustainable Development, Ottawa

Dr. Percy S. Mistry, Oxford International Group, United Kingdom

Prof. Solomon Picciotto, Lancaster University, United Kingdom

Mr. Andreas Ragaz, SOFI, Switzerland

Prof. Albert Edward Safarian, University of Toronto

Ms. Magdolna Sass, Hungarian Academy of Sciences, Budapest

Mr. Pierre Sauvé, OECD

Prof. M. Sornarajah, National University of Singapore

Prof. Joel P. Trachtman, Tufts University, United States

Dr. Cynthia Wallace, Consultant, United States
