VIEW

In view of the growing interest surrounding the issue of a possible multilateral framework on investment, the journal is beginning, with this issue, a special section containing individual views on this subject.

The Multilateral Investment Agreement

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Introduction

The negotiations on a Multilateral Agreement on Investment (MAI), which started in September 1995, have entered their final phase. After a series of orientation debates on the main features of the agreement, the structure of the MAI is now clearly emerging. Many issues are still unresolved, however, which makes meeting the goal set by the OECD Ministerial Council of having the MAI ready by the spring of 1997 a formidable challenge. Enough is known by now, however, to give a reasonably accurate idea of what the MAI will look like.

This article is structured in two sections. The first provides an overview of what the MAI is likely to contain. The second examines issues related to the participation of non-OECD countries. The reasons why a MAI is needed are not reviewed here as this has already been done on an earlier occasion (Witherell, 1995).

The structure of the negotiations

Before dealing with the status of the negotiations, a word needs to be said about the process. The OECD Ministerial Council established a Negoti-

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ating Group on the MAI in June 1995. As the MAI is to be an independent treaty, to which non-OECD countries may accede, the Negotiating Group operates independently from any standing OECD committee. Whereas it directs the negotiations as a whole, the drafting of texts has so far been done by working groups to which countries send the appropriate experts. These groups work on the basis of directives given by the Negotiating Group on the particular subject at hand. They submit their proposals to the Negotiating Group, which in turn either discharges the group or renews its mandate. Any remaining problems ultimately have to be solved by the Negotiating Group itself.

The contents of the Agreement

Definitions

The fundamental point of how to define investment in the context of the MAI has been the subject of extensive debate. Finding an early solution to the definition problem has enjoyed the highest priority, if only because it holds the key to agreement on the actual MAI disciplines and, most important of all, on the scope of dispute settlements. There was an early consensus that the MAI should have a single broad definition, going beyond the traditional notion of FDI to cover tangible and intangible assets, and which applies to both pre- and post-establishment. An earlier option of having two definitions, a narrow one for pre-establishment, and a wider one for post-establishment, was generally seen as undesirable. The choice for a single broad definition implies having to reconcile two conflicting desires. On the one hand, the definition should be broad enough to ensure that all relevant forms of investment undertaken by foreign investors enjoy the benefits of the MAI. Such relevant forms not only include non-tangible assets such as intellectual property, but also any portfolio investment that an investor has acquired or may wish to acquire. On the other hand, the definition should not be so wide as to cover trade operations, or purely financial transactions such as take place in capital and money markets, and that are not part of an investor's real assets.

Whereas distinguishing between portfolio investment as an asset on the one hand, and trade or financial operations on the other, may be easy in theory, actually translating that into a draft text has proven to be quite difficult. This led some countries to propose that portfolio investment be

excluded from the MAI altogether. Most others maintained that foreign investors operate on the financial markets of a host country just as any domestic investor does, and acquiring such portfolio investments is very much part of their overall investment in that country.

Although formal agreement has not yet been reached, the most widely supported proposal is that the definition of investment consists of an open (i.e. non-exhaustive) list of assets that are considered an investment, and a short closed list of items or operations that, except for purposes of investment protection, are *not* considered an investment. The latter list would include things like trade credits, traded goods and foreign exchange operations. An alternative proposal is to have only an open ''positive'' list, but to allow countries to make reservations on national treatment (except for protection) for those items that are now mentioned in the ''negative list''. Although this would allow each MAI party some flexibility as to what to exclude, it would also, in the eyes of many, have the drawback of being less transparent than a scope and definition of general application.

Whichever option is chosen, the definition of investment will most likely include the following:

''Every kind of asset owned or controlled by an investor, including

(i) an enterprise (being a legal person or any other entity constituted or organized under the applicable law of the Contracting Party, whether or not for profit, and whether private or government-owned or -controlled, and includes a corporation, trust, partnership, sole proprietorship, branch, joint venture, association or organization);

(ii) shares, stocks or other forms of equity participation in an enterprise, and rights derived therefrom;

(iii) bonds, debentures, loans and other forms of debt;

(iv) rights under contracts, including turnkey, construction or management contracts, production or revenue-sharing contracts, or concession contracts;

(v) claims to money, and claims to performance having an economic value;

(vi) intellectual property rights;

(vii) rights conferred pursuant to law or contracts such as concessions, licences and permits.''

The only real debate concerning the definition of investor has focused on the question whether branches could be considered as such. Legislation in most countries does not confer upon branches the appropriate legal capacity to independently act as an investor. Only in the area of financial services can branches sometimes act as such.

Thus the definition of investor would be:

''(i) A natural person having the nationality of, or permanently residing in, a Contracting Party in accordance with its applicable law; or

(ii) A legal person or any other entity constituted or organized under the appropriate law of a Contracting Party, whether or not for profit, and whether private or government-owned or controlled, and includes a corporation, trust, partnership, sole proprietorship, joint venture, association or organization.''

Investment protection

As expected, the drafting of provisions on investment protection has proceeded relatively quickly. There are only a few items where full agreement is still lacking. These differences of view mainly reflect the differences in model bilateral investment agreements: there is no disagreement about the core principles of investment protection. Thus, there is an article on general treatment, which, among others, lays down the basic rule of fair and equitable treatment and full and constant protection and security which is to be accorded to investments of another Contracting Party at all times. The article on expropriation is in conformity with best practice in bilateral investment agreements, as is the article on protection from strife.

A key article is the obligation for the host State to ensure free transfer of payments related to an investment. Such free transfer relates to:

- The initial capital and additional amounts to maintain or increase an investment;
- Returns;

- Payments made under a contract including a loan agreement;
- Proceeds from the sale or liquidation of all or any part of an investment;
- Payments of compensation relating to expropriation;
- Payments arising out of the settlement of a dispute;
- Earnings and other remuneration of personnel engaged from abroad in connection with an investment.

A number of delegations feel that the article on free transfer is a core provision of the MAI and as such should be unrestricted. Other countries, however, point to the IMF Agreement which allows countries to restrict transfers in case of a balance-of-payments crisis. Many of these countries acknowledge, however, that the IMF Agreement does not prevent MAI parties from waiving among themselves any rights under the IMF Agreement. This debate is also related to the question of which definition of investment will eventually be adopted.

Treatment of investment

The draft text on the treatment of investments clearly shows that the principle of non-discrimination is the cornerstone of the MAI: the obligation to extend national treatment and most-favoured-nation treatment applies to:

> "the establishment, acquisition, expansion, operation, management, maintenance, use, enjoyment, and sale or other disposition of investments".

The strength of the MAI is largely determined by the extent that countries are allowed to deviate from the national treatment principle. In other words, which grounds for general exceptions should be included (national security comes to mind here), and how should the MAI deal with country-specific reservations. The difference between these concepts is that exceptions will be explicitly acknowledged grounds for not observing the national treatment rule, whereas country-specific reservations would list certain sectors or economic activities where foreign investors face restrictions. Such reservations will be subject to a so-called standstill obligation, i.e. no new restrictions are allowed once the MAI has taken effect for a country.

This raises the question of how the MAI can contribute to liberalization of investment policies. Whereas the standstill obligation will ensure that parties remain committed to the level liberalization agreed to at the entry into force of the MAI, some countries would like to see a mechanism that ensures that this level of liberalization is satisfactory to all. This implies that a process of "upfront liberalization" would have to take place before the negotiations on the MAI can be concluded. This would imply negotiations about proposed reservations aimed at achieving a satisfactory balance of commitments. Other countries are convinced that the MAI as an agreement represents a convincing liberalising effort. Further liberalization could be achieved by applying "peer pressure", as is done under the existing OECD instruments.

At its meeting in December 1996, the Negotiating Group agreed that countries should, by the end of February 1997, table an initial list of reservations they intend to lodge with regard to the MAI obligations. This will provide an adequate basis for a subsequent discussion on how to achieve the appropriate level of liberalization.

Looking at the issue of general exceptions, two questions are still under discussion. First there is the debate whether national security would be the only ground for a general exception. Some countries have said that public order should be added. A few also want a general exception for certain "cultural industries", such as publishing or films.

The second question is to what extent national security (or public order) is a "self-judging" concept, i.e. whether an invocation of such an exception can or cannot be challenged through dispute settlement. In both these cases, countries will have to exert their political judgements. The willingness of a country to make concessions on such points will to a large extent be determined by the importance that it attaches to the MAI as a whole.

Additional disciplines

An important feature of the MAI is that it will also address obstacles to investment that are not covered by the rule of national treatment and MFN. Six issues have been examined:

- Temporary entry and stay of investors and key personnel;
- Performance requirements;

- Privatization;
- Monopolies and State enterprises;
- Investment incentives;
- Corporate practices.

Temporary entry and stay is based on the recognition that foreign investors attach considerable importance to the ability to freely transfer or hire personnel to perform key functions. Firms accept that countries cannot simply waive immigration or visa requirements, but they ask for simplified and speedy procedures when certain basic criteria are met. They greatly benefit from a waiver on any standing requirements to recruit employees locally. Besides key personnel, the MAI will also simplify entry and temporary stay of investors (i.e. natural persons) who are in the process of setting up an investment.

Performance requirements are obligations that governments may impose on investors to secure perceived economic benefits to the country as a whole. In some cases performance requirements are linked to grants, subsidies or other financial advantages. The concern here is that such requirements interfere with decisions to be made by the investor himself, and that they lead to market distortions. In the WTO Agreement on Trade-related Investment Measures (TRIMs), the focus is on trade-related performance requirements. In the MAI, the focus is on all performance requirements that distort investment flows. From that perspective, any performance requirement that can have such distorting effects are prohibited. This is irrespective of whether measures also apply to domestic investors, or whether they are maintained at the central, regional or local level.

The MAI is expected to prohibit requirements to:

- Export a given level or percentage of goods or services;
- To achieve a given level or percentage of domestic content;
- To purchase, use or accord a preference to goods produced or services provided in its territory, or to purchase goods or services from persons in its territory;

- To relate in any way the volume or value of imports to the volume or value of exports or to the amount of foreign exchange inflows associated with such investment;

- To restrict sales of goods or services in its territory that such investment produces or provides by relating such sales in any way to the volume or value of its exports or foreign exchange earnings;

- To transfer technology, a production process or other proprietary knowledge to a natural or legal person in its territory;

- To locate the headquarters for a specific region or the world market in a contracting party;

- To supply one or more of the goods that it produces or the services that it provides to a specific region or world market exclusively from the territory of that contracting party.

Performance requirements linked to subsidies are a more difficult issue, particularly in the case of fiscal incentives. Although there is consensus that the rules on performance requirements in the MAI should to the extent possible also apply to requirements that are linked to subsidies, opinions are still divided on this issue.

The preceding is an automatic introduction to the next potential new discipline: *investment incentives*. Now that practically all countries actively promote inward foreign investment, the use of various kinds of incentives, including fiscal measures such as tax holidays, has increased noticeably. This has led to a competition among countries to attract foreign investors. UNCTAD has done valuable analytical work in this area, particularly the illuminating chapter on incentives that appeared in the *World Investment Report 1995* (UNCTAD, 1995, pp. 288-305), in itself based on a separate study on incentives (UNCTAD, 1996).

It will come as no surprise that, also among OECD countries, views differ on what the MAI can include on incentives. To begin with, there are serious problems of definition: what should be termed an incentive and what not? Most countries agree that the effects of the incentives competition are often undesirable. But, they say, applying subsidies to promote economic development through new investment, domestic or foreign, is in itself a legitimate policy tool.

There is consensus that, rather than aiming for outright prohibition of incentives, we should begin by making the offering of incentives more transparent. The first thing to consider would be to apply the rule of national treatment to incentives to avoid positive discrimination of foreign investors. Furthermore, applying the most-favoured-nation principle should eliminate discrimination between foreign investors from different countries.

Other new, but relevant topics from an investment perspective are *privatization, monopolies and State enterprises*. The relevance of dealing with privatization will be self-evident: in many countries, OECD as well as non-OECD member countries, the government is engaged in an ongoing process of transferring ownership and control of firms to the private sector. The proposal is that, once such firms (or parts thereof) are offered to private investors, the non-discrimination principle of the MAI should apply. In other words: foreign investors should have the same rights to acquire government-held assets as domestic investors. The point of departure is that the decision to privatize remains in the hands of a government. In other words, the MAI cannot in any way be construed as containing an obligation to privatize. That said, a potential problem could arise with so-called special share arrangements that are sometimes imposed on privatized companies: under such arrangements, certain categories of shareholders may have rights that exceed those of other shareholders to allow them to, for instance, veto certain policy decisions.

There is broad agreement among the MAI negotiators that the national treatment, MFN and transparency obligations of the MAI will apply to both the initial and the subsequent sales associated with a privatization. In view of this, special share arrangements that explicitly discriminate against foreign investors are regarded as inconsistent with these obligations and would therefore have to be covered by a reservation.

Where a monopoly exists there is no room for other private investors, foreign or domestic. The MAI will not interfere in this area. As in the case of privatization, the decision to demonopolize is a sovereign right of each country. In fact, most countries feel that the decision to create or abolish a monopoly is mainly subject to considerations of national competition policy and thus remains outside the scope of the MAI. However, monopoly enterprises often represent significant forces in a given market. They also sometimes exercise certain powers conferred upon them by the government. Thus, it was considered desirable that the MAI contain rules on the behav-

iour of monopolies so as to ensure that the non-discrimination principle be observed. Full consensus does not yet exist on this issue.

A remaining point of discussion is the question whether in case of demonopolization of a particular industry a MAI party would be allowed to lodge a reservation with regard to obligations under the MAI. Some countries recognize that the MAI applies as soon as a sector is demonopolized, but they would want an exception to the obligation on standstill on new reservations so as to preserve a certain measure of policy flexibility.

The idea behind possible rules on *corporate practices* is that whereas governments would be obliged to provide national treatment to foreign investors, firms might still be free to discriminate against them in areas outside government control. An example would be inserting into the articles of association a possibility to prevent a foreign take-over. As in the case of monopolies however, this debate leads into the area of competition policy. Consequently, most countries see little scope for actual disciplines in the MAI. On the other hand, a suggestion that the MAI prohibit nationality requirements for senior management positions is likely to be adopted. NAFTA in fact contains a provision to that effect.

Dispute settlement

This is a central feature of the MAI. In principle, any obligation under the MAI will be subject to dispute settlement. As a concept, dispute settlement is fairly novel to OECD (although there is a precedent with the Shipbuilding Agreement, which has not yet entered into force). But there is consensus that a state-of-the-art agreement on investment should contain a mechanism for dispute resolution which is at least equal to model bilateral agreements on investment, and to that which has been developed in WTO. WTO is particularly relevant here, because the GATS, to the extent that commitments have been made, includes the right of establishment to set up a commercial presence.

Whereas the dispute settlement under the WTO system is limited to disputes between States parties, the MAI will, in addition, contain a procedure for arbitration of disputes between an investor and a host State. In both cases, decisions by arbitral panels will be binding on parties to the MAI, and they should also be enforceable in their territories. The mechanism and procedures for State-State disputes relating to the MAI do not re-

ally differ from those that are contained in the many hundreds of bilateral investment treaties. The three-member ad hoc tribunal may in its awards provide various forms of relief that include a declaration, a recommendation that a party bring its measures into conformity with the MAI, or any relief to which the party against whom the award is made consents; this may include restitution in kind.

In case of a procedure initiated by an investor, the latter has a choice of submitting it to a court or tribunal of the host country, or to the arbitration by an international tribunal as foreseen under either the Convention on the Settlement of Investment Disputes between States and Nationals of other States (the ICSID Convention), the so-called ICSID Additional Facility (in case a party has not ratified the ICSID Convention), the Arbitration Rules of the United Nations Commission on International Trade Law (UNCITRAL), or the Rules of Arbitration of the International Chamber of Commerce (ICC).

The forms of relief that awards of any of these tribunals may provide will be clearly circumscribed in the MAI. They include a declaration, compensatory monetary damages, restitution in kind, or, with the consent of all parties to the dispute, any other form of relief.

Although the main characteristics of dispute settlements are clear, there are several issues that featured dominantly in the discussions and where consensus has not yet been reached. In the context of investor-to-State disputes, there is the issue of whether national and international arbitration procedures are mutually exclusive (if they should at all be mutually exclusive). In the investment jargon, this is known as the ''fork in the road''. A number of countries feel that, once the road of national judicial arbitration is chosen by an investor, the road to international procedures is automatically cut off. Other countries say that a choice for national procedures does not preclude access to international procedures if the investor so desires. It has also been noted that preserving the option of international arbitration has been accepted by many countries in the context of bilateral agreements on investment protection.

Another issue is the application of investor-to-State dispute settlements to the pre-establishment obligations in the MAI. In other words, should an investor who wishes to make an investment but is precluded from doing so by a (potential) host government be able to start proceedings

against that government? Many countries feel that investor-State procedures should apply to all those provisions in the MAI which create rights for investors. Some of them point to NAFTA as an example of an agreement where these procedures apply to disputes on establishment. Other countries feel that such questions are more properly dealt with under State-to-State procedures, since establishment questions are too closely linked to a country's sovereignty to allow an investor to start proceedings. Another concern is that of the risk of a proliferation of unfounded, frivolous disputes. It has also been pointed out that the WTO dispute-settlement system, which does not provide for investor-State procedures, could be negatively affected. This would be a relevant factor where a dispute on establishment is also covered by the General Agreement on Trade in Services (GATS).

Taxation and the Multilateral Agreement on Investment

Taxation is a vital point in foreign investment decisions. Foreign investors attach primary importance to fair fiscal treatment. Logically, therefore, the non-discrimination rule in the MAI should extend to fiscal treatment. But in reality, things are not that simple. Fiscal experts have identified a number of problems that would arise if the provision of MAI were in its entirety to apply to taxation. Their primary concern is that strong obligations on national treatment, non-discrimination and MFN treatment, as envisaged in the MAI, could conflict with obligations contained in the many bilateral agreements on the avoidance of double taxation. Although these agreements are also based on the non-discrimination principle, this does not necessarily mean that a foreign investor is always taxed identically to a local firm. Also, because bilateral agreements on taxation do not contain arbitration as a dispute-settlement mechanism, there might be a preference for firms to use the MAI mechanism and thus pre-empt the application of taxation treaties.

These considerations led some fiscal experts to advocate a provision in the MAI stating that the agreement would not apply to tax measures. Other experts are of the opinion that some MAI rules could possibly apply to taxation: thus, the tax carve-out would have to be more accurately defined. After considerable debate the conclusion is that, as a general rule, the MAI will not apply to fiscal measures, except for certain specific provisions such as expropriation and transparency. Although taxes will not normally have an expropriatory effect, it is conceivable that a country could use fiscal meas-

ures to achieve a so-called creeping expropriation. Also, investors should have the right to be fully informed about applicable fiscal policies.

Accession by non-OECD countries

As already mentioned, non-OECD member countries should be able to accede to the MAI, once it has been developed. To that end, the MAI will be an independent treaty rather than an OECD instrument. This would also allow those OECD countries that cannot (yet) become a party to the MAI to accede at a later point (or not at all). The current state of thinking is that the members of the MAI Negotiating Group sign a Final Act. This Final Act will presumably lay down the reservations that the signatories intend to lodge with regard to MAI obligations. Those signatories of the Final Act that wish to sign up to the MAI can do so at their own convenience. In doing so, they will become members of the MAI Parties Group.

A country or other sovereign entity that did not sign the Final Act can accede to the MAI on terms to be agreed upon between it and the members of the Parties Group. In essence, an acceding country will negotiate the terms of its accession with the MAI parties. That does not mean reopening negotiations on the text of the MAI, but it does mean agreeing on the reservations, if any, that the country concerned would have to lodge to the various MAI provisions. It might also include agreement on a transition period with regard to certain obligations.

Why would it be attractive for a country to accede to the MAI, even if it has not taken part in the negotiation of the text? The main attraction of the MAI is that it represents high standards in every respect. High standards mean clear rules on market access, treatment and legal protection, supported by an effective dispute-settlement mechanism. For a country wishing to attract investment, signing up to the MAI means saying loud and clear to investors that the country concerned subscribes to these standards. This cannot fail to have positive effects on investment decisions by foreign firms.

For countries that are also a source of outward investment, the MAI offers the additional attraction of ensuring market access and legal protection for all forms of investment into the other MAI countries. In view of the fact that more and more traditionally capital-importing countries are also

becoming capital-exporting countries, this other side of the coin should be firmly kept in perspective.

In this context, the question arises whether or not investors are entitled to the benefits of the MAI anyway through the MFN principle as embodied in the GATS or in the bilateral investment agreements. To a certain extent that is true. But the MAI will be much more comprehensive, both in substance and in the scope of its dispute-settlement procedures: in substance, because it covers all sectors of economic activity, not just services; and in the scope of dispute settlement, because investors can themselves bring claims before an arbitral panel.

An important thing to consider is that, once a country has acceded to the MAI, it will be a member of the Parties Group, enjoying the same rights as all the Parties, OECD member or not. The OECD ministers decided not to invite other countries to take part in the negotiations as such, mainly because experience shows that the more countries are involved, the slower the pace of work. Instead, they opted for the best alternative: they have requested that non-OECD member countries be kept informed about the MAI. Given this political commitment, the Chair of the Negotiating Group has, together with the OECD Secretariat, taken the initiative to organize meetings in Paris where non-OECD member countries receive the latest information about the state of play of the negotiations.

The outlook

At the time of publication of this article, the MAI negotiations have entered their final year. This implies that the orientation stage of the debate has been concluded, and that countries must make decisions, both on the specific provisions of the MAI, and on the reservations that will have to be made. Before the MAI is to be signed, there will have to be a consensus among countries that a balance of commitments exists. In other words, not every reservation proposed by one country may necessarily be acceptable to other countries. This is why countries have been asked to submit their list of proposed reservations by the end of February 1997.

Although there is a considerable degree of policy consensus among OECD countries when it comes to treatment of foreign investment, there are

more general differences in legal and policy concepts that have arisen as obstacles. These include the following:

- Some countries may have difficulties in binding their sub-federal territories to the MAI. This would be a particular problem where such territories have independent legislative authority in the area of investment;
- There is no consensus as to the possibility to be allowed for regional economic integration organizations to internally advance liberalization on investment without extending it to other MAI partners;
- Some countries want to be able to deviate from MAI obligations on grounds of cultural policies;
- Many countries want the MAI to contain guarantees that a country cannot adopt legislation which is meant to be applied outside its territory, leading to conflicting requirements for investors between home and host State legislation.

These problems do not alter the fact that there is an encouraging determination among the OECD countries to conclude the negotiations. This suggests that it is a realistic expectation to have the Agreement ready for adoption by the summer of 1997. ■

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