The OECD Multilateral Agreement on Investment

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The ministers of the Organisation for Economic Co-operation and Development, at their meeting in May 1995, decided to launch negotiations among the member countries aimed at reaching a Multilateral Agreement on Investment by mid-1997. Negotiations commenced in September 1995 with a first meeting of the Negotiating Group, which will be meeting frequently in Paris during the next two years. Once agreed, the Multilateral Agreement on Investment will be open to signature by non-member countries which will be consulted as the negotiations proceed.

The launching of these negotiations is one of the most important international initiatives in recent years. At present, companies making cross-border investments are confronted with a vast array of different legal frameworks as they consider where to invest. Differences in laws, regulations and other international agreements would, of course, continue after agreement on the Multilateral Agreement on Investment, but investors would be assured non-discriminatory treatment and be provided protection. Although investment regimes have become much more open and welcoming in the recent past, there is no assurance that they will remain so in the years to come. Moreover, important barriers to foreign direct investment remain. The Multilateral Agreement on Investment initiative aims at providing a strong and comprehensive framework for foreign direct investment, widening the scope of existing liberalization and providing legal security for international investors. The proposed Agreement seeks to "level the playing field" and ease market access, essentially by embodying the principle of national treatment in a multilateral and most-favoured-nation context. To give teeth to the Multilateral Agreement on Investment, it would be legally binding and contain effective dispute-settlement provisions.

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Background

During 1993-1994, foreign-direct-investment (FDI) flows from the Organisation for Economic Co-operation and Development (OECD)[1] countries resumed the long-term trend towards increasing international investment relative to GNP that characterised the 1980s and was interrupted by the cyclical slowdown in the early 1990s. These outflows grew by 11 per cent in 1994, reaching an estimated $196 billion, and this growth appears to be continuing unabated in 1995 (OECD, 1995a).

Foreign direct investment is of increasing importance to a broad and growing range of countries and enterprises, linking them together in an increasingly globalized economy. Whereas in the past a few developed countries accounted for the bulk of FDI flows, most OECD countries—and a number of advanced non-OECD countries—are now exporters of investment capital as well. At the same time, some of the main investment-exporting countries have become major host countries as well, and FDI inflows have become more widely distributed in the OECD area. The share of OECD FDI outflows going to non-OECD countries has recovered from the levels of the late 1980s (when they were depressed by the aftermath of the debt crisis), but most OECD FDI—some 75 per cent—still flows among the OECD countries.

While macroeconomic and market developments play a large role in determining FDI flows and their distribution, the growing process of international economic integration has been both an important cause and a consequence of this strong upward trend. Competition for investment funds has intensified. The spectacular FDI growth has been supported by widespread liberalization of inward investment regimes, deregulation, privatization and the lifting of exchange controls. The result has been a more favourable investment climate, especially in the OECD area, and increasingly in a growing number of non-OECD countries as well. Partly in response to these developments (but also to advances in technology), an increasing number of firms have shifted from product to geographical diversification, reflecting a growing recognition of the need to expand beyond domestic markets. Such activity creates a chain reaction, with firms investing abroad in response to moves by their rivals—and the globalization process gathers further momentum.

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[1] The 25 OECD member countries are the following: Australia, Austria, Belgium, Canada, Denmark, Finland, France, Germany, Greece, Iceland, Ireland, Italy, Japan, Luxembourg, Mexico, The Netherlands, Norway, New Zealand, Portugal, Spain, Sweden, Switzerland, Turkey, United Kingdom, United States.

The new investment-policy environment

There is a strong and growing international consensus as to the benefits of FDI in terms of productivity and competitiveness, transfer of technical and managerial know-how and integration in a rapidly changing international economy. The liberalisation of FDI policies by many countries and the increasing competition for FDI at the national and subnational level attest to the growing awareness of the importance of FDI. The phenomenon is striking among OECD countries. It is also increasingly apparent among non-OECD countries which see the need for FDI to supplement domestic savings and stimulate economic growth and recognise that there is great international competition for capital supplies.

Within the OECD area, the positive investment environment owes a great deal to the OECD investment instruments, in particular, the Declaration and Decisions on International Investment and Multinational Enterprises and the OECD Codes of Liberalisation of Capital Movements and of Invisible Transactions (see box; OECD, 1992a, 1992b, 1994, 1995b). These instruments have played a valuable role over the past several decades and should serve as a starting point for developing a more comprehensive set of multilateral rules for investment. Taken together, these instruments provide for:

- national treatment, both before and after establishment;
- repatriation of profits, dividends, rents and the proceeds of liquidated investments;
- transparency of regulations;
- a mechanism of consultation to deal with complaints; and
- peer review to promote rollback of remaining restrictions.

These instruments continue to be a positive force for liberalization among OECD countries. But, even taken together, they do not constitute the comprehensive and fully binding multilateral agreement on investment that the OECD countries believe is needed in the new investment environment.

Despite the widespread liberalization in recent years, foreign investors still encounter investment barriers, discriminatory treatment and legal and regulatory uncertainties. Such remaining restrictions are a potential source of international friction, not the least because they are now widely perceived as barriers to market access. This perception has become more acute as other

Box. The OECD investment instruments

A. Draft Convention on the Protection of Private Property

The Draft Convention, which was published in its current form in 1967, differs from the other instruments in that it has no follow-up procedures in the Organisation. While not formally an "instrument", it bears mention as the text has served widely as a model for bilateral investment treaties, and as a useful reference especially for developing countries that are generally asked to conform as far as possible to the model bilateral treaty proposed by their developed country partners.

B. Declaration and Decisions on International Investment and Multinational Enterprises

Adopted in 1976, the Declaration on International Investment and Multinational Enterprises contains four distinct elements woven into a balanced overall package of instruments designed to address key issues for international co-operation. The Declaration is a political undertaking, supported by legally-binding Decisions of the OECD Council, that provides active follow-up procedures covering notification, policy monitoring, review and consultation.

The four elements of the Declaration are as follows:

- — a ***National Treatment*** instrument provides that OECD members should treat foreign-controlled enterprises operating in their territories no less favourably than domestic enterprises in like situations;
- — ***Guidelines for Multinational Enterprises*** that establish voluntary standards of conduct representing the collective expectations of OECD governments as to the behaviour of such enterprises;
- — an instrument on ***Investment Incentives and Disincentives*** that encourages transparency and provides for consultation and review; and
- — an instrument on ***Conflicting Requirements***, designed to avoid or minimise the imposition by OECD governments of conflicting requirements on TNCs and providing a forum for consultation.

C. Codes of Liberalisation of Capital Movements and Current Invisible Operations

The Liberalisation Codes, which are legally-binding Decisions of the OECD, promote the progressive liberalization of capital movements and current transactions. They cover most international transactions other than trade in goods. As early as 1961, when the Codes were adopted at the same time as the OECD came into being, specific provisions were included on inward FDI, including the creation of new enterprises; expansion of existing enterprises; mergers, take-overs; and participation in domestic enterprises by non-residents. However, it was only in April 1984 that agreement was reached to make these provisions fully effective by requiring that member countries apply the national treatment principle when considering applications for licenses, or other authorisations needed for conducting business in the country concerned. A 1984 amendment brought within the preview of the Capital Movements Code the main elements of the right of establishment.

Although of different legal standing, the Liberalisation Codes and the National Treatment instrument form together a coherent set of instruments to promote an open climate for international investment, free of governmental barriers. They apply formally only to the OECD area. However, the Codes recommend that liberalization be extended to all members of the International Monetary Fund. The European Community joined (1991) in the Declaration of OECD member governments that contains the National Treatment principle. In 1994, Hungary adhered to the National Treatment instrument, including its follow-up procedures.

barriers to market access have been liberalized. The tolerance for the remaining restrictions is decreasing, and some countries are pursuing more forceful ways to ensure disciplines and resolve disputes. A tendency to resort to unilateral measures, including reciprocity, as a way of forcing more market access threatens to undermine the principle of non-discrimination on which OECD liberalization has been traditionally based and can thereby work in particular against the interests of smaller countries. A similar call for reciprocity is heard from countries opening up activities previously closed to private sector investment, whether domestic or foreign. Such developments can also contribute to investor uncertainty.

The Uruguay Round of Multilateral Trade Negotiations successfully concluded agreements on Trade-Related Investment Measures (TRIMs), Trade-Related aspects of Intellectual Property Rights (TRIPs) and the General Agreement on Trade in Services (GATS). These agreements are important steps in increasing disciplines in these areas, but address only to a limited extent the investment concerns cited above.

Faced with these developments in the investment-policy environment, OECD governments have been actively negotiating new bilateral, regional and sectoral agreements to promote a favourable environment for investment flows. As non-OECD countries are playing a growing role in international investment and access to their markets is of increasing importance to the OECD countries themselves, investment agreements are being negotiated or discussed in practically all parts of the world.

Bilateral, regional and sectoral agreements have brought clear benefits to FDI. However, the need for such approaches arises partly because existing multilateral disciplines are insufficient. Moreover, the lack of an overall cohesive structure may potentially distort the pattern of FDI flows and complicate corporate activity which is increasingly carried out on a global scale. There is a danger of spreading individualistic or self-centered solutions (either bilateral or regional) and conflicting rules. Investors are calling for a more secure, straightforward and consistent framework in which to conduct their international operations.

Investment-policy makers and international business circles have now perceived the need for something more: a comprehensive framework of binding investment rules which is sufficient to meet the requirements of the new international investment environment. Such a Multilateral Agreement on Investment (MAI) would set standards for equal competitive opportunities and provide stable and consistent treatment of FDI across all sectors.

In fact, business and labour have expressed support for a MAI to be negotiated in the OECD:

- The Business and Industry Advisory Committee (BIAC) to the OECD cites concern about the resurgence of negative attitudes towards FDI and the need for transnational corporations (TNCs) to be able to count on stable and consistent treatment of their investment as reasons for pursuing a MAI. Its companies are forging changes in the traditional patterns of doing business and are calling for a set of agreed common standards among all potential host countries to help create equal competitive opportunities for TNCs and domestic entities. BIAC believes the instrument could act as a catalyst for global economic growth by providing confidence to enterprises to increase FDI flows.

- The Trade Union Advisory Committee (TUAC) to the OECD favours a multilateral investment agreement which would, inter alia, set standards on employment and industrial relations. It believes that the phenomenon of globalization cannot be tackled by liberalization alone and that employment and environmental concerns must be discussed in the context of international movements of capital and enterprises.

The Multilateral Agreement on Investment

At the May 1995 meeting of the OECD Council at Ministerial Level, the ministers called for the immediate start of negotiations in the OECD aimed at reaching a Multilateral Agreement on Investment by the ministerial meeting in May 1997. They asked that this agreement "provide a broad multilateral framework for international investment with high standards for the liberalisation of investment regimes and investment protection and with effective dispute-settlement procedures" and that it "be a free-standing international treaty open to all OECD Members and the European Communities, and to accession by non-OECD Member countries, which will be consulted as the negotiations progress" (OECD, 1995b). Pursuant to this mandate, a Negotiating Group has been established which is responsible for conducting the negotiations and preparing the text of the agreement. This group held its first meeting in September 1995 and selected its bureau: Chairperson—F. A. Engering (Netherlands); Vice Chairperson—A. Saiki (Japan) and A. P. Larson (United States). An intensive work programme for the coming months was established.

The choice by the member governments of the OECD as the forum for these negotiations was based on a number of considerations. As noted earlier, the OECD has traditionally been a leader in the development of international investment rules. While recent developments have seen other countries join the ranks of home and host countries for FDI, OECD countries play a major role in the world economy and still account for the bulk of FDI flows and stocks. Sharing a common outlook towards FDI and long experience in promoting liberalization through existing instruments, OECD is the logical place to pursue discussions on a broad, multilateral investment agreement. Its existing basic framework of rules means negotiations will not have to start from scratch, making the objective of reaching agreement by mid-1977 feasible. The OECD committee structure provides an established basis for discussions in support of negotiations on an investment instrument, including consultations with experts in other disciplines (e.g., trade, taxation, competition policies), and with the private sector. As the OECD forms a group of broadly like-minded countries at similar levels of economic development and where liberalization is already very advanced, it is reasonable to expect that the highest standards of liberalization and investment protection could be achieved in this forum. This is considered essential, as there would be no value to investors or governments in an instrument incorporating watered-down, lowest common denominator standards.

Likely features of the Multilateral Agreement on Investment

The MAI would build on the achievements of the present OECD instruments, consolidating and strengthening existing commitments under the Liberalisation Codes and the 1976 Declaration and Decisions on International Investment and Multinational Enterprises. But it would be a new free-standing international treaty. The aim of negotiations is to conclude an agreement incorporating roll-back, standstill, national treatment and non-discrimination/most-favoured-nation (MFN) treatment, as well as new disciplines to improve market access and to strengthen the basis of mutual confidence between enterprises and states. The liberalization obligations would be complemented by high-level provisions on investment protection. The obligations under the agreement, which would be binding, would need to be reinforced by effective dispute-settlement procedures.

The agreement would be comprehensive in scope, covering all sectors. The MAI would aim to raise the level of existing liberalization based on a "top-down" approach under which the only exceptions permitted are those listed when adhering to the agreement and which are subject to progressive liberalization. The multilateral character of the agreement would be reinforced by embodying the principles of national treatment and non-discrimination/MFN and by opening it to accession by non-member countries. In particular, the aim of the negotiations is to achieve an agreement, with a satisfactory scope and balance of commitments, that would:

- set high standards for the treatment and protection of investment;

- go beyond existing commitments to achieve a high standard of liberalisation covering both the establishment and post-establishment phase, with broad obligations on national treatment, standstill, roll-back, non-discrimination/MFN and transparency, and apply disciplines to areas of liberalization not satisfactorily covered by the present OECD instruments;

- be legally binding and contain provisions regarding its enforcement;

- apply these commitments to all parties to the MAI at all levels of government;

- deal with measures taken in the context of regional economic integration organisations;

- encourage conciliation and provide for effective resolution of disputes, taking account of existing mechanisms; and

- take account of member countries' international commitments, with a view towards avoiding conflicts with agreements in the World Trade Organization (WTO) (such as GATS, TRIMs and TRIPs) and tax agreements; and, similarly, seek to avoid conflicts with internationally accepted principles of taxation.

These objectives were set as a result of the extensive work carried out by the Committee on International Investment and Multinational Enterprises (CIME) and by the Committee on Capital Movements and Invisible Transactions (CMIT), and in particular by the five working groups, composed of independent governmental experts set up in 1994 to explore, at the technical and analytical levels, the major issues for the MAI. The groups dealt, respectively, with liberalization obligations under existing OECD instruments, liberalization obligations in new areas, investment protection, dispute settlement and the involvement of non-members and institutional matters.

Completing the negotiations by May 1997 on an agreement that meets these high objectives will be a difficult task, requiring intensive work and a strong commitment on the part of all participants. The Negotiating Group, at its first meeting in September 1995, got off to a good start in this regard, reviewing the wide range of topics to be covered. It established a work programme through the end of the year. The Negotiating Group will be meeting every six weeks during the coming months, with working or drafting groups meeting possibly even more frequently. Delegates are to be connected through an electronic network, which will permit the rapid circulation of texts and comments.

The ambitious nature of this work programme appears more feasible when account is taken of the extensive preparatory work that has already been completed. Indeed, in the area of investment protection, the Negotiating Group has already asked a drafting group to produce texts for consideration by the group at its December 1995 meeting.

There are, of course, a large number of issues that will have to be addressed by the Negotiating Group in the coming months. The following is an illustrative sample of such issues:

- ***Scope of coverage***. The territorial scope of application of the agreement will have to be determined, as will the substantive scope of application, which depends on both the definition of investment and the definition of investor that are adopted. Choices will have to be made, *inter alia*, between asset-based and enterprise-based definitions of investment and how the definition should be applied to liberalization and investment protection. It is intended that the obligations of the MAI will apply to all parties to the agreement, including the European Union, and at all levels of agreement. How best to achieve this objective in the case of certain federal States will have to be resolved. The agreement will also need to deal with measures taken in the context of regional economic integration organisations, taking account of the economic rationale for these measures.

- ***Investment protection***. The OECD member countries have a large number of bilateral investment treaties from which high-level, state-of-the-art standards can be extracted. In view of the high degree of convergence of standards in this area, it is hoped that agreement on texts can be reached relatively rapidly. Yet, even in this area there are a number of different practices among OECD member countries. Provisions on expropriation, compensation and the transfer of funds are key elements. A comprehensive investment instrument should contain strong obligations in this respect, and should also address issues such as subrogation, protection from strife and observance of other obligations. The goal is to guarantee the investor and the investment fair and equitable treatment and full protection and security. Such a "general treatment" provision would likely be supplemented by national treatment and non-discrimination obligations. The exact scope of the investment protection provisions will be determined once the outcome of the negotiations on other issues, particularly the definition of investment to which the protection provisions will apply and the dispute settlement mechanisms available to enforce them, are clear. A number of technical issues would also need to be addressed, such as the definition of expropriation and the conditions relating thereto and the method for calculating compensation.

- ***Liberalization***. As noted above, the aim is a "top down" approach which goes beyond existing commitments to achieve a high standard of liberalization, covering both the establishment and post-establishment phase, with broad obligations on national treatment, non-discrimination/MFN transparency, standstill and roll-back. Options have been identified in the preparatory work that go well beyond the provisions of existing international agreements, including those of the OECD. Important issues are:

  - A basic obligation will be to provide *national treatment*, i.e., not to treat foreign investors less favourably than national investors in like situations. When applied to conditions of establishment and participation in existing enterprises by non-resident investors, this obligation would require the removal of entry restrictions on non-resident investors. Conditions of operation in the host country of foreign-controlled entities after establishment would, of course, also be covered by such an obligation. As noted earlier, OECD governments have been operating under a non-binding national treatment instrument since 1976, but the MAI obligations will be binding.

  - *Non-discrimination (or MFN)* refers to the obligation of a host country to grant to all foreign investors similar treatment irrespective of their country of origin. Negotiators will have to decide the extent to which (and how) this principle should be applied to other obligations in the MAI and to the operations and measures covered by it.

- The objective of *transparency* is important for it covers the provision of information that may be useful to investors and other parties and provides support for provisions of the agreement. The negotiators will have to consider various options for insuring transparency, such as notification requirements and publication of a country's positions under the MAI obligations.

- The objective of including *standstill* provisions implies the imposition of the status quo (notwithstanding other obligations such as non-discrimination) as an irreversible minimum standard for liberalization. Such provisions would exclude the introduction of new restrictions, unless this is made possible by other provisions, e.g. (temporary) derogations.

- *Roll-back* provisions would be designed to reduce over time exceptions to liberalization obligations, with a view to their eventual elimination. Roll-back will likely include both initial measures taken as negotiated preconditions for accession to an agreement and measures taken after accession. One option for the latter could be a predetermined timetable; an alternative would be future rounds of negotiations. Peer pressure enforcement mechanisms resting on moral suasion by partners to the agreement might be utilised. The OECD practice of undertaking reviews of measures and practices of countries, analysing and measuring them against the standards set by the agreement, could play a role. Such peer reviews could be undertaken by a "Parties Group" in which all those who adhere to the instrument would participate. Such mechanisms may be viewed as a useful complement to enforcement through the dispute-settlement provisions.

- Important but difficult questions will arise in the consideration of possible provisions for *exceptions*, *reservations* and *derogations* to the basic liberalization obligations. These issues will be related to the development of effective liberalization mechanisms and procedures in the agreement.

- ***Dispute settlement.*** The agreement will contain conciliation and dispute-settlement mechanisms. These will be developed bearing in mind the existing dispute-settlement mechanisms in other fora. Despite the ample precedents in bilateral investment treaties and other investment agreements, there are a number of difficult issues that will have to be addressed. Clearly, the MAI would be a stronger instrument if it provided for effective settlement for **both** investor-to-State and State-to-State disputes. The scope and application of such provisions would need to be determined. One question is the extent to which decisions relating to the establishment phase of an investment could be referred to the State-to-State dispute-resolution mechanism of the agreement. Another issue is whether an investor could bring a claim against a State for the breach of a liberalization obligation regarding establishment. Where the amicable settlement of disputes is not possible, the MAI would likely provide for recourse to international arbitration for investors and contracting parties. This raises questions about the appropriate institutional forum(s) and the enforceability of arbitration awards. There are numerous other, mostly technical, issues relating to dispute settlement that will have to be considered. Fortunately, there are ample precedents in bilateral investment treaties and other investment agreements.

- ***Specific issues***. The quest for higher standards of liberalization is expected to include an examination of possible disciplines with respect to a number of specific issues that appear to be of growing importance in the determination of the conditions for carrying out an investment operation:

  - The movement and emplacement of *key personnel* addresses two important issues: the ability to bring into the host country personnel key to the operations of an investment; and the right to employ, in connection with an investment, certain personnel who are legally within the host country, regardless of nationality.

  - The implications of *privatization practices* for FDI need to be considered, particularly with respect to the national treatment obligations issue.

  - *Monopolies/concessions and state enterprises* raise questions with respect to possible barriers to FDI.

  - *Corporate practices* also raise informal investment-barrier questions.

  - Mandatory *performance requirements* are addressed in the TRIMs agreement, and the question is whether a further, more ambitious step is needed.

  - *Investment incentives*, which are sometimes connected with performance requirements, are a large, complex area. There is an economic rationale for seeking to limit competition among countries in providing incentives, but there are also significant practical concerns about the feasibility of developing and implementing disciplines in this area.

In drafting the MAI, the negotiators could usefully draw, where appropriate, on the ideas and methods of other international agreements, for example, NAFTA, the Energy Charter Treaty and bilateral investment treaties. With respect to other international agreements and possible overlap (and bearing in mind the relevant legal rules on successive treaties on the same matter), the MAI should avoid conflicting obligations and allow better treatment for the investor to prevail. The relation between the MAI and taxation agreements as well as its interface with the GATS, TRIMs and TRIPs agreements will require special attention. Accordingly, these will be close co-operation with fiscal and trade experts and with the secretariat of the WTO. The WTO is expected to be an observer in the negotiations.

While the negotiations will be carried out by the 25 OECD member countries and the Commission of the European Communities, it is important to note that ministers asked that the resulting Agreement, which will be a free-standing international treaty, be open to accession by non-OECD countries, and that there be consultations with interested countries as the negotiations progress. The OECD has a wide range of possible mechanisms available for carrying out these consultations, including its Advisory Group on Investment involving the former centrally-planned economies and its "Policy Dialogue Workshops" with nine dynamic non-OECD economies of Asia and Latin America (Hong Kong, Malaysia, Republic of Korea, Singapore, Taiwan Province of China, Thailand, Argentina, Brazil and Chile) plus China, India and Indonesia. The purpose of these consultations will be to keep interested non-member countries informed of the development of the MAI and obtain their views on various aspects of the issues under negotiation. The member countries will wish to take account of these views, as it is hoped that a number of non-member countries will decide, in due course, that it would be in their interest to adhere to the MAI and that they are able to take on the MAI's obligations. All of the eventual parties to the treaty would then participate in its implementation, with the OECD more than likely providing the Secretariat function. ■

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