RECENT POLICY DEVELOPMENTS AND KEY ISSUES

CHAPTER III

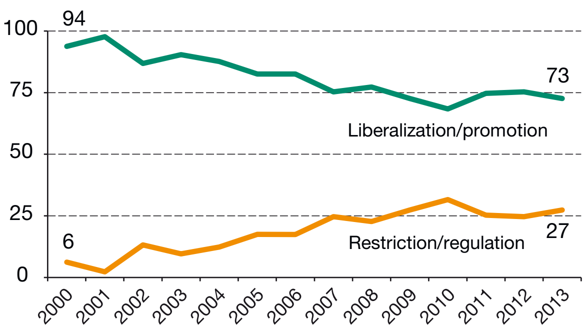
A. NATIONAL INVESTMENT POLICIES

1. Overall trends

Most investment policy measures remain geared towards promotion and liberalization, but the share of regulatory or restrictive measures increased.

In 2013, according to UNCTAD's count, 59 countries and economies adopted 87 policy measures affecting foreign investment. Of these measures, 61 related to liberalization, promotion and facilitation of investment, while 23 introduced new restrictions or regulations on investment (table III.1). The share of new regulations and restrictions increased slightly, from 25 per cent in 2012 to 27 per cent in 2013 (figure III.1). Almost half of the policy measures applied across the board. Most of the industry-specific measures addressed the services sector (table III.2).

Figure III.1. Changes in national investment policies, 2000–2013
(Per cent)



Source: UNCTAD, Investment Policy Monitor.

a. FDI liberalization and promotion

New FDI liberalization measures were mainly reported for countries in Asia. Several of them pertained to the telecommunications industry. For instance, *India* removed the cap on foreign direct investment in telecommunications.[1] The *Republic of Korea* passed the amended Telecommunications Business Act, which allows foreign investors covered by a free trade agreement (FTA) with the Republic of Korea to acquire up to 100 per cent of Korea's facility-based telecommunications businesses with the exception of SK and KT Telecom.[2] *Mexico* increased the threshold for foreign investment in telecommunications to 100 per cent in all areas except radio and television broadcasting, where the limit is 49 per cent under certain conditions.[3]

In addition to liberalizing telecommunications investment, *India* raised the FDI cap in the defence sector beyond 26 per cent upon approval by the Cabinet Committee on Security and under specific conditions. In other sectors, including petroleum and natural gas, courier services, single-brand retail, commodity exchanges, credit information companies, infrastructure companies in the securities market and power exchanges, government approval requirements have been relaxed.[4] *Indonesia* amended the list of business fields open to foreign investors and increased the foreign investment ceiling in several industries, including pharmaceuticals, venture capital operations in financial services and power plant projects in energy generation.[5] *The Philippines*

Table III.1. Changes in national investment policies, 2000–2013
(Number of measures)

Item	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
Number of countries that introduced changes	46	52	44	60	80	78	71	50	41	47	55	49	54	59
Number of regulatory changes	**81**	**97**	**94**	**125**	**164**	**144**	**126**	**79**	**68**	**88**	**121**	**80**	**86**	**87**
Liberalization/promotion	75	85	79	113	142	118	104	58	51	61	80	59	61	61
Restriction/regulation	5	2	12	12	20	25	22	19	15	23	37	20	20	23
Neutral/indeterminate[a]	1	10	3	-	2	1	-	2	2	4	4	1	5	3

Source: UNCTAD, Investment Policy Monitor database.
[a] In some cases, the expected impact of the policy measure on the investment is undetermined.

Table III.2. Changes in national investment policies, by industry, 2013
(Per cent and number of measures)

Sector/industry	Liberalization/promotion (%)	Restriction/regulation (%)	Neutral/indeterminate (%)	Total number of measures
Total	72	25	3	93
Cross-industry	80	17	2	41
Agribusiness	80	20	-	5
Extractive industries	60	30	10	10
Manufacturing	75	25	-	4
Services	64	33	3	33

Source: UNCTAD, Investment Policy Monitor database.
Note: Overall totals differ from table III.1 because some of the measures can be classified under more than one type.

amended its Rural Bank Act to allow foreign individuals or entities to hold equity of up to 60 per cent in rural banks.[6]

Among the FDI promotion measures, the National Assembly of *Cuba* approved a new law on foreign investment which offers guarantees to investors and fiscal incentives.[7] The country also set up a new special economic zone (SEZ) for foreign investors in Mariel.[8] The *Republic of Korea* has introduced a new system lowering the minimum required area to designate an investment zone.[9] In *Pakistan*, the Commerce Ministry finalized an agreement with the National Insurance Company for comprehensive insurance coverage of foreign investors.[10]

b. Investment liberalization and promotion for domestic and foreign investors

General investment liberalization policies in 2013 were characterized mainly by new privatizations. Full or partial privatizations benefiting both domestic and foreign investors took place in at least 10 countries. For instance, in *Peru*, the Congress approved the privatization of up to 49 per cent of the State energy firm Petroperú – the first time that investment of private capital in Petroperú has been authorized.[11] In *Serbia*, Etihad Airways (United Arab Emirates) acquired a 49 per cent stake in JAT Airways, the Serbian national flag carrier (see also chapter II.A.4).[12] In *Slovenia*, the Parliament gave its support to the Government's plan to sell 15 State-owned firms, including the largest telecommunications operator, Telekom Slovenia.[13] Another important liberalization relates to recent energy reforms in *Mexico.* In December 2013, the Mexican Congress approved modifications to the Constitution, including the lifting of a restriction on private capital in the oil industry (see also chapter II.A.3). The reforms allow the Government to issue licenses and enter into contracts for production sharing, profit sharing and services.[14]

Investment incentives and facilitation measures applying to investors irrespective of their nationality were enacted most commonly in Africa and in Asia. Promotion measures, which mainly focused on fiscal incentive schemes, included a number of sector-specific programs. Some policies were adopted in early 2014. For instance, the *Dominican Republic* extended tax benefits for investors in its tourism development law.[15] *Malaysia* announced its National Automotive Policy 2014, which grants fiscal incentives with the objective to promote a competitive and sustainable domestic automotive industry.[16]

Facilitation measures concentrated on simplifying business registration. For instance, *Mongolia* passed a new Investment Law that reduces approval requirements, streamlines the registration process and provides certain legal guarantees and incentives.[17] *Mozambique* passed a decree that will facilitate the establishment of new companies through a single business registration form.[18] Dubai, in *the United Arab Emirates*, introduced a series of reforms making it easier to set up hotels.[19]

A number of countries introduced SEZs or revised policies related to existing SEZs. For instance, *China* launched the China (Shanghai) Pilot Free Trade Zone, introducing various new policy measures on trade, investment and finance (see also chapter II.A.2.a). With regard to inward FDI, this free trade zone adopts a new approach, providing for establishment rights, subject to exceptions. Specific segments in six service sectors – finance, transport, commerce and trade, professional services, cultural services and public services – were opened to foreign investors.[20] The Government of *South Sudan* officially launched the Juba SEZ, an industrial area for business and investment activities.[21]

c. New FDI restrictions and regulations

Newly introduced FDI restrictions and related policies included revision of entry regulations, rejection of investment projects after review and a nationalization. At least 13 countries introduced new restrictions specifically for foreign investors in 2013.

Among the revisions of entry regulations, *Indonesia* lowered the foreign ownership ceiling in several industries, including onshore oil production and data communications system services.[22] *Sri Lanka* restricted foreigners from owning land but still allows long-term leases of land.[23] *Canada* changed the Investment Canada Act to make it possible for the Minister of Industry to decide – in the context of "net benefit" reviews under the act – that an entity is controlled by one or more foreign State-owned enterprises even though it would qualify as Canadian-controlled under the criteria established by the act.[24] The Government of *France* issued a decree reinforcing its control mechanisms for foreign investments in the interests of public order, public security or national defence. The measure covers the following strategic sectors: energy, water, transportation, telecommunications, defence and health care.[25] The Government of *India* amended the definition of the term "control" for the purpose of calculating the total foreign investment in Indian companies.[26] Recently, the *Russian Federation* added three types of transport-related activities to its law on procedures for foreign investment in business entities of strategic importance for national defence and state security.[27]

Some governments blocked a number of foreign takeovers. For instance, under the national security provisions of the Investment Canada Act, *Canada* rejected the proposed acquisition of the Allstream division of Manitoba Telecom Services by Accelero Capital Holdings (Egypt).[28] The Commission on Foreign Investment of the *Russian Federation* turned down the request by Abbott Laboratories (United States) to buy Russian vaccine maker Petrovax Pharm, citing protection of the country's national security interests, among other considerations.[29] In addition, the *European Commission* prohibited the proposed acquisition of TNT Express (the Netherlands) by UPS (United States). The Commission found that the takeover would have restricted competition in member States in the express delivery of small packages.[30]

The *Plurinational State of Bolivia* nationalized the Bolivian Airport Services (SABSA), a subsidiary of Abertis y Aena (Spain) for reasons of public interest.[31]

d. New regulations or restrictions for domestic and foreign investors

Some countries introduced restrictive or regulatory policies affecting both domestic and foreign investors. For instance, *the Plurinational State of Bolivia* introduced a new bank law that allows control by the State over the setting of interest rates by commercial banks. It also authorizes the Government to set quotas for lending to specific sectors or activities.[32] *Ecuador* issued rules for the return of radio and television frequencies in accordance with its media law, requiring that 66 per cent of radio frequencies be in the hands of private and public media (33 per cent each), with the remaining 34 per cent going to "community" media.[33] *The Bolivarian Republic of Venezuela* adopted a decree regulating the automotive sector regarding the production and sale of automobiles.[34]

e. Divestment prevention and reshoring promotion[35]

An interesting recent phenomenon entails government efforts to prevent divestments by foreign investors. In light of economic crises and persistently high domestic unemployment, some countries have introduced new approval requirements for dislocations and layoffs. In addition, some home countries have started to promote reshoring of overseas investment by their TNCs.

- In *France* the Parliament passed a bill imposing penalties on companies that shut down operations that are deemed economically viable. The law requires firms with more than 1,000 employees to prove that they have exhausted options for selling a plant before closing it.[36]
- *Greece* passed a law that makes it more difficult for companies listed on the Greek stock exchange to relocate their head offices abroad. The Greek capital markets law now requires approval of relocation by 90 per cent of shareholders, rather than the prior threshold of 67 per cent.[37]
- The *Republic of Korea* passed the Act on Supporting the Return of Overseas Korean Enterprises. Accordingly, the Government founded the Reshoring Support Centre and is planning to provide reshoring businesses with incentives that are similar to those provided to foreign-invested companies.[38]
- Since 2011, the Government of the *United States* has been operating the "Select USA" program, which, inter alia, has the objective of attracting and retaining investment in the United States economy.[39]

2. Recent trends in investment incentives

Incentives are widely used for attracting investment. Linking them to sustainable development goals and monitoring their impact could improve their effectiveness.

Policymakers use incentives to stimulate investments in specific industries, activities or disadvantaged regions. However, such schemes have been criticized for being economically inefficient and leading to misallocations of public funds.

a. Investment incentives: types and objectives

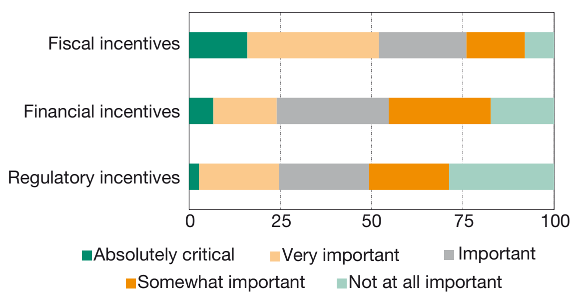
Although there is no uniform definition of what constitutes an investment incentive, such incentives can be described as non-market benefits that are used to influence the behaviour of investors. Incentives can be offered by national, regional and local governments, and they come in many forms. These forms can be classified in three main categories on the basis of the types of benefits that are offered: financial benefits, fiscal benefits and regulatory benefits (see table III.3).

From January 2014 to April 2014, UNCTAD conducted a global survey of investment promotion agencies (IPAs) on their prospects for FDI and for the promotion of sustainable development through investment incentives for foreign investors.[40] According to the survey results, fiscal incentives are the most important type for attracting and benefiting from foreign investment (figure III.2).[41] This is particularly true in developing and transition economies. Financial and regulatory incentives are considered less important policy tools for attracting and benefiting from FDI. In addition to investment incentives, IPAs consider investment facilitation measures as particularly important for attracting investment.

Investment incentives can be used to attract or retain FDI in a particular host country (*locational incentives*). In such cases, they can be perceived as compensation for information asymmetries between the investor and the host government, as well as for deficiencies in the investment climate, such as weak infrastructure, underdeveloped human resources and administrative constraints. In this context, investment incentives can become a key policy instrument in the competition between countries and within countries to attract foreign investment.

Investment incentives can also be used as a tool to advance public policy objectives such as economic

Figure III.2. Importance of investment incentives in the country's overall strategy to attract and benefit from FDI
(Per cent)



Source: UNCTAD survey of IPAs (2014).
Note: Regulatory incentives only refer to the lowering of standards.

Table III.3. Investment incentives by type and mechanism

Financial incentives	
Investment grants	"Direct subsidies" to cover (part of) capital, production or marketing costs in relation to an investment project
Subsidized credits and credit guarantees	Subsidized loans Loan guarantees Guaranteed export credits
Government insurance at preferential rates, publicly funded venture capital participating in investments involving high commercial risks	Government insurance at preferential rates, usually available to cover certain types of risks (such as exchange rate volatility, currency devaluation and non-commercial risks such as expropriation and political turmoil), often provided through an international agency
Fiscal incentives	
Profit-based	Reduction of the standard corporate income tax rate or profit tax rate, tax holiday
Capital-investment-based	Accelerated depreciation, investment and reinvestment allowances
Labour-based	Reduction in social security contribution Deductions from taxable earnings based on the number of employees or other labour-related expenditures
Sales-based	Corporate income tax reductions based on total sales
Import-based	Duty exemptions on capital goods, equipment or raw materials, parts and inputs related to the production process Tax credits for duties paid on imported materials or supplies
Export-based	Export tax exemptions, duty drawbacks and preferential tax treatment of income from exports Income tax reduction for special foreign-exchange-earning activities or for manufactured exports Tax credits on domestic sales in return for export performance, income tax credits on net local content of exports Deduction of overseas expenditures and capital allowance for export industries
Based on other particular expenses	Corporate income tax deduction based on, for example, expenditures relating to marketing and promotional activities
Value added based	Corporate income tax reductions or credits based on the net local content of outputs Income tax credits based on net value earned
Reduction of taxes for expatriates	Tax relief to help reduce personal tax liability and reduce income tax and social security contribution
Other incentives (including regulatory incentives)	
Regulatory incentives	Lowering of environmental, health, safety or labour standards Temporary or permanent exemption from compliance with applicable standards Stabilization clauses guaranteeing that existing regulations will not be amended to the detriment of investors
Subsidized services (in kind)	Subsidized dedicated infrastructure: electricity, water, telecommunication, transportation or designated infrastructure at less than commercial price Subsidized services, including assistance in identifying sources of finance, implementing and managing projects and carrying out pre-investment studies; information on markets, availability of raw materials and supply of infrastructure; advice on production processes and marketing techniques; assistance with training and retraining; and technical facilities for developing know-how or improving quality control
Market privileges	Preferential government contracts Closing the market to further entry or the granting of monopoly rights Protection from import competition
Foreign exchange privileges	Special exchange rates Special foreign debt-to-equity conversion rates Elimination of exchange risks on foreign loans Concessions of foreign exchange credits for export earnings Special concessions on repatriation of earnings and capital

Source: Based on UNCTAD (2004).

growth through foreign investment or to make foreign affiliates in a country undertake activities regarded as desirable (*behavioural incentives*). For this purpose, incentives may focus on support for economic growth indicators, such as job creation, skill transfer, research and development (R&D), export generation and establishment of linkages with local firms.

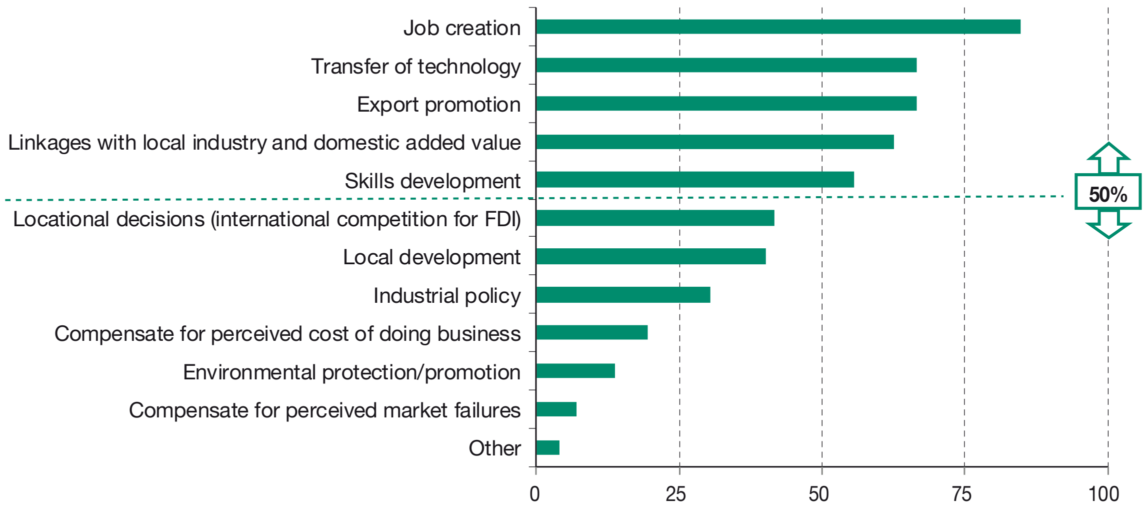
For most countries, job creation is the most important objective of investment incentives. About 85 per cent of IPAs indicated that job creation ranks among their top five objectives (figure III.3), with almost 75 per cent ranking it their primary or secondary objective. In importance, job creation is followed by technology transfer, export promotion, local linkages and domestic value added, and skills development. Just over 40 per cent of respondents indicated that locational decisions and international competition rank among the top five objectives of their incentive policies. Interestingly, this is the case for more than half of IPAs from developed countries but less than one third of those from developing or transition economies. An explanation might be that other objectives, such as technological development, exports and skill development, are already relatively advanced in most developed countries. Finally, two potential objectives – environmental protection and promotion, and local development – do not rank as highly, confirming that there is considerable room for improvement when it comes to connecting incentive strategies with sustainable development goals such as those being discussed for the United Nations post-2015 development agenda (see chapter IV for further details).

Investment incentives are usually conditioned on the fulfilment by the investor of certain performance requirements. The IPA survey shows that such requirements primarily relate to job creation and to technology and skill transfer, followed by minimum investment and locational and export requirements (figure III.4). Environmental protection, along with some other policy objectives, does not rank among the key concerns.

Investment incentives may target specific industries. According to IPAs, the most important target industry for investment incentives is the IT and business services industry. Over 40 per cent of the respondents indicate that this industry is among their top five target industries (figure III.5). Other key target industries include agriculture and hotels and restaurants. Even though renewable energy is among the top target industries, still less than one third of promotion agencies rank it among the top five industries.

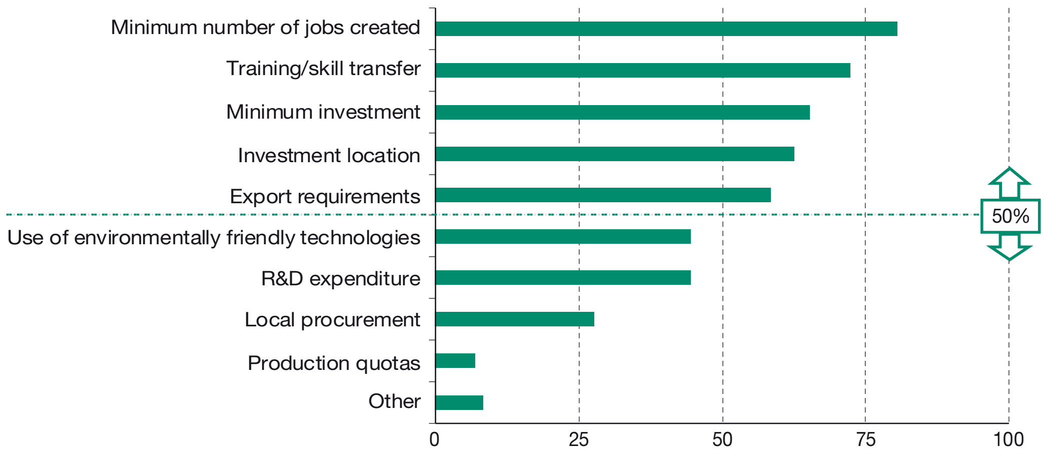
The use of FDI-specific investment incentives differs from country to country. About 40 per cent

Figure III.3. Most important objectives of investment incentives for foreign investors
(Per cent)



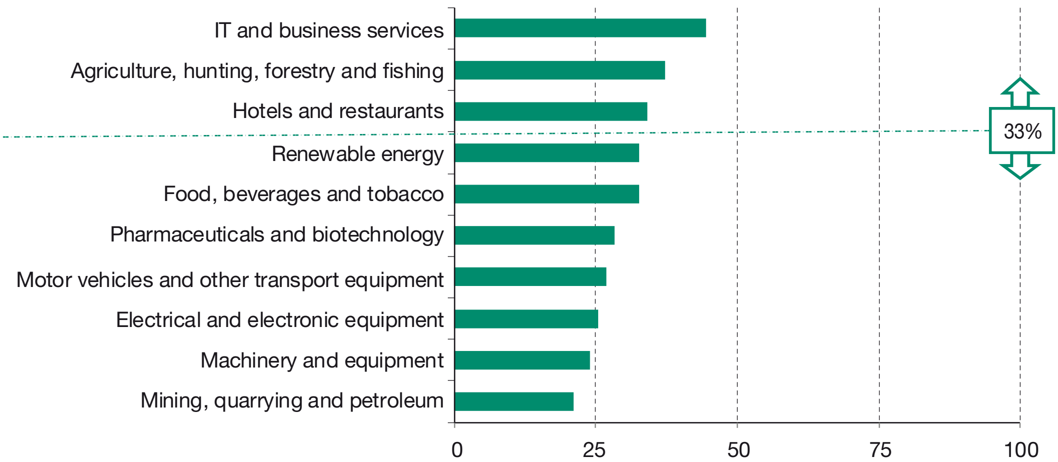
Source: UNCTAD survey of IPAs (2014).
Note: Based on number of times mentioned as one of the top five objectives.

Figure III.4. Most important performance requirements linked to investment incentives for foreign investors
(Per cent)



Source: UNCTAD survey of IPAs (2014).
Note: Based on number of times mentioned as one of the top five performance requirements.

Figure III.5. Top 10 target industries of investment incentive policies
(Per cent)



Source: UNCTAD survey of IPAs (2014).
Note: Based on number of times mentioned as one of the top five target industries.

of IPAs indicated that incentives frequently target foreign investors specifically, while a quarter of the agencies say this is never the case. More than two thirds of IPAs indicated that incentive programmes frequently fulfil their purpose, while 11 per cent indicated that they always do so.

b. Developments related to investment incentives

For the most part, investment incentives have escaped systematic monitoring. Therefore, data on trends in the use of investment incentives and changes in policy objectives – including the promotion of sustainable development – are scarce.

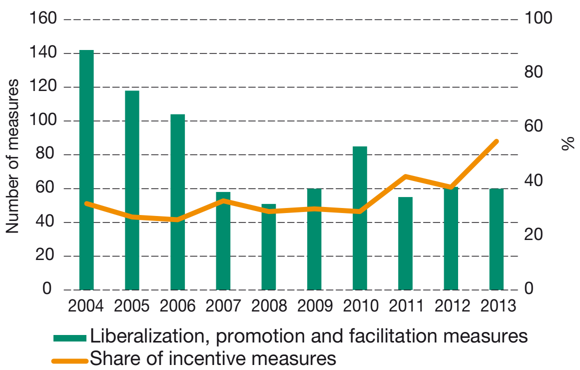
Data from UNCTAD's Investment Policy Monitor suggest that investment incentives constitute a significant share of newly adopted investment policy measures that seek to create a more attractive investment climate for investors. Between 2004 and 2013, this share fluctuated between 26 per cent and 55 per cent, with their overall importance increasing during the period (figure III.6). In 2013, over half of new liberalization and promotion measures related to the provision of incentives to investors. More than half of these incentive measures are fiscal incentives.

Although sustainable development is not among the most prominent objectives of incentive policies, some recent measures cover areas such as health care, education, R&D and local development. For instance, in *Angola*, the Patrons Law of 2012 defines the tax and other incentives available to corporations that provide funding and support to projects related to social initiatives, education, culture, sports, science, health and information technology.[42] In 2010, *Bulgaria* adopted legislation that grants reimbursement of up to 50 per cent for spending on educational and R&D activities, and provides a subsidy of up to 10 per cent for investments in processing industries.[43] In 2011, *Poland* adopted the "Programme to support investments of high importance to the Polish economy for 2011–2020", with the aim of increasing innovation and the competitiveness of the economy by promoting FDI in high-tech sectors.[44] In 2011, the *Russian Federation* exempted education and health-care services from the corporate profit tax under certain conditions.[45]

A number of countries introduced measures to promote local development. For instance in 2012, *Algeria* implemented an incentives regime that is applicable to the wilayas (provinces) of the South and the Highlands.[46] *China* has provided preferential taxation rates on imports of equipment, technologies and materials by foreigners investing in the central and western areas of the country.[47] *Japan* recently designated six SEZs in an attempt to boost local economies. These zones are located around the country and focus on different industries, including agriculture, tourism and R&D.[48]

Among regions, over the last decade Asia has introduced the most policy changes related to investment incentives, followed by Africa (figure III.7). China and the Republic of Korea took the lead in Asia, while Angola, Egypt, Libya and South Africa were the front-runners in Africa. Most of these incentives (75 per cent) do not target any industry in particular; of the industry-specific incentives, most target the services industries, followed by manufacturing.

Figure III.6. Investment incentives as a share of total number of liberalization, promotion and facilitation measures, 2004–2013
(Number of measures and per cent)



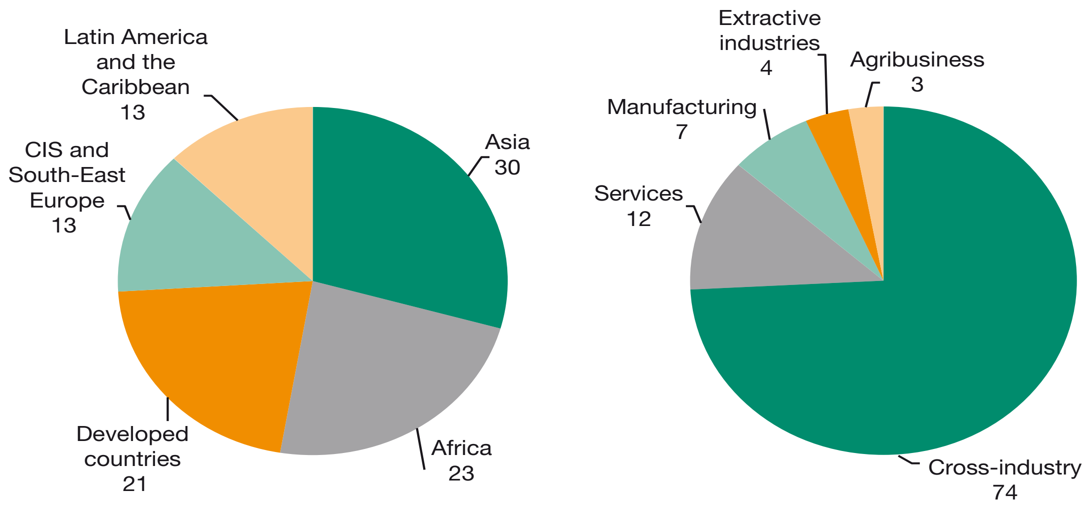
Source: UNCTAD, Investment Policy Monitor.

c. Policy recommendations

Despite the fact that investment incentives have not been a major determinant of FDI and that their cost-effectiveness can be questioned, recent UNCTAD data show that policymakers continue to use incentives as an important policy instrument for attracting FDI. Linking investment incentives schemes to sustainable development goals could make them a more effective policy tool to remedy market failures and could offer a response to the criticism raised against the way investment incentives have traditionally been used (see also chapter IV).

Governments should also follow a number of good practices: (i) The rationale for investment incentives should derive explicitly from the country's development strategy, and their effectiveness should be fully assessed before adoption. (ii) Incentives for specific industries should aim to ensure self-sustained viability so as to avoid subsidizing non-viable industries at the expense of the economy as a whole. (iii) All incentives should be granted on the basis of pre-determined, objective, clear and transparent criteria, offered on a non-discriminatory basis and carefully assessed in terms of long-term costs and benefits prior to implementation. (iv) The costs and benefits of incentives should be periodically reviewed and their effectiveness in achieving the desired objectives thoroughly evaluated and monitored.[49]

Figure III.7. Share of policy changes relating to investment incentives, by region and industry, 2004–2013
(Per cent)



Source: UNCTAD, Investment Policy Monitor.

B. INTERNATIONAL INVESTMENT POLICIES

1. Trends in the conclusion of international investment agreements

a. The IIA universe continues to grow

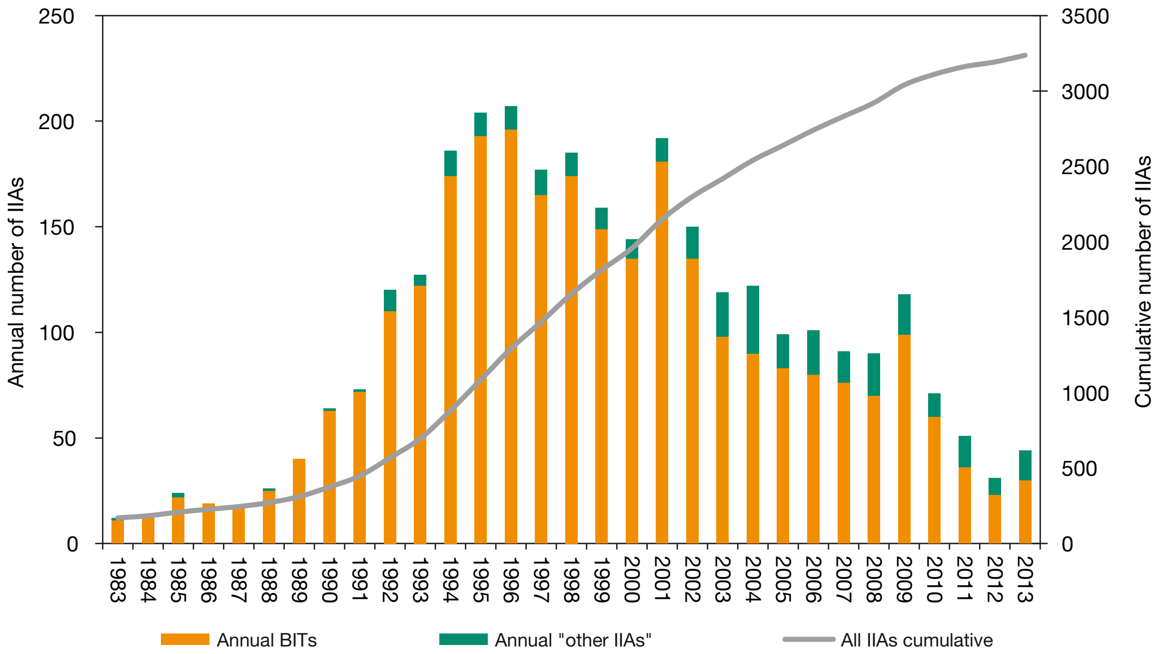
The past years brought an increasing dichotomy in investment treaty making: disengaging and "up-scaling."

The year 2013 saw the conclusion of 44 international investment agreements (IIAs) (30 bilateral investment treaties, or BITs, and 14 "other IIAs"[50]), bringing the total number of agreements to 3,236 (2,902 BITs and 334 "other IIAs") by year-end[51] (figure III.8). Countries that were particularly active in concluding BITs in 2013 include Kuwait (7); Turkey and the United Arab Emirates (4 each); and Japan, Mauritius and the United Republic of Tanzania (3 each). (See annex table III.7 for a list of each country's total number of BITs and "other IIAs".)

In 2013, several BITs were terminated.[52] South Africa, for example, gave notice of the termination of its BITs with Germany, the Netherlands, Spain and Switzerland in 2013;[53] and Indonesia gave notice of the termination of its BIT with the Netherlands in 2014. Once taking effect, the terminated BITs that were not replaced by new ones will reduce the total number of BITs, albeit only marginally (by 43, or less than 2 per cent). By virtue of "survival clauses", however, investments made before the termination of these BITs will remain protected for periods ranging from 10 to 20 years, depending on the relevant provisions of the terminated BITs.[54]

"Other IIAs" concluded in 2013 can be grouped into three broad categories, as identified in *WIR12*:

Figure III.8. Trends in IIAs signed, 1983–2013



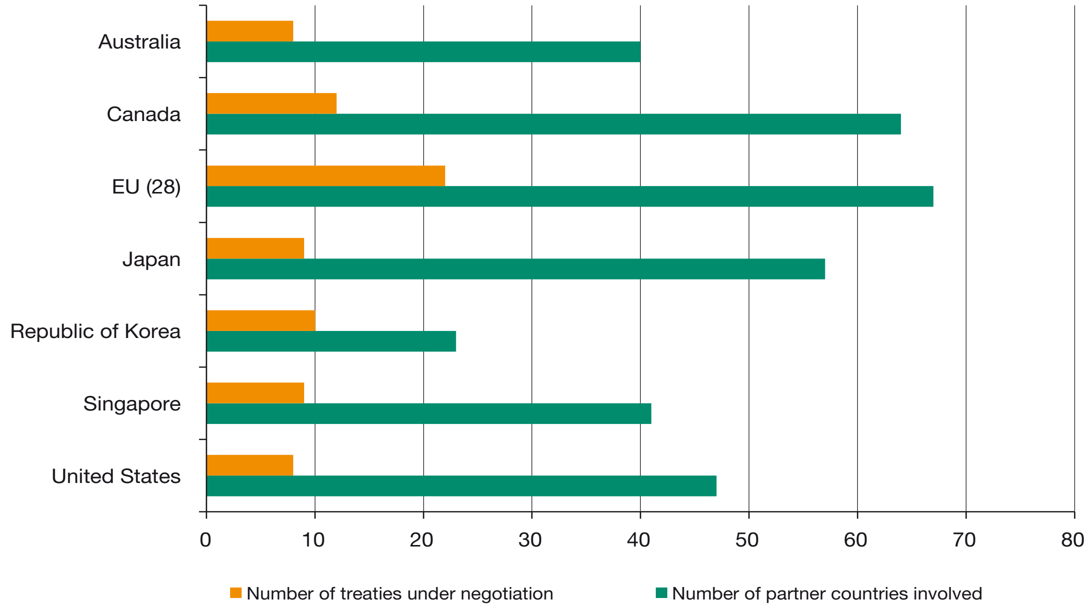
Source: UNCTAD, IIA database.

- *Seven agreements with BIT-equivalent provisions.* The Canada–Honduras Free Trade Agreement (FTA); the China–Iceland FTA; Colombia's FTAs with Costa Rica, Israel, the Republic of Korea, and Panama; and New Zealand's FTA with Taiwan Province of China all fall in the category of IIAs that contain obligations commonly found in BITs, including substantive standards of investment protection and investor–State dispute settlement (ISDS).
- *Two agreements with limited investment provisions.* The China–Switzerland FTA and the EFTA–Costa Rica–Panama FTA fall in the category of agreements that provide limited investment-related provisions (e.g. national treatment with respect to commercial presence or free movement of capital relating to direct investments).
- *Five agreements with investment cooperation provisions and/or a future negotiating mandate.* The Chile–Thailand FTA and the EFTA–Bosnia and Herzegovina FTA, as well as the trade and investment framework agreements signed by the United States with the Caribbean Community (CARICOM), Myanmar and Libya, contain general provisions on cooperation in investment matters and/or a mandate for future negotiations on investment.

An important development occurred in early 2014, when Chile, Colombia, Mexico and Peru, the four countries that formed the Pacific Alliance in 2011, signed a comprehensive protocol that includes a chapter on investment protection with BITs-like substantive and procedural investment protection standards.

In addition, at least 40 countries and 4 regional integration organizations are currently or have been recently revising their model IIAs. In terms of ongoing negotiations of “other IIAs”, the European Union (EU) is engaged in negotiating more than 20 agreements that are expected to include investment-related provisions (which may vary in their scope and depth).[55] Canada is engaged in negotiating 12 FTAs; the Republic of Korea is negotiating 10; Japan and Singapore are negotiating 9 agreements each; and Australia and the United States are negotiating 8 each (figure III.9). Some of these agreements are megaregional ones (see below).

Figure III.9. Most active negotiators of "other IIAs": treaties under negotiation and partners involved
(Number)



Source: UNCTAD, IIA database.
Note: The selection of countries represented in this chart is based on those that are the "most active" negotiators of "other IIAs". It has to be noted that the scope and depth of investment provisions under discussion varies considerably across negotiations.

The agreements concluded in past years and those currently under negotiation are contributing to an "up-scaling" of the global investment policy landscape. This effect can be seen in the participation rate (i.e. the large number of countries that have concluded or are negotiating treaties), the process (which exhibits an increasing dynamism) and the substance of agreements (the expansion of existing elements and inclusion of new ones). All of this contributes to a growing dichotomy in the directions of investment policies over the last few years, which has manifested itself in simultaneous moves by countries to expand the global IIA regime and to disengage from it.

In a general sense, the more countries engage in IIA negotiations, including megaregional ones, the more they create a spirit of action and engagement also for those countries that are not taking part. However, the successful creation of the numerous "other IIAs", BITs and megaregional agreements under negotiation is far from certain. A stagnation or breakdown of one or several of these negotiations could cause the climate for international investment policymaking to deteriorate and effectively hinder the momentum and spirit of action at the bilateral, regional and multilateral levels.

b. Sustainable development elements increasingly feature in new IIAs

New IIAs illustrate the growing tendency to craft treaties that are in line with sustainable development objectives.

A review of the 18 IIAs concluded in 2013 for which texts are available (11 BITs and 7 FTAs with substantive investment provisions), shows that most of the treaties include sustainable-development-oriented features, such as those identified in UNCTAD's Investment Policy Framework for Sustainable Development (IPFSD) and in *WIR12* and *WIR13*.[56] Of these agreements, 15 have general exceptions – for example, for the protection of human, animal or plant life or health, or the conservation of exhaustible natural resources[57] – and 13 refer in their preambles to the protection of health and safety, labour rights, the environment or sustainable development. Twelve treaties under review contain a clause that explicitly

Table III.4. Selected aspects of IIAs signed in 2013

	Policy Objectives																						
Select aspects of IIAs commonly found in IIAs, in order of appearance	Sustainable-development-enhancing features	Focus on investments conducive to development	Preserve the right to regulate in the public interest	Avoid overexposure to litigation	Stimulate responsible business practices	Serbia-United Arab Emirates BIT	Russian Federation-Uzbekistan BIT	New Zealand-Taiwan Province of China FTA	Morocco-Serbia BIT	Japan-Saudi Arabia BIT	Japan-Myanmar BIT	Japan-Mozambique BIT	EFTA-Costa Rica-Panama FTA	Colombia-Singapore BIT	Colombia-Republic of Korea FTA	Colombia-Panama FTA	Colombia-Israel FTA	Colombia-Costa Rica FTA	Canada-United Republic of Tanzania BIT	Canada-Honduras FTA	Benin-Canada BIT	Belarus-Lao People's Democratic Republic BIT	Austria-Nigeria BIT
References to the protection of health and safety, labour rights, environment or sustainable development in the treaty preamble	X	X	X		X	X		X		X	X	X	X		X		X	X	X	X	X		X
Refined definition of investment (exclusion of portfolio investment, sovereign debt obligations or claims of money arising solely from commercial contracts)		X		X		X		X	X					X	X	X	X	X	X	X	X		
A carve-out for prudential measures in the financial services sector			X	X				X		X	X	X	X	X		X	X		X	X	X		
Fair and equitable standard equated to the minimum standard of treatment of aliens under customary international law			X	X				X						X	X	X		X	X	X	X		
Clarification of what does and does not constitute an indirect expropriation			X	X				X						X	X	X	X	X	X	X	X	X	
Detailed exceptions from the free-transfer-of-funds obligation, including balance-of-payments difficulties and/or enforcement of national laws			X	X		X		X	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X
Omission of the so-called “umbrella” clause				X		X	X	X	X	X			X	X	X	X	X	X	X	X	X		
General exceptions, e.g. for the protection of human, animal or plant life or health; or the conservation of exhaustible natural resources	X		X	X				X	X	X	X	X	X	X	X	X	X	X	X	X	X	X	
Explicit recognition that parties should not relax health, safety or environmental standards to attract investment	X	X			X			X		X	X	X	X			X	X	X	X	X	X		X
Promotion of corporate and social responsibility standards by incorporating a separate provision into the IIA or as a general reference in the treaty preamble	X												X			X		X		X	X		
Limiting access to ISDS (e.g., limiting treaty provisions subject to ISDS, excluding policy areas from ISDS, limiting time period to submit claims, no ISDS mechanism)			X	X				X		X	X	X	X	X	X	X	X	X	X	X	X		X

Source: UNCTAD.

Note: This table is based on IIAs concluded in 2013 for which the text was available. It does not include “framework agreements”, which do not include substantive investment provisions.

recognizes that parties should not relax health, safety or environmental standards in order to attract investment.

These sustainable development features are supplemented by treaty elements that aim more broadly at preserving regulatory space for public policies of host countries and/or at minimizing exposure to investment arbitration. Provisions found with differing frequency in the 18 IIAs include clauses that (i) limit treaty scope (for example, by excluding certain types of assets from the definition of investment); (ii) clarify obligations (by crafting detailed clauses on fair and equitable treatment (FET) and/or indirect expropriation); (iii) set forth exceptions to the transfer-of-funds obligation or carve-outs for prudential measures; (iv) carefully regulate ISDS (for example, by limiting treaty provisions that are subject to ISDS, excluding certain policy areas from ISDS, setting out a special mechanism for taxation and prudential measures, and restricting the allotted time period within which claims can be submitted); or (v) omit the so-called umbrella clause (table III.4).

In addition to these two types of clauses (i.e. those strengthening the agreement's sustainable development dimension and those preserving policy space), a large number of the treaties concluded in 2013 also add elements that expand treaty standards. Such expansion can take the form of adding a liberalization dimension to the treaty and/or strengthening investment protections (e.g. by enlarging the scope of the treaty or prohibiting certain types of government conduct previously unregulated in investment treaties). Provisions on pre-establishment and rules that prohibit additional performance requirements or that require the publication of draft laws and regulations are examples (included in, e.g., the Benin–Canada BIT, the Canada–Tanzania FTA, the Japan–Mozambique BIT and the New Zealand–Taiwan Province of China FTA).

The ultimate protective and liberalizing strength of an agreement, as well as its impact on policy space and sustainable development, depends on the overall combination (i.e. the blend) of its provisions (IPFSD). Reconciling the two broad objectives – the pursuit of high standard investment protection and liberalization on the one hand and the preservation of the right to regulate in the public interest on the other – is the most important challenge facing IIA negotiators and investment policymakers today. Different combinations of treaty clauses represent each country's attempt to identify the "best fit" combination of treaty elements.

2. Megaregional agreements: emerging issues and systemic implications

Megaregional agreements are broad economic agreements among a group of countries that together have significant economic weight and in which investment is only one of several subjects addressed.[58] The last two years have seen an expansion of negotiations for such agreements. Work on the Trans-Pacific Partnership (TPP), the EU–United States Transatlantic Trade and Investment Partnership (TTIP) and the Canada–EU Comprehensive Economic and Trade Agreement (CETA) are cases in point. Once concluded, these are likely to have a major impact on global investment rule making and global investment patterns.

During the past months, negotiations for megaregional agreements have become increasingly prominent in the public debate, attracting considerable attention – support and criticism alike – from different stakeholders. Prime issues relate to the potential economic benefits of the agreements on the one hand, and their likely impact on Contracting Parties' regulatory space and sustainable development on the other. In this section, the focus is on the systemic implications of these agreements for the IIA regime.

a. The magnitude of megaregional agreements

Megaregional agreements merit attention because of their sheer size and potentially huge implications.

Megaregional agreements merit attention because of their sheer size, among other reasons (table III.5; see also table I.1 in chapter I). Together, the seven negotiations listed in table III.5 involve 88 countries.[59] In terms of population, the biggest is the Regional Comprehensive Economic

Table III.5. Overview of selected megaregional agreements under negotiation

Megaregional agreement	Negotiating parties	Number of countries	Selected indicators 2012			IIA impact	No.
			Items	Value ($ billion)	Share in global total (%)		
CETA	EU (28), Canada	29	GDP:	18 565	26.1	Overlap with current BITs:	7
			Exports:	2 588	17.5	Overlap with current “other IIAs”:	0
			Intraregional exports:	81		New bilateral relationships created:[a]	21
			FDI inward stock:	2 691	17.6		
			Intraregional FDI inflows:	28			
Tripartite Agreement	COMESA, EAC and SADC	26[b]	GDP:	1 166	1.6	Overlap with current BITs:	43
			Exports:	355	2.4	Overlap with current “other IIAs”:	8
			Intraregional exports:	68		New bilateral relationships created:[a]	67
			FDI inward stock:	372	2.4		
			Intraregional FDI inflows:	1.3			
EU-Japan FTA	EU (28), Japan	29	GDP:	22 729	32.0	Overlap with current BITs:	0
			Exports:	2 933	19.9	Overlap with current “other IIAs”:	0
			Intraregional exports:	154		New bilateral relationships created:[a]	28
			FDI inward stock:	2 266	14.8		
			Intraregional FDI inflows:	3.6			
PACER Plus	Australia, New Zealand, Pacific Islands Forum developing countries	15	GDP:	1 756	2.5	Overlap with current BITs:	1
			Exports:	299	2.0	Overlap with current “other IIAs”:	2
			Intraregional exports:	24		New bilateral relationships created:[a]	103
			FDI inward stock:	744	4.9		
			Intraregional FDI inflows:	1			
RCEP	ASEAN countries and Australia, China, Japan, India, Republic of Korea and New Zealand	16	GDP:	21 113	29.7	Overlap with current BITs:	68
			Exports:	5 226	35.4	Overlap with current “other IIAs”:	28
			Intraregional exports:	2 195		New bilateral relationships created:[a]	5
			FDI inward stock:	3 618	23.7		
			Intraregional FDI inflows:	93			
TPP	Australia, Brunei Darussalam, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, United States and Viet Nam	12	GDP:	26 811	37.7	Overlap with current BITs:	14
			Exports:	4 345	29.4	Overlap with current “other IIAs”:	26
			Intraregional exports:	2 012		New bilateral relationships created:[a]	22
			FDI inward stock:	7 140	46.7		
			Intraregional FDI inflows:	136.1			
TTIP	EU (28), United States	29	GDP:	31 784	44.7	Overlap with current BITs:	9
			Exports:	3 680	24.9	Overlap with current “other IIAs”:	0
			Intraregional exports:	649		New bilateral relationships created:[a]	19
			FDI inward stock:	5 985	39.2		
			Intraregional FDI inflows:	152			

Source: UNCTAD.

[a] “New bilateral relationships” refers to the number of new bilateral IIA relationships created between countries upon signature of the megaregional agreement in question.

[b] Overlapping membership in COMESA, EAC and SADC have been taken into account.

Note: This table does not take into account the negotiations for the Trade in Services Agreement (TISA) which have sectoral focus.

ASEAN: Brunei Darussalam, Cambodia, Indonesia, Lao People’s Democratic Republic, Malaysia, Myanmar, Philippines, Singapore, Thailand and Viet Nam.

COMESA: Burundi, the Comoros, the Democratic Republic of the Congo, Djibouti, Egypt, Eritrea, Ethiopia, Kenya, Libya, Madagascar, Malawi, Mauritius, Rwanda, Seychelles, Sudan, Swaziland, Uganda, Zambia and Zimbabwe.

EAC: Burundi, Kenya, Rwanda, Uganda, the United Republic of Tanzania.

EU (28): Austria, Belgium, Bulgaria, Croatia, Cyprus, the Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, the Netherlands, Poland, Portugal, Romania, the Slovak Republic, Slovenia, Spain, Sweden and the United Kingdom.

Pacific Island Forum countries: Australia, Cook Islands, Federated States of Micronesia, Kiribati, Nauru, New Zealand, Niue, Palau, Papua New Guinea, the Marshall Islands, Samoa, Solomon Islands, Tonga, Tuvalu and Vanuatu.

SADC: Angola, Botswana, the Democratic Republic of the Congo, Lesotho, Madagascar, Malawi, Mauritius, Mozambique, Namibia, Seychelles, South Africa, Swaziland, the United Republic of Tanzania, Zambia and Zimbabwe.

Partnership (RCEP), accounting for close to half of the global population. In terms of GDP, the biggest is TTIP, representing 45 per cent of global GDP. In terms of global FDI inward stock, TPP tops the list.

Megaregional agreements are also significant in terms of the new bilateral IIA relationships they can create. For example, when it is concluded, the Pacific Agreement on Closer Economic Relations (PACER) Plus may create 103 such new relationships.

b. Substantive issues at hand

Megaregional negotiations cover several of the issues typically addressed in negotiations for BITs or "other IIAs". For the investment chapter, negotiators need to devise key IIA provisions, including the clause setting out the treaty's coverage of investments and investors, the treaty's substantive standards of protection (e.g. national treatment, most-favoured-nation (MFN) treatment, FET, expropriation, transfer of funds, performance requirements), its liberalization dimension and its procedural protections, notably ISDS.

Similar to what occurs in negotiations for "other IIAs", megaregional negotiators are also tasked with addressing treaty elements beyond the investment chapter that have important investment implications. The protection of intellectual property rights (IPRs), the liberalization of trade in services and the facilitation of employee work visas are examples in this regard.

In addition to issues that have been considered in numerous past agreements, some megaregional negotiators also face the challenge of dealing with new issues that have emerged only recently. How to address issues related to State-owned enterprises or sovereign wealth funds and how to pursue regulatory cooperation are cases in point.

Table III.6. Selected investment and investment-related issues under consideration in negotiations of megaregional agreements

Selected investment provisions	Selected investment-related provisions
Scope and coverage: the definition of public debt (i.e. whether or not debt instruments of a Party or of a State enterprise are considered covered investments), the type of sovereign wealth funds (SWF) investments that would be protected (e.g. only direct investments or also portfolio investments)	*Regulatory cooperation*: the requirement to provide information and to exchange data on regulatory initiatives (i.e. draft laws/regulations), the requirement to examine – where appropriate – regulations' impact on international trade and investment prior to their adoption, the use of mutual recognition arrangements in specific sectors, the establishment of a regulatory cooperation council
Performance requirements: the prohibition of performance requirements beyond those listed in TRIMs (e.g. prohibiting the use or purchase of a specific (domestic) technology)	*Intellectual property rights (IPRs)*: the property protected (e.g. undisclosed test data), the type of protection offered (e.g. exclusive rights) and the level of protection offered (e.g. extending the term of patent protection beyond what is required by TRIPS)
Standards of treatment: different techniques for clarifying the meaning of indirect expropriation and fair and equitable treatment (FET)	*Trade in services*: the nature of services investment covered ("trade in services" by means of commercial presence) and the relationship with the investment chapter
Investment liberalization: the depth of commitments, the possibility of applying ISDS to pre-establishment commitments	*Financial services*: the coverage of "commercial presence"-type investments in the sector and the promotion of more harmonized regulatory practices
Denial of benefit: a requirement for investors to conduct "substantial business operations" in the home country in order to benefit from treaty protection	*Government procurement*: the obligation to not discriminate against foreign companies bidding for State contracts and the opening of certain aspects of governments' procurement markets to foreign companies
Transfer of funds exceptions: the scope and depth of exceptions to free transfer obligations	*Competition*: provisions on competitive neutrality (e.g. to ensure that competition laws of Parties apply to SOEs)
ISDS: the inclusion of ISDS and its scope (e.g. only for post-establishment or also for pre-establishment commitments), potential carve-outs or special mechanisms applying to sensitive issues (e.g. public debt or financial issues), methods for effective dispute prevention and the inclusion of an appeals mechanism	*Corporate social responsibility (CSR)*: the inclusion of non-binding provisions on CSR
Key personnel: the inclusion of provisions facilitating the presence of (foreign) natural persons for business purposes	*General exceptions*: the inclusion of GATT- or GATS-type general exceptions for measures aimed at legitimate public policy objectives

Source: UNCTAD.

In all of this, negotiators have to carefully consider the possible interactions between megaregional agreements and other investment treaties; between the different chapters of the agreement; and between the clauses in the investment chapter of the agreement in question.

Table III.6 offers selected examples of key issues under discussion in various current megaregional negotiations. The table is not exhaustive, and the inclusion of an issue does not mean that it is being discussed in all megaregional agreements. Moreover, it should be noted that discussions on investment issues are at different stages (e.g. negotiations for the Tripartite agreement plan to address investment issues only in the second phase, which is yet to start). In sum, the table offers a snapshot of selected issues.

Negotiations of megaregional agreements may present opportunities for the formulation of a new generation of investment treaties that respond to the sustainable development imperative. Negotiators have to determine where on a spectrum between utmost investor protection and maximum policy flexibility a particular agreement should be located. This also offers space to apply lessons learned about how IIAs have been implemented and how they have been interpreted by arbitral tribunals.

c. Consolidation or further complexities

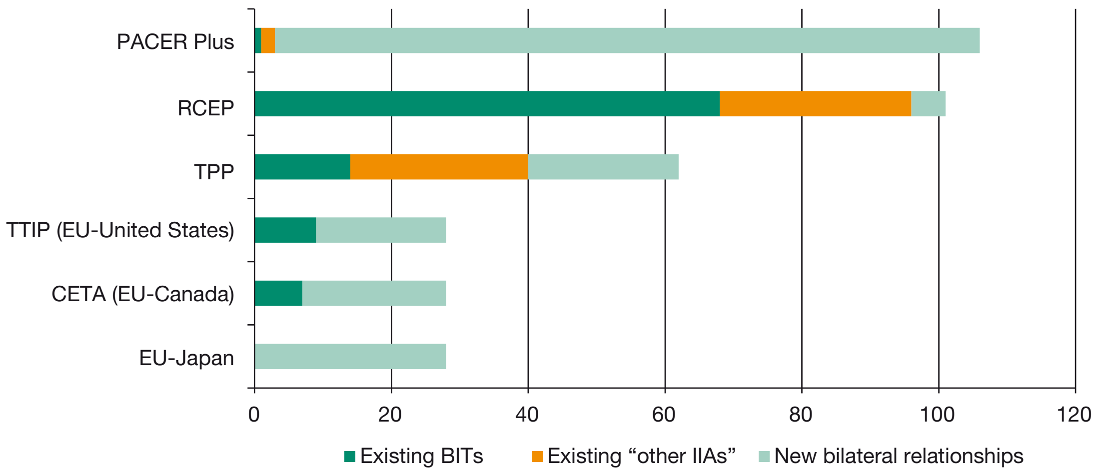
Depending on how they are implemented, megaregionals can either help consolidate the IIA regime or create further complexities and inconsistencies.

Once concluded, megaregional agreements may have important systemic implications for the IIA regime. They offer opportunities for consolidating today's multifaceted and multilayered treaty network. This is not automatic however. They could also create new inconsistencies resulting from overlaps with existing agreements.

Megaregional agreements present an opportunity to consolidate today's network of close to 3,240 IIAs. Overlapping with 140 agreements (45 bilateral and regional "other IIAs" and 95 BITs), the six megaregional agreements in which BITs-type provisions are on the agenda have the potential of transforming the fragmented IIA network into a more consolidated and manageable one of fewer, but more inclusive and more significant, IIAs. At the same time, the six agreements would create close to 200 new bilateral IIA relationships (figure III.10).

The extent of consolidation of the IIA regime that megaregional agreements may bring about

Figure III.10. Existing IIAs and new bilateral relationships created, for six megaregional agreements
(Number)



Source: UNCTAD, IIA database.
Note: "New bilateral relationships" refers to the number of new IIA relationships created between countries upon signature of a megaregional agreement.

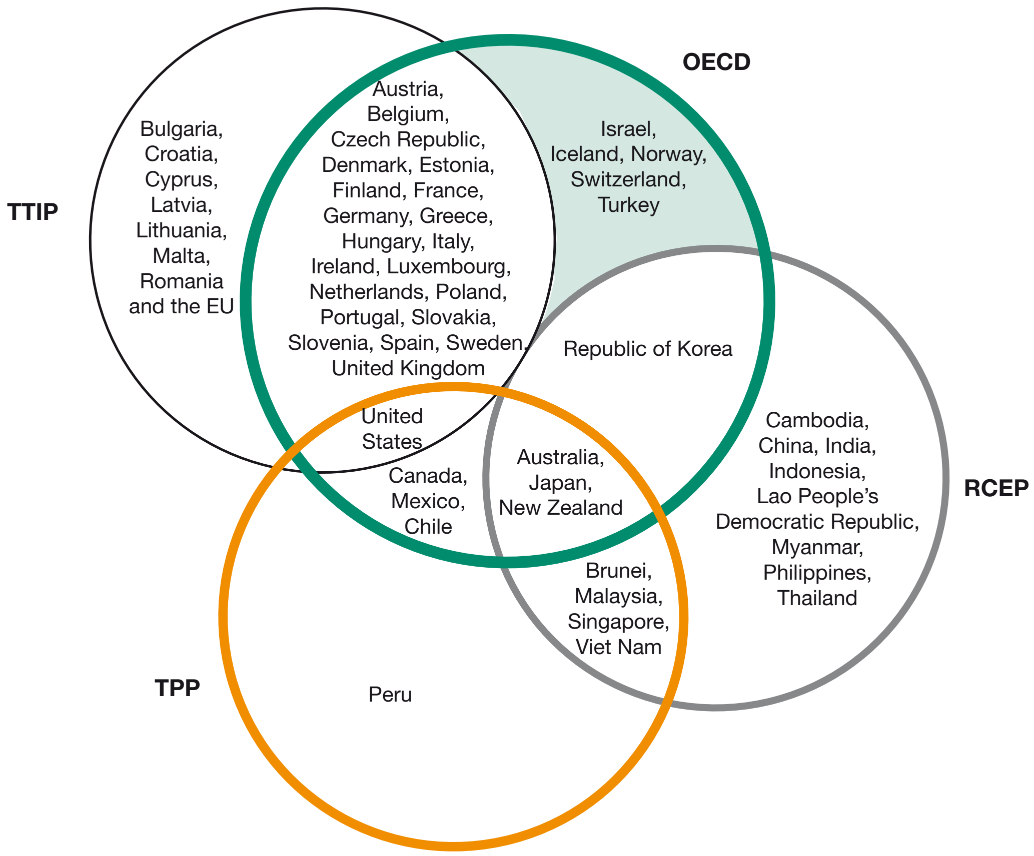
depends crucially on whether the negotiating parties opt to replace existing bilateral IIAs with the pertinent megaregional agreement. The currently prevailing approach to regionalism has resulted in a degree of *parallelism* that adds complexities and inconsistencies to the system (*WIR13*). The coexistence of megaregional agreements and other investment treaties concluded between members of these agreements raises questions about which treaty should prevail.[60] This may change, however, with the increasing number of agreements involving the EU, where prior BITs between individual EU member States and megaregional partners will be replaced by the new EU-wide treaties.

In addition, megaregional agreements may create new investment standards on top of those that exist in the IIAs of the members of the megaregional agreement with third countries – be they bilateral or plurilateral. Insofar as these standards will differ, they increase the chance for "treaty shopping" by investors for the best clauses from different treaties by using the MFN clause. This can work both ways, in terms of importing higher standards into megaregional agreements from other agreements ("cherry-picking") or benefiting from megaregionals' higher standards in other investment relationships ("free-riding").

Several arbitral decisions have interpreted the MFN clause as allowing investors to invoke more investor-friendly language from treaties between the respondent State and a third country, thereby effectively sidelining the "base" treaty (i.e. the treaty between the investor's home and host countries) on the basis of which the case was brought. Therefore, the issue of "cherry-picking" requires careful attention in the drafting of the MFN clause (UNCTAD, 2010; see also IPFSD).

Insofar as "free-riding" and excluding others from the megaregional agreement's benefits are concerned, treaty provisions that except investor treatment granted within a regional economic integration or-

Figure III.11. Participation in key megaregionals and OECD membership



Source: UNCTAD.

ganization from the application of the MFN clause (the so-called regional economic integration organization, or REIO clause) can apply (UNCTAD, 2004).

d. Implications for existing plurilateral cooperation

Megaregional agreements can have implications for existing plurilateral cooperation.

At the plurilateral level, they raise questions about their future relationship with existing investment codes, such as the OECD instruments (i.e. the OECD Codes on Liberalization of Capital Movements and on Liberalization of Current Invisible Operations) and the Energy Charter Treaty (ECT).

Of the 34 OECD members, 22 would be bound by the TTIP's investment provisions, 7 participate in TPP and 4 in RCEP, resulting in a situation where all but 5 (Iceland, Israel, Norway, Switzerland and Turkey) would be party to one or more megaregional agreement (figure III.11). Similarly, 28 ECT members would be subject to the TTIP's provisions, and 2 ECT members are engaged in the TPP and 2 in RCEP negotiations.[61]

Once concluded, some megaregional agreements will therefore result in considerable overlap with existing plurilateral instruments and in possible inconsistencies that could give rise to "free-riding" problems.

Related to this are questions concerning the rationale for including an investment protection chapter (including ISDS) in megaregional agreements between developed countries that have advanced regulatory and legal systems and generally open investment environments. To date, developed countries have been less active in concluding IIAs among themselves. The share of "North-North" BITs is only 9 per cent (259 of today's total of 2,902 BITs). Moreover, 200 of these BITs are intra-EU treaties – many of which were concluded by transition economies before they joined the EU (figure III.12).

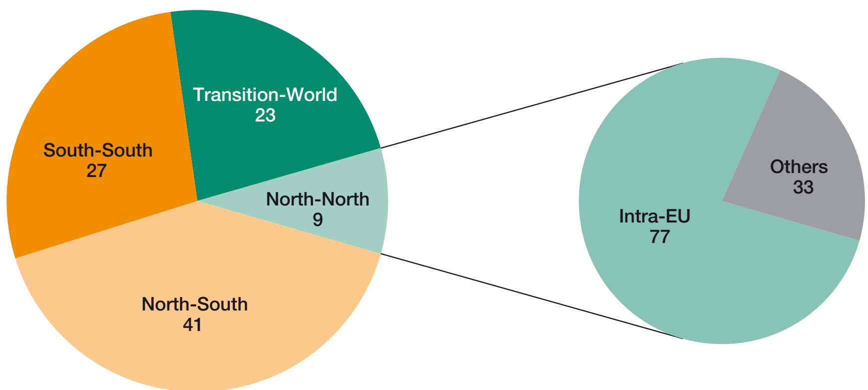
e. Implications for non-participating third parties

In terms of systemic implications for the IIA regime, megaregional agreements may also affect countries that are not involved in the negotiations. These agreements can create risks but also offer opportunities for non-parties.

There is the risk of potential marginalization of third parties, which could further turn them from "rule makers" into "rule takers" (i.e. megaregional agreements make it even more difficult for non-parties to effectively contribute to the shaping of the global IIA regime). To the extent that megaregional agreements create new IIA rules, non-parties may be left behind in terms of the latest treaty practices.

At the same time, megaregional agreements may present opportunities. Apart from "free-riding" (see above), megaregional agreements can also have a demonstrating effect on other negotiations. This

Figure III.12. Share of North-North BITs in global BITs, by end 2013
(Per cent)



Source: UNCTAD, IIA database.

applies to both the inclusion of new rules and the reformulation or revision or omission of existing standards.

Third parties may also have the option of acceding to megaregional agreements. This could, however, reinforce their role as "rule-takers" and expose them to the conditionalities that sometimes emanate from in accession procedures. This is particularly problematic, given that many non-participating third countries are poor developing countries.

* * *

Megaregional agreements are likely to have a major impact on global investment rule making in the coming years. This also includes the overall pursuit of sustainable development objectives. Transparency in rule making, with broader stakeholder engagement, can help in finding optimal solutions and ensuring buy-in from those affected by a treaty. It is similarly important that the interests of non-parties are adequately considered.

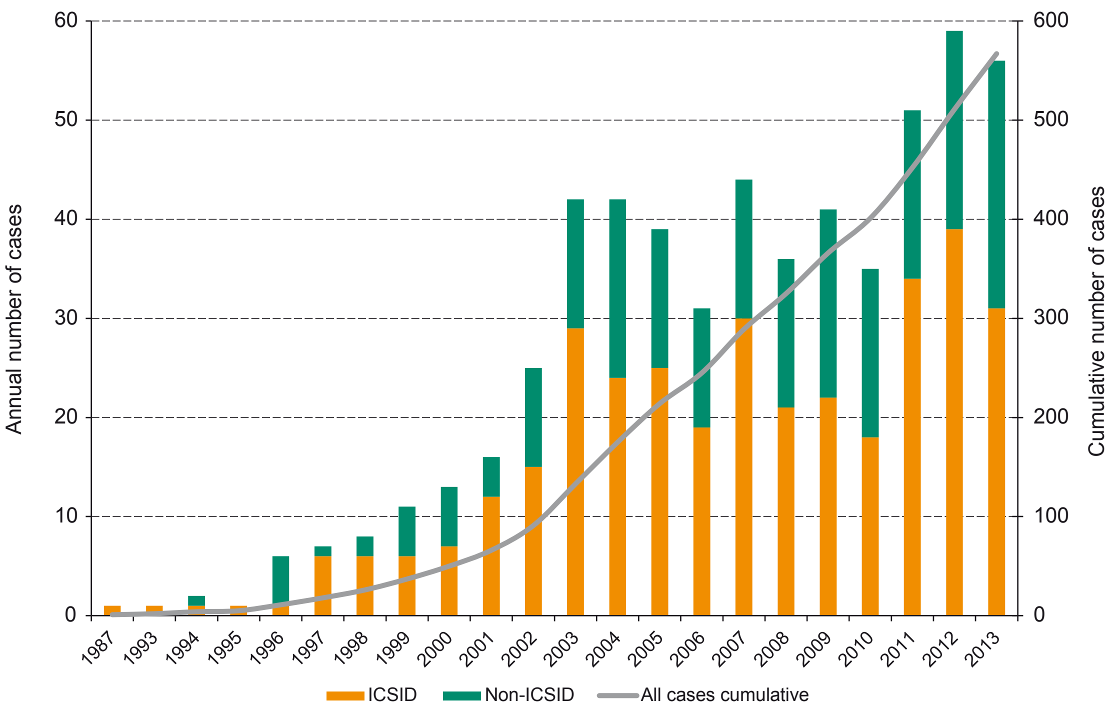
The challenge of marginalization that potentially arises from megaregional agreements can be overcome by "open regionalism". A multilateral platform for dialogue among regional groupings on key emerging issues would be helpful in this regard.

3. Trends in investor–State dispute settlement

With 56 new cases, the year saw the second largest number of known investment arbitrations filed in a single year, bringing the total number of known cases to 568.

In 2013, investors initiated at least 56 known ISDS cases pursuant to IIAs (UNCTAD 2014) (figure III.13). This comes close to the previous year's record-high number of new claims. In 2013 investors brought an unusually high number of cases against developed States (26); in the remaining cases, developing (19) and transition (11) economies are the respondents.

Figure III.13. Known ISDS cases, 1987–2013



Source: UNCTAD, ISDS database.
Note: Due to new information becoming available for 2012 and earlier years the number of known ISDS cases has been revised.

Forty-two per cent of cases initiated in 2013 were brought against member States of the EU. In all of these EU-related arbitrations, except for one, the claimants are EU nationals bringing the proceedings under either intra-EU BITs or the ECT (sometimes relying on both at the same time). In more than half of the cases against EU member States, the respondents are the Czech Republic or Spain.

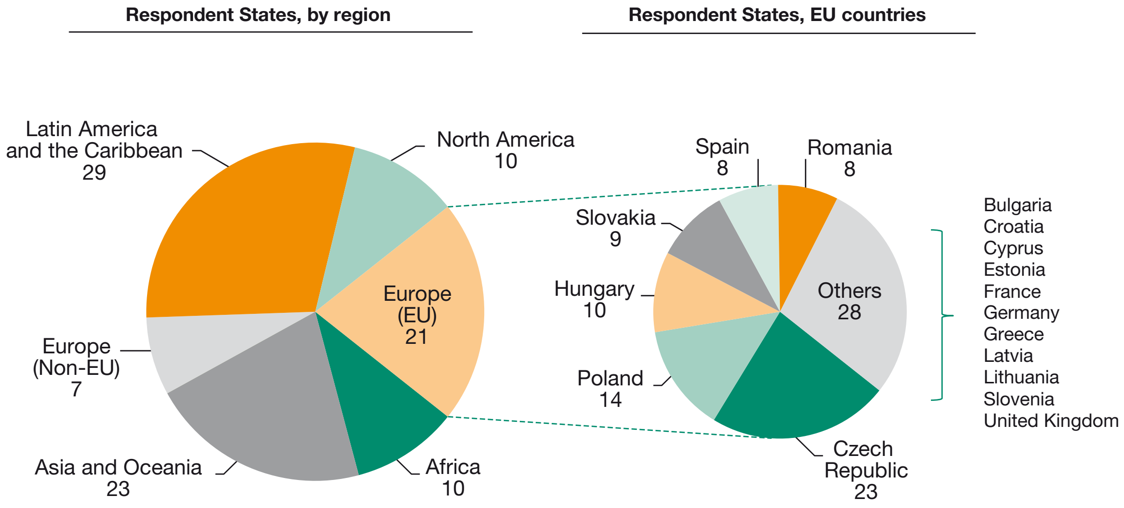
In fact, nearly a quarter of all arbitrations initiated in 2013 involve challenges to regulatory actions by those two countries that affected the renewable energy sector. With respect to the Czech Republic, investors are challenging the 2011 amendments that placed a levy on electricity generated from solar power plants. They argue that these amendments undercut the viability of the investments and modified the incentive regime that had been originally put in place to stimulate the use of renewable energy in the country. The claims against Spain arise out of a 7 per cent tax on the revenues of power generators and a reduction of subsidies for renewable energy producers.

Investors also challenged the cancellation or alleged breaches of contracts by States, alleged direct or de facto expropriation, revocation of licenses or permits, regulation of energy tariffs, allegedly wrongful criminal prosecution and land zoning decisions. Investors also complained about the creation of a State monopoly in a previously competitive sector, allegedly unfair tax assessments or penalties, invalidation of patents and legislation relating to sovereign bonds.

By the end of 2013, the number of known ISDS cases reached 568, and the number of countries that have been respondents in at least one dispute increased to 98. (For comparison, the World Trade Organization had registered 474 disputes by that time, involving 53 members as respondents.) About three quarters of these ISDS cases were brought against developing and transition economies, of which countries in Latin America and the Caribbean account for the largest share. EU countries ranked third as respondents, with 21 per cent of all cases (figure III.14). The majority of known disputes continued to accrue under the ICSID Convention and the ICSID Additional Facility Rules (62 per cent), and the UNCITRAL Rules (28 per cent). Other arbitral venues have been used only rarely.

The overwhelming majority (85 per cent) of all ISDS claims by end 2013 were brought by investors from developed countries, including the EU (53 per cent) and the United States (22 per cent).[62] Among the EU member States, claimants come most frequently from the Netherlands (61 cases), the United Kingdom (43) and Germany (39).

Figure III.14. Respondent States by geographical region and EU in focus, total by end 2013
(Per cent)



Source: UNCTAD, ISDS database.

The three investment instruments most frequently used as a basis for all ISDS claims have been NAFTA (51 cases), the ECT (42) and the Argentina–United States BIT (17). At least 72 arbitrations have been brought pursuant to intra-EU BITs.

At least 37 arbitral decisions were issued in 2013, including decisions on objections to a tribunal's jurisdiction, on the substantive merits of the claims, on compensation and on applications for annulment of an arbitral award. For only 23 of these decisions are the texts in the public domain.

Known decisions on jurisdictional objections issued in 2013 show a 50/50 split – half of them rejecting the tribunal's jurisdiction over the dispute and half affirming it and thereby letting the claims proceed to their assessment on the merits. Of eight decisions on the merits that were rendered in 2013, seven accepted – at least in part – the claims of the investors, and one dismissed all of the claims; this represents a higher share of rulings in favour of investors than in previous years. At least five decisions rendered in 2013 awarded compensation to the investors, including an award of $935 million plus interest, the second highest known award in the history of ISDS.[63]

Arbitral developments in 2013 brought the overall number of concluded cases to 274.[64] Of these, approximately 43 per cent were decided in favour of the State and 31 per cent in favour of the investor. Approximately 26 per cent of cases were settled. In these cases, the specific terms of settlement typically remain confidential.

The growing number of cases and the broad range of policy issues raised in this context have turned ISDS into arguably the most controversial issue in international investment policymaking. Over the past year, the public discourse about the pros and cons of ISDS has continued to gain momentum. This has already spurred some action. For example, UNCITRAL adopted new Rules on Transparency in Treaty-based Investor–State Arbitration on 11 July 2013. Similarly, the Energy Charter Secretariat invited Contracting Parties to discuss measures to reform investment dispute settlement under the ECT. In all of this effort, UNCTAD's IPFSD table on policy options for IIAs (notably section 6) and the roadmap for five ways to reform the ISDS system identified in *WIR13* can help and guide policymakers and other stakeholders (figure III.15).

4. Reform of the IIA regime: four paths of action and a way forward

Four different paths of IIA regime reform emerge: status quo, disengagement, selective adjustments and systematic reform.

The IIA regime is undergoing a period of reflection, review and reform. While almost all countries are parties to one or several IIAs, few are satisfied with the current regime for several reasons: growing uneasiness about the actual effects of IIAs in terms of promoting FDI or reducing policy and regulatory space, increasing exposure to ISDS and the lack of specific pursuit of sustainable development objectives. Furthermore, views on IIAs are strongly diverse, even within countries. To this adds the complexity and multifaceted nature of the IIA regime and the absence of a multilateral institution (like the WTO for trade). All of this makes it difficult to take a systematic approach towards comprehensively reforming the IIA (and the ISDS) regime. Hence, IIA reform efforts have so far been relatively modest.

Many countries follow a "wait and see" approach. Hesitation in respect to more holistic and far-reaching reform reflects a government's dilemma: more substantive changes might undermine a country's attractiveness for foreign investment, and first movers could particularly suffer in this regard. In addition, there are questions about the concrete content of a "new" IIA model and fears that some approaches could aggravate the current complexity and uncertainty.

IIA reform has been occurring at different levels of policymaking. At the national level, countries have revised their model treaties, sometimes on the basis of inclusive and transparent multi-stakeholder processes. In fact, at least 40 countries (and 5 regional organizations) are currently in the process of reviewing and revising their approaches to international-investment-related rule making. Countries have also continued negotiating IIAs at the bilateral and regional levels, with novel provisions and reformulations (table III.4). Megaregional agreements are a case in point. A few countries have walked away from IIAs, terminating some of their BITs or denouncing international arbitration

Table III.7. Four paths of action: an overview

Path	Content of policy action	Level of policy action
Systematic reform	**Designing investment-related international commitments that:** • create proactive sustainable-development-oriented IIAs (e.g. add SDG investment promotion) • effectively rebalance rights and obligations in IIAs (e.g. add investor responsibilities, preserve policy space) • comprehensively reform ISDS (i.e. follow five ways identified in *WIR 13*) • properly manage interactions and foster coherence between different levels of investment policies and investment and other public policies (e.g. multi-stakeholder review)	**Taking policy action at three levels of policymaking (simultaneously and/or sequentially):** • national (e.g. creating a new model IIA) • bilateral/regional (e.g. (re-)negotiating IIAs based on new model) • multilateral (e.g. multi-stakeholder consensus-building, including collective learning)
Selective adjustments	**Pursuing selective changes to:** • add a sustainable development dimension to IIAs (e.g. sustainable development in preamble) • move towards rebalancing rights and obligations (e.g. non-binding CSR provisions) • change specific aspects of ISDS (e.g. early discharge of frivolous claims) • selectively address policy interaction (e.g. not lowering standards clauses)	**Taking policy action at three levels of policymaking (selectively):** • national (e.g. modifying a new model IIA) • bilateral/regional (e.g. negotiating IIAs based on revised models or issuing joint interpretations) • multilateral (e.g. sharing of experiences)
Status quo	**Not pursuing any substantive change to IIA clauses or investment-related international commitments**	**Taking policy action at bilateral and regional levels:** • continue negotiating IIAs based on existing models • leave existing treaties untouched
Disengagement	**Eliminating investment-related commitments**	**Taking policy action regarding different aspects:** • national (e.g. eliminating consent to ISDS in domestic law and terminating investment contracts) • bilateral/regional (e.g. terminating existing IIAs)

Source: UNCTAD.

conventions. At the multilateral level, countries have come together to discuss specific aspects of IIA reform.

Bringing together these recent experiences allows the mapping of four broad paths that are emerging regarding actions for reforming the international investment regime (table III.7):

- Maintaining the status quo
- Disengaging from the regime
- Introducing selective adjustments
- Engaging in systematic reform

Each of the four paths of action comes with its own advantages and disadvantages, and responds to specific concerns in a distinctive way (table III.7). Depending on the overall objective that is being pursued, what is considered an advantage by some stakeholders may be perceived as a challenge by others. In addition, the four paths of action, as pursued today, are not mutually exclusive; a country may adopt elements from one or several of them, and the content of a particular IIA may be influenced by one or several paths of action.

This section discusses each path from the perspective of strategic regime reform. The discussion begins with the two most opposed approaches to investment-related international commitments: at one end is the path that maintains the status quo; at the other is the path that disengages from the IIA regime. In between are the two paths of action that opt for reform of the regime, albeit to different degrees.

The underlying premise of the analysis here is that the case for reform has already been made (see above). UNCTAD's IPFSD, with its principle of "dynamic policymaking" – which calls for a continuing assessment of the effectiveness of policy instruments – is but one example. The questions are not about whether to reform the international investment regime but how to do so. Furthermore, today's questions are not only about the change to one aspect in a particular agreement but about the comprehensive reorientation of the global IIA regime to balance investor protection with sustainable development considerations.

a. Maintaining the status quo

At one end of the spectrum is a country's choice to maintain the status quo. Refraining from substantive changes to the way that investment-related international commitments are made sends an image of continuity and investor friendliness. This is particularly the case when maintaining the status quo involves the negotiation of new IIAs that are based on existing models. Above all, this path might be attractive for countries with a strong outward investment perspective and for countries that have not yet responded to numerous – and highly politicized – ISDS cases.

Intuitively, this path of action appears to be the easiest and most straightforward to implement. It requires limited resources (e.g. there is no need for assessments, domestic reviews and multi-stakeholder consultations) and avoids unintended, potentially far-reaching consequences arising from innovative approaches to IIA clauses.

At the same time, however, maintaining the status quo does not address any of the challenges arising from today's global IIA regime and might contribute to a further stakeholder backlash against IIAs. Moreover, as an increasing number of countries are beginning to reform IIAs, maintaining the status quo (i.e. maintaining BITs and negotiating new ones based on existing templates) may become increasingly difficult.

b. Disengaging from the IIA regime

At the other end of the spectrum is a country's choice to disengage from the international investment regime, be it from individual agreements, multilateral arbitration conventions or the regime as a whole. Unilaterally quitting IIAs sends a strong signal of dissatisfaction with the current regime. This path of action might be particularly attractive for countries in which IIA-related concerns feature prominently in the domestic policy debate.

Intuitively, disengaging from the IIA regime might be perceived as the strongest, or most far-reaching path of action. Ultimately, for inward and outward investors, it would result in the removal of international commitments on investment protection that are enshrined in international treaties. Moreover, this would result in the effective shielding from ISDS-related risks.

However, most of the desired implications will materialize only over time, and only for one treaty at a time. Quitting the system does not immediately protect the State against future ISDS cases, as IIA commitments usually endure for a period through survival clauses. In addition, there may be a need to review national laws and State contracts, as they may also provide for ISDS (including ICSID arbitration), even in the absence of an IIA. Moreover, unless termination is undertaken on a consensual basis, a government's ability to terminate an IIA is limited. Its ability to do so depends on the formulation of the treaty at issue (i.e. the "survival" clause) and may be available only at a particular, limited point in time *(WIR13)*.

Moreover, eliminating single international commitments at a time (treaty by treaty) does not contribute to the reform of the IIA regime as a whole, but only takes care of individual relationships. Only if such treaty termination is pursued with a view to renegotiation can it also constitute a move towards reforming the entire IIA regime.

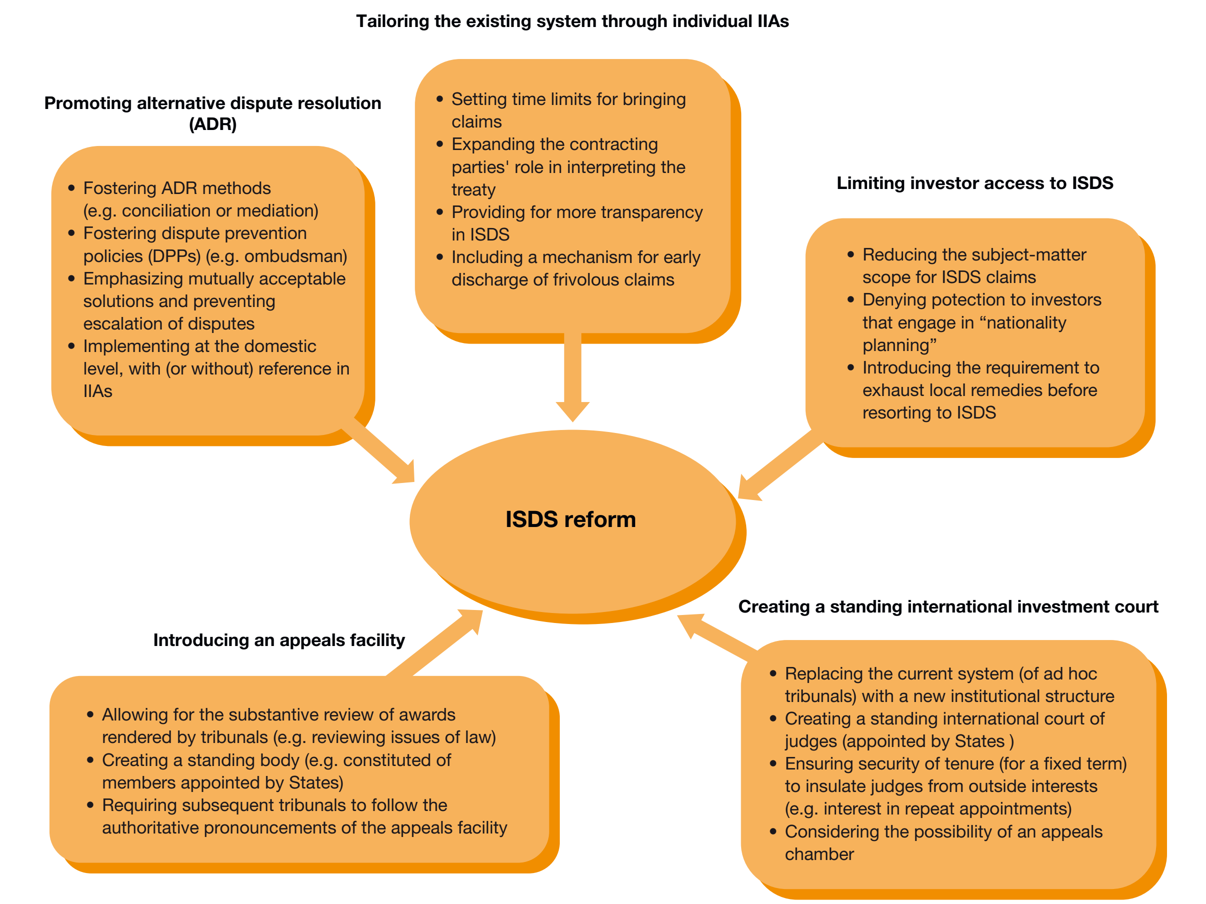
c. *Introducing selective adjustments*

Limited, i.e. selective, adjustments that address specific concerns is the path of action that is gaining ground rapidly. It may be particularly attractive for those countries that wish to respond to the challenges posed by IIAs but wish to demonstrate their continued, constructive engagement with the investment regime. It can be directed towards sustainable development and other policy objectives.

This path of action has numerous advantages. The selective choice of modifications can permit the prioritization of "low-hanging fruit" or concerns that appear most relevant and pressing, while leaving the treaty core untouched (see for example, the option of "tailored modifications" in UNCTAD's five paths of reform for ISDS, figure III.15). It also allows the tailoring of the modification to a particular negotiating counterpart so as to suit a particular economic relationship. Moreover, selective adjustment also allows the testing and piloting of different solutions; the focus on future treaties facilitates straightforward implementation (i.e. changes can be put in practice directly by the parties to individual negotiations); the use of "soft" (i.e. non-binding) modifications minimizes risk; and the incremental step-by-step approach avoids a "big bang" effect (and makes the change less prone to being perceived as reducing the agreement's protective value). Indeed, introducing selective adjustments in new agreements may appear as an appealing – if not the most realistic – option for reducing the mounting pressure on IIAs.

At the same time, however, selective adjustments in *future* IIAs cannot comprehensively address the challenges posed by the *existing* stock of treaties.[65] It cannot fully deal with the interaction of

Figure III.15. Five ways of reform for ISDS, as identified in *WIR13*, illustrative actions



Source: UNCTAD.

treaties with each other and, unless the selective adjustments address the MFN clause, it can allow for "treaty shopping" and "cherry-picking".[66] It may not satisfy all stakeholders. And, throughout all of this, it may lay the groundwork for further change, thus creating uncertainty instead of stability.

d. Pursuing systematic reform

Pursuing systematic reform means designing international commitments that promote sustainable development and that are in line with the investment and development paradigm shift (*WIR12*). With policy actions at all levels of governance, this is the most comprehensive approach to reforming the current IIA regime.

This path of action would entail the design of a new IIA treaty model that effectively addresses the three challenges mentioned above (increasing the development dimension, rebalancing rights and obligations, and managing the systemic complexity of the IIA regime), and that focuses on proactively promoting investment for sustainable development. Systematic reform would also entail comprehensively dealing with the reform of the ISDS system, as outlined in last year's *World Investment Report* (figure III.15).

At first glance, this path of action appears daunting and challenging on numerous fronts. It may be time- and resource-intensive. Its result – more "balanced" IIAs – may be perceived as reducing the protective value of the agreements at issue and offering a less attractive investment climate. Comprehensive implementation of this path requires dealing with existing IIAs, which may be seen as affecting investors' "acquired rights." And amendments or renegotiation may require the cooperation of a potentially large number of treaty counterparts.

Yet this path of action is the only one that can bring about comprehensive and coherent reform. It is also the one best suited for fostering a common response from the international community to today's shared challenge of promoting investment for the Sustainable Development Goals (SDGs).

* * *

A way forward: UNCTAD's perspective

Multilateral facilitation and a comprehensive gradual approach to reform could effectively address the systemic challenges of the IIA regime.

Whichever paths countries take, a multilateral process is helpful to bring all parties together. It also brings a number of other benefits to the reform process:

- facilitating a more holistic and more coordinated approach, in the interest of sustainable development (see chapter IV) and the interests of developing countries, particularly the LDCs;
- factoring in universally agreed principles related to business and development, including those adopted in the UN context and international standards;
- building on the 11 principles of investment policymaking set out in UNCTAD's IPFSD (table III.8);
- ensuring inclusiveness by involving all stakeholders;
- backstopping bilateral and regional actions; and
- helping to address first mover challenges.

Such multilateral engagement could facilitate a gradual approach with carefully sequenced actions. This could first define the areas for reform (e.g. by identifying key and emerging issues and lessons learned, and agreeing on what to change and what not to change), then design a roadmap for reform (e.g. by identifying different options for reform, assessing them and agreeing on a roadmap), and finally implement reform. Naturally, such multilateral engagement in consensus building is not the same as negotiating legally binding rules on investment.

The actual implementation of reform-oriented policy choices will be determined by and happening at the national, bilateral, and regional levels. For example, national input is essential for identifying key and emerging issues and lessons learned; consultations between countries (at the bilateral and regional levels) are required for agreeing on areas for change and areas for disagreement; national

Table III.8. Core Principles for investment policymaking for sustainable development

	Area	Core Principles
1	**Investment for sustainable development**	• The overarching objective of investment policymaking is to promote investment for inclusive growth and sustainable development.
2	**Policy coherence**	• Investment policies should be grounded in a country's overall development strategy. All policies that impact on investment should be coherent and synergetic at both the national and international levels.
3	**Public governance and institutions**	• Investment policies should be developed involving all stakeholders, and embedded in an institutional framework based on the rule of law that adheres to high standards of public governance and ensures predictable, efficient and transparent procedures for investors.
4	**Dynamic policymaking**	• Investment policies should be regularly reviewed for effectiveness and relevance and adapted to changing development dynamics.
5	**Balanced rights and obligations**	• Investment policies should be balanced in setting out rights and obligations of States and investors in the interest of development for all.
6	**Right to regulate**	• Each country has the sovereign right to establish entry and operational conditions for foreign investment, subject to international commitments, in the interest of the public good and to minimize potential negative effects.
7	**Openness to investment**	• In line with each country's development strategy, investment policy should establish open, stable and predictable entry conditions for investment.
8	**Investment protection and treatment**	• Investment policies should provide adequate protection to established investors. The treatment of established investors should be non-discriminatory.
9	**Investment promotion and facilitation**	• Policies for investment promotion and facilitation should be aligned with sustainable development goals and designed to minimize the risk of harmful competition for investment.
10	**Corporate governance and responsibility**	• Investment policies should promote and facilitate the adoption of and compliance with best international practices of corporate social responsibility and good corporate governance.
11	**International cooperation**	• The international community should cooperate to address shared investment-for-development policy challenges, particularly in least developed countries. Collective efforts should also be made to avoid investment protectionism.

Source: IPFSD.

experiences are necessary for identifying different options for reform; and sharing such experiences at the multilateral level can help in assessing different options.

The successful pursuit of these steps requires effective support in four dimensions: consensus building, analytical support, technical assistance, and multi-stakeholder engagement.

- A multilateral focal point and platform could provide the infrastructure and institutional backstopping for *consensus building* activities that create a comfort zone for engagement, collective learning, sharing of experiences and identifyication of best practices and the way forward.
- A multilateral focal point could provide general backstopping and *analytical support*, with evidence-based policy analysis and system-wide information to provide a global picture and bridge the information gap.
- A multilateral focal point and platform could also offer effective *technical assistance*, particularly for low-income and vulnerable developing countries (including LDCs, LLDCs and SIDS) that face challenges when striving to engage effectively in IIA reform, be it at the bilateral or the regional level. Technical assistance is equally important when it comes to the implementation of policy choices at the national level.
- A multilateral platform can also help ensure the *inclusiveness and universality* of the process. International investment policymakers (e.g. IIA negotiators) would form the core of such an effort but be joined by a broad set of other investment-development stakeholders.

Through all of these means, a multilateral focal point and platform can effectively support national, bilateral and regional investment policymaking, facilitating efforts towards redesigning international commitments in line with today's sustainable development priorities. UNCTAD already offers some of these support functions. UNCTAD's 2014 World Investment Forum will offer a further opportunity in this regard.

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38. National Assembly, Act on Supporting the Return of Overseas Korean Enterprises, 27 June 2013.
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40. Of 257 IPAs contacted, 75 completed the questionnaire, representing an overall response rate of 29 per cent. Respondents included 62 national and 13 subnational agencies. Regarding the geographical breakdown, 24 per cent of respondents were from developed countries, 24 per cent from countries in Africa, 21 per cent from countries in Latin America and the Caribbean, 19 per cent from countries in Asia and 8 per cent from transition economies.
41. The survey also included investment facilitation as a policy instrument for attracting and benefiting from FDI. However, as that instrument falls outside the scope of this section, related results have been not been included here.
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49. For more details on policy recommendations, see the National Investment Policy Guidelines of UNCTAD's IPFSD.

50 "Other IIAs" refers to economic agreements other than BITs that include investment-related provisions (e.g., investment chapters in economic partnership agreements and FTAs, regional economic integration agreements and framework agreements on economic cooperation).

51 The total number of IIAs given in *WIR13* has been revised downward as a result of retroactive adjustments to UNCTAD's database on BITs and other IIAs. Readers are invited to visit UNCTAD's expanded and upgraded database on IIAs, which allows a number of new and more user-friendly search options (http://investmentpolicyhub.unctad.org).

52 Of 148 terminated BITs, 105 were replaced by a new treaty, 27 were unilaterally denounced, and 16 were terminated by consent.

53 South Africa gave notice of the termination of its BIT with Belgium and Luxembourg in 2012.

54 Investments made by investors in South Africa before the BITs' termination will remain protected for another 10 years in the case of Spanish investments (and vice versa), 15 years in the case of Dutch investments and 20 years in the cases of German and Swiss investments. Investments made by Dutch investors in Indonesia will remain protected for an additional 15 years after the end of the BIT.

55 This figure includes agreements for which negotiations have been finalized but which have not yet been signed.

56 See annex table III.3 of *WIR12* and annex table III.1 of *WIR13*. Note that in the case of "other IIAs", these exceptions are counted if they are included in the agreement's investment chapter or if they relate to the agreement as a whole.

58 This definition of "megaregional agreement" does not hinge on the requirement that the negotiating parties jointly meet a specific threshold in terms of share of global trade or global FDI.

59 The number avoids double counting by taking into account the overlap of negotiating countries, e.g. between TPP and RCEP or between TTIP and TPP, as well as between countries negotiating one agreement (Tripartite).

60 This is an issue governed by the Vienna Convention on the Law of Treaties.

61 "Membership in the Energy Charter Treaty", as counted here, includes States in which ratification of the treaty is still pending.

62 A State is counted if the claimant, or one of the co-claimants, is a national (physical person or company) of the respective State. This means that when a case is brought by claimants of different nationalities, it is counted for each nationality.

63 *Mohamed Abdulmohsen Al-Kharafi & Sons Co. v. Libya and others*, Final Arbitral Award, 22 March 2013.

64 A number of arbitral proceedings have been discontinued for reasons other than settlement (e.g., due to the failure to pay the required cost advances to the relevant arbitral institution). The status of some other proceedings is unknown. Such cases have not been counted as "concluded".

65 Unless the new treaty is a renegotiation of an old one (or otherwise supersedes the earlier treaty), modifications are applied only to newly concluded IIAs (leaving existing ones untouched).

66 Commitments made to some treaty partners in old IIAs may filter through to newer IIAs through an MFN clause (depending on its formulation), with possibly unintended consequences.