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INVESTMENT PROVISIONS IN ECONOMIC INTEGRATION AGREEMENTS

CHAPTER 5

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V. INTERACTIONS

There are three main types of interactions affecting the investment rules of EIIAs. The first type of interaction occurs between investment rules within the EIIA. The second type of interaction takes place when an EIIA's rules on trade, investment and/or other types of transactions affect related aspects of the same activity. The third type of interaction is between EIIAs and between EIIAs and other types of investment agreements.

A. Interactions between Provisions within EIIAs

As the investment rules of an EIIA become increasingly comprehensive and complex, and especially since investment is only one of various disciplines addressed by these agreements, investment provisions of EIIAs sometimes interact such that the full impact of a provision cannot be determined by reading that provision alone. Such interactions fall into two broad categories. One broad category includes those situations in which different provisions of EIIAs interact to provide meaning to each other and thereby to define the obligations of the parties. A second broad category of interactions includes those situations in which there is overlap and inconsistency between two or more provisions applying to related aspects of the same activity.

1. Interactions between Investment Provisions

The most common types of interactions between investment provisions in an EIIA take place in the context of the first category, that is when two or more investment provisions interact to complement or qualify the obligations of the parties. The first of the situations in which this occurs involves the interaction of the definitions provisions of agreements with the substantive provisions. For example, the expropriation provision found in many EIIAs requires payment of compensation for the expropriation of investment, but the nature of the assets protected by this provision typically can be identified only with reference to the definition of the term "investment".

The second situation involves the interactions of general exceptions with the substantive provisions of the agreements. For example, the expropriation of assets within the definition of "investment" might nevertheless not require the payment of compensation if the seizure of the assets were within a general exception for measures necessary for protecting national security interests. That is, the meaning of a substantive provision, such as the expropriation provision, can be ascertained only by reference to the general exception provisions as well as the definitions provisions. The definitions and general exceptions, moreover, are themselves effectively meaningless until considered with the substantive provisions.

The third situation involves the interaction of the substantive provisions with the dispute resolution mechanisms. For example, some EIIAs contain an investor-State dispute resolution mechanism that applies to disputes involving the provisions of the EIIA. Thus, the disputes that are within the jurisdiction of any tribunal formed in accordance with this provision can be identified only by referring to the relevant substantive provisions. Without the substantive provisions, the dispute resolution provision is meaningless. At the same time, the substantive provisions gain much of their force by the presence of the dispute resolution mechanism.

2. Interactions between Investment and Other Provisions

When investment provisions overlap with other provisions of an EIIA, obvious problems arise if there is inconsistency or conflict between them. One situation in which this might happen occurs in agreements that have a chapter on investment and a separate chapter on trade in services. This situation can give rise to some special complexities because, as has been noted above, the admission and establishment provisions of the investment chapter are more likely to use a negative list approach, while the market access provisions of the trade-in-services chapter are more likely to use a positive list approach. Issues may arise concerning the interaction of the two chapters if the same sector is listed in the annexes to both chapters or in the annexes to neither. In the latter case, for example, the investment chapter would seem to grant a right of establishment in that sector, even though it was in a services sector and no market access commitments had been made in the market access list under the trade-in-services chapter. Another situation occurs in agreements that have a chapter on trade in services generally and additional chapters on trade in certain service sectors, such as financial services.

Several EIIAs contain provisions that explicitly state which chapter shall prevail in the event of any inconsistency. One such provision in an EIIA appears in NAFTA, article 1112(1) of which provides that *"[i]n the event of any inconsistency between this Chapter [on investment] and another Chapter, the other Chapter shall prevail to the extent of any inconsistency"*. Therefore, in the NAFTA, the investment chapter is subordinated to the other chapters. At the same time, however, the NAFTA seeks to ensure that all investments are covered by the investment chapter. Thus, article 1213 provides that the term *"cross-border trade in services"* does not include the provision of services by an investment. Accordingly, an investment of one party that provides services in the territory of another party is covered by the investment chapter, not the services chapter.

The interaction is extremely complex in some recent agreements, such as the Free Trade Agreement between Singapore and the United States. That agreement includes chapters on investment, services and financial services. Article 15.3 of the investment chapter contains the provision found in other NAFTA-inspired agreements, stating that in the event of any inconsistency between the investment chapter and another chapter, the other chapter shall prevail to the extent of any inconsistency. Article 8.1 of the chapter on cross-border trade in services contains the provision, also found in NAFTA, defining cross-border trade in services to exclude services supplied by an investment of one party in the territory of another party. Notwithstanding this general exclusion of investment from the services chapter, article 8.2 states that certain provisions of the services chapter do apply to measures by a party affecting the supply of services in its territory by an investor of the other party or a covered investment. Those provisions that do apply are those on market access, domestic regulation and transparency. Thus, not only do some portions of the services chapter apply to investment affecting cross-border trade in services, but also, under article 15.3, they actually prevail over the investment chapter provisions to the extent of any inconsistency. Article 8.2 also states that the cross-border trade in services chapter does not apply to financial services, except for the provisions on market access, domestic regulation and transparency. Article 15.3 provides that the investment chapter does not apply to financial services either. Thus, financial services, including financial services provided by covered investments, are governed by the financial services chapter. Article 10.1 of the financial services chapter, however, explicitly states that certain provisions of the services and investment chapters do apply to financial services, including those on expropriation, transfers and investor-State dispute resolution.

As this indicates, where there are separate chapters on services and specific service sectors, the tendency is for the more specific chapter to prevail in the event of any inconsistency. This is to be expected because a separate chapter on one sector of the economy, such as financial services, is an indication that that sector raises special concerns. For example, because of the key role that the financial services sector plays in the stability of the entire economy, host States may wish to afford different treatment in that sector than in services sectors generally. If the general services chapter prevailed over the more specific chapter, the host State's purpose of having a separate chapter on a specific sector would be defeated. As the example of the Singapore-United States free trade agreement shows, however, the financial services chapter may well follow the same approach as the general services chapter in many respects.

Another situation in this category occurs where one provision of an EIIA amplifies the effect of another provision. For example, a host State that includes an EIIA with a chapter on trade in services modelled on the GATS may grant market access with certain limitations to service providers in a particular sector of the economy. Once a service provider has established a commercial presence in the host State in accordance with the market access commitment, the commercial presence may also be considered an investment within the meaning of the investment chapter and, therefore, entitled to all of the protections afforded to investment generally. In that situation, the investment chapter has amplified the effect of the market access provisions of the trade-in-services chapter. Indeed, if the definition of "investment" is broad enough, even assets brought into the host State by a cross-border service provider that do not constitute a commercial presence might nevertheless be considered investment and be subject to the investment protection provisions of the EIIA.

Policymakers negotiating an EIIA must be careful to consider the combined effect of different provisions. It must be kept in mind that a transaction that is facilitated, promoted or protected by one provision might also be protected by other provisions, so that the effect of implementing one provision may be trigger the application of other provisions, perhaps in other chapters of the agreement.

Occasionally, EIIAs have provisions intended to prevent one provision from amplifying the effects of other provisions. For example, the NAFTA includes a provision intended to prevent the investment chapter from being applied to services in certain cases. The concern was that financial security that a host State might require a foreign service provider to offer as a condition for being entitled to deliver cross-border services might be defined as investment, resulting in the application of the investment chapter to the service. To prevent that result, Article 1112(2) provides that:

> *A requirement by a Party that a service provider of another Party post a bond or other form of financial security as a condition of providing a service into its territory does not of itself made this Chapter applicable to the provisions of that cross-border service. This Chapter applies to that Party's treatment of the posted bond or financial security.*

In other words, a bond or financial security would be considered investment and protected by the provisions of the investment chapter, but the investment chapter would not, merely by virtue of the posting of the bond, become applicable to the provision of the service.

B. Interactions between Agreements Dealing with Investment

The coexistence of an increasing number of EIIAs and other types of investment agreements inevitably gives rise to multiple interactions between investment rules at all levels. EIIAs sometimes include provisions that address the interaction between the EIIA and another agreement. The most common types of provisions addressing these interactions fall into two categories: provisions aimed at ensuring consistency and those intended to address inconsistencies.

1. Ensuring Consistency

Most commonly, EIIA provisions addressing interactions between agreements assume consistency between the purposes of the EIIA and those of the other agreement, and the EIIA provisions are intended in some way to ensure adherence to, or at least action consistent with the provisions of, the other agreement. Several different approaches can be found in the EIIAs.

a. Concluding another agreement

First, EIIAs sometimes require the parties to conclude another agreement. This approach is typical of EIIAs between the European Community or EFTA and a non-member State in which the parties agree to accede to a number of conventions for the protection of intellectual property. In those situations, the only obligation is to accede to the other agreements. A violation of the other agreements presumably would not also violate the EIIA, except perhaps to the extent that the violation of the other agreement called into question whether the obligation to enter into the other agreement had been performed in good faith.

b. Reaffirming commitments under other treaties

Second, EIIAs sometimes include provisions in which the parties reaffirm commitments under other treaties to which they are already parties. This occurs, for example, in services-related provisions in which parties reaffirm their commitments under the GATS. Thus, article 29 of the European Community's Euro-Mediterranean agreement with Egypt "reaffirms" the parties' GATS commitments, particularly those relating to MFN treatment, and also incorporates the exceptions to MFN treatment provided for by the GATS. This provision presumably refers to evolving commitments under the GATS. That is, the parties reaffirm not only existing GATS obligations, but also future commitments made under the GATS. Similarly, article 12(1) of the Framework Agreement on the ASEAN Investment Area provides that *"Member States affirm their existing rights and obligations under the 1987 ASEAN Agreement for the Promotion and Protection of Investments and its 1996 Protocol"*.

c. Requiring observance of obligations under another agreement

Third, EIIAs sometimes require the parties to observe obligations under another agreement. The European Community has concluded treaties requiring the non-European party to abide by the TRIMs Agreement. For example, article 74 of the association agreement between the European Community and Bulgaria provides that *"Bulgaria shall honour the rules on Trade-*

Related Aspects of Investment Measures (TRIMs)". Similarly, article 17(2) of the Free Trade Agreement between EFTA and the Czech Republic provides that:

> *[t]he States Parties to this Agreement shall accord to each other's nationals treatment no less favourable than that they accord to their own nationals. Exemptions from this obligation must be in accordance with the substantive provisions Article 3 of the TRIPS Agreement.*

Article 17(2) has a parallel provision with respect to MFN treatment. A number of other agreements, negotiated by the EFTA States, include a similar provision, but also provide for national and MFN treatment, subject to exemptions in accordance with the TRIPS Agreement.

The effect of a provision in an EIIA requiring the parties to observe another agreement is to make a violation of the other agreement a violation of the EIIA. This in turn would often permit submission of a dispute involving an alleged violation of the other agreement to the dispute resolution mechanism of the EIIA. Language such as that described in the third approach would seem to have that effect. Language such as that described in the second approach might have it as well. If the other agreement has its own dispute resolution mechanism, presumably the dispute could be submitted to either mechanism, or to both.

d. Incorporating obligations under other agreements: The MFN clause

Fourth, EIIAs may incorporate obligations under other agreements. For example, article 35 of the EFTA free trade agreement with Singapore provides that *"[a]rticles XI and XII of the GATS shall apply to payments and transfers, and to restrictions to safeguard the balance-of-payments relating to trade in services"*. The incorporation may be literal. Article VIII of the ASEAN Framework Agreement on Services provides that:

> *[s]chedules of specific commitments and Understandings arising from subsequent negotiations under this Framework Agreement and any other agreements or arrangements, action plans and programmes arising thereunder shall form an integral part of this Framework Agreement.*

The incorporation may also be quite broad, going beyond a few specific provisions. For example, article XIV of the ASEAN Framework Agreement on Services provides that:

> *[t]he terms and definitions and other provisions of the GATS shall be referred to and applied to matters arising under this Framework Agreement for which no specific provision has been made under it.*

The free trade agreement between the Central American States and Chile incorporate five BITs already concluded between Chile and individual Central American States.

One provision common to EIIAs that, in effect, incorporates the provisions of numerous other treaties is the MFN clause, requiring the host State to provide covered investment with treatment no less favourable than that provided to any other foreign investment. As a result of this provision, the host State is obligated under the EIIA to honour, with respect to covered investments, commitments made with respect to foreign investment in any other agreements. The

obligations under those agreements in effect become obligations under the EIIA (UNCTAD, 1999d).

Alternatively, EIIAs may treat other agreements as baseline agreements setting standards that the EIIAs are intended to exceed. Article IV of the ASEAN Framework Agreement on Services provides that the members shall enter into negotiations:

> *directed toward achieving commitments which are beyond those inscribed in each Member State's schedule of commitments under the GATS and for which Member States shall accord preferential treatment to one another on an MFN basis.*

These commitments are to be set out in a schedule, and under Article X may be modified or withdrawn after three years, provided that compensatory adjustments are made.

Or, the EIIA may treat the other agreement not as a floor, but as a ceiling, setting forth the maximum protection that may be provided under the EIIA. For example, article 51 of the Partnership Agreement between the European Community and the Russian Federation provides that:

> *[t]reatment granted by either Party to the other hereunder shall, as from the day one month prior to the date of entry into force of the relevant obligations of the GATS, in respect of sectors or measures covered by the GATS, in no case be more favourable than that accorded by such first Party under the provisions of the GATS, and this, in respect of each service sector, subsector and mode of supply.*

The balance of the article includes a mechanism under which obligations under the EIIA may be adjusted in the light of the parties' obligations under the GATS.

EIIAs often rely upon institutional arrangements created by other agreements. For example, the ASEAN agreements on investment and services provide that the ASEAN Dispute Settlement Mechanism, created under a separate agreement, shall be utilized to resolve disputes arising under those agreements. An illustration of this approach is article VII(1) of the ASEAN Framework Agreement on Services, which provides that:

> *[t]he Protocol on Dispute Settlement Mechanism for ASEAN shall generally be referred to and applied with respect to any disputes arising from, or any differences between Member States concerning the interpretation or application of, this Framework Agreement or any arrangements arising therefrom.*

To provide flexibility, however, Article VII(2) provides that *"[a] specific dispute settlement mechanism may be established for the purposes of this Framework Agreement which shall form an integral part of this Framework Agreement"*.

2. Addressing Inconsistencies

All of the foregoing provisions assume consistency between the EIIA and another agreement. The question arises, however, as to how to address potentially inconsistent obligations under other agreements. Several approaches can be identified.

a. Commitment not to modify parties' obligations under other agreements

One approach is to provide that the EIIA shall not modify or affect a party's obligations under any other agreement. For example, Article 30 of the EFTA free trade agreement with Singapore provides that:

> *Any such recognition [of credentials and certifications of service providers] conferred by a Party shall be in conformity with the relevant provisions of the WTO and, in particular, Article VII of the GATS.*

Similarly, Article IX(1) of the ASEAN Framework Agreement on Services provides that:

[t]his Framework Agreement or any action taken under it shall not affect the rights and obligations of the Member States under any existing agreements to which they are parties.

A footnote to the provision indicates that "*Existing Agreements are not affected as these have been notified in the MFN Exemption List of the GATS*". Thus, the ASEAN language would preserve any existing inconsistent obligation in another agreement. At the same time, the ASEAN language implies that the parties intend that future inconsistent obligations not be assumed. Specifically, Article IX(2) states that:

> *[n]othing in this Framework Agreement shall affect the rights of the Member States to enter into other agreements not contrary to the principles, objectives and terms of the Framework Agreement.*

b. EIIA provisions to prevail over other agreements

An alternative approach is to stipulate that the EIIA's provisions prevail over those of the other agreement. For example, article 91 of the partnership agreement between the African, Caribbean and Pacific States and the European Community states that:

> *[n]o treaty, convention, agreement or arrangement of any kind between one or more Member States of the Community and one or more ACP States may impede the implementation of this Agreement.*

Note that this provision does not apply to agreements between a party and third countries.

c. Establishing a mechanism for resolving inconsistencies

Yet another approach is not to resolve the inconsistency, but to establish a mechanism for resolving it in the future. For example, article 5 of chapter 17 of the Australia-Singapore free trade agreement provides that:

> *[i]n the event of any inconsistence between this Agreement and any other agreement to which both Parties are parties, the Parties shall immediately consult with each other with a view to finding a mutually satisfactory solution in accordance with customary rules of public international law.*

Thus, in this approach, resolution of any inconsistencies is left to future consultations. This provides flexibility, which may be important because the parties very likely cannot anticipate the inconsistencies that may be discovered later and thus may wish to reserve their position on how conflicts are to be resolved until the specific conflicts have been identified. Of course, consultations may not result in agreement on how to resolve the conflict and the result may be that one party observes the obligations of one agreement and the other party observes the inconsistent obligations of the other agreement, resulting in claims by each that the other has violated one of the agreements and invocation of any State-State dispute resolution mechanisms available, which could result in submissions to different forums and inconsistent results.

d. Termination of a prior inconsistent agreement

Conclusion of an EIIA may even result in the termination of a prior, potentially inconsistent agreement. For example, article 21.4 of the Free Trade Agreement between Chile and the Republic of Korea provides that upon entry into force of the FTA, the BIT between the two parties shall no longer be in effect. Neither shall the rights and obligations derived from the BIT. This latter clause is important because BITs typically provide that the protection they afford shall continue for some period of time, often 10 years, following termination of the agreement. The language of the Chile-Republic of Korea FTA in effect would repeal that provision of the BIT and extinguish rights and obligations intended to survive the termination of the BIT.

e. Requiring the higher level of protection to prevail

In some cases, the provisions of an EIIA and another agreement may be different, though not inconsistent. This occurs, for example, where two investment protection provisions require different levels of protection for investment. In this situation, EIIAs sometimes explicitly require that the higher level of protection provided by the two different agreements be afforded. For example, article 12 of the Framework Agreement on the ASEAN Investment Area, after reaffirming the parties' rights and obligations under the ASEAN Agreement for the Protection and Promotion of Investment and its 1996 Protocol, states that:

> *[i]n the event that this Agreement provides for better or enhanced provisions over the said Agreement and Protocol, then such provisions of this Agreement shall prevail.*

The provision may also contemplate that the other agreement may provide the more favourable treatment, in which case the other agreement should prevail. For example, article I of the Free Trade Agreement between Jordan and the United States states that:

> *This Agreement shall not be construed to derogate from any international legal obligation between the Parties that entitles a good or service, or the supplier of a good or service, to treatment more favorable than that accorded by this Agreement.*

f. Allowing the parties to choose

Alternatively, the agreements may allow a party to choose which agreement shall be applied, where more than one agreement is applicable. For example, article 12 of the Australia-Singapore free trade agreement provides that the investment chapter shall not apply to:

> *a natural person who is a permanent resident but not a citizen of a Party where . . . the provisions of an investment agreement between the other Party and the country of which the person is a citizen have already been invoked in respect of the same matter….*

This provision addresses the situation where a natural person is a permanent resident of a party but a citizen of another State and is protected by investment agreements concluded by both States. If the natural person invokes the protection of the other State's investment agreement, it may not invoke the protection of the investment agreement concluded by the State of which he or she is a permanent resident. In effect, the person may choose to be protected by only one of the two agreements.

In addition to potential conflicts in substantive obligations, EIIAs may have dispute resolution mechanisms that overlap with those under other agreements. This is particularly true with respect to the services provisions that may create obligations similar to those under the GATS and that may therefore give rise to disputes that could also fall within the WTO dispute resolution mechanism. One approach is to allow the parties to select the forum in which the dispute shall be resolved. For example, Article 56 of the EFTA free trade agreement with Singapore provides that:

> *[d]isputes on the same matter arising under both this Agreement and the WTO Agreement, or any agreement negotiated thereunder, to which the Parties are party, may be settled in either forum at the discretion of the complaining Party. The forum selected shall be used to the exclusion of the other.*

Article 56(2) states that "*[b]efore a Party initiates a dispute settlement proceeding under the WTO Agreement against another Party or Parties, or vice-versa, that Party shall notify all other Parties of the intention*".

The EIIA may allow a choice only if both the parties agree. For example, article 17(4)(c) of the Free Trade Agreement between Jordan and the United States provides that:

> *[e]xcept as otherwise agreed by the Parties, a Party may invoke a panel under paragraph 1(c) of this Article for claims arising under Article 4 only to the extent that the same claim would not be subject to resolution through the WTO Understanding on Rules and Procedures Governing the Settlement of Disputes.*

That is, WTO procedures must be followed unless both parties agree otherwise.

g. Including an exception to the MFN clause

Finally, just as an EIIA may amplify the effects of another treaty by requiring that provisions in that other treaty be applied to investments covered by the EIIA, another treaty may amplify the effects of the EIIA. This occurs where obligations under the EIIA are incorporated into another treaty, such as where the other treaty has an MFN clause that requires an EIIA party to afford to the parties to the other treaty the same treatment as it provides to parties to the EIIA. This may be undesirable for the party because the party may have extended favourable treatment to other parties under the EIIA in exchange for certain commitments from those parties under the EIIA that were not made by the parties to the other agreement. A party that wishes to avoid this result should insert into all other investment-related agreements that include an MFN clause an

exception for the EIIA, under which the MFN obligation in that agreement does not apply to treatment afforded under the EIIA. However, this MFN exception would be effective only with respect to newly concluded other investment-related agreements (Karl, 1996).

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VI. POLICY CHALLENGES

The number of EIIAs has increased greatly, especially since the 1990s, and there are indications that it will continue to grow in the near future. Increasingly, EIIAs involve countries with dissimilar economic characteristics and levels of development. A country contemplating the negotiation of an EIIA faces a number of policy challenges, some of which are addressed here.

First, a country wishing to provide investors with assurances of a favourable investment climate may choose to do so through the inclusion of investment provisions in an EIIA or through negotiation of another type of investment agreement. Therefore, an initial issue that arises concerns the nature of the agreement. To some extent, the choice of instruments between an EIIA and another type of IIA, for example BITs, may depend upon a country's objectives in negotiating the agreement. The goal of attracting selected foreign investment by offering certain protections perhaps militates in favour of concluding a BIT type of agreement, while the goal of seeking some level of real integration into the regional or global economy by lowering at least some barriers to the international flow of capital may militate in favour of an EIIA. Certain advantages of negotiating either EIIAs or BITs relate not to the type of agreement but to the number of parties involved (UNCTAD, 1996). One of the main advantages of EIIAs *vis-à-vis* other types of IIA is that, by addressing related economic transactions in a single framework, these agreements can provide policy coherence and coordination in the economic area.

Indeed, as noted in the introduction, the inclusion of investment provisions as part of an economic integration agreement covering trade and other types of economic transactions reflects a desire to expand and deepen integration efforts among a number of economies by facilitating investment flows between the parties. However, EIIAs' approaches to investment issues vary considerably and reflect different visions concerning the policies that will best promote the economic welfare and development of the parties involved. A few EIIAs, particularly some of the EIIAs that include only developing countries and that date from the period before the late 1980s, assume that economic development rests on providing preferential treatment to investment from within the EIIA area. The majority of recent EIIAs, however, including many that involve only developing countries, assume that liberalizing investment flows among different economies will promote economic development by fostering the efficient allocation of resources and augmenting the factors of production available to developing economies.

Second, once the decision to negotiate an EIIA has been made, a country faces a large number of more specific policy choices relating to the inclusion of particular investment provisions. Negotiation of an EIIA does not occur in a vacuum, but in the context of the 218 EIIAs that have already been concluded. Countries will inevitably come to the bargaining table with expectations about what should be included, based on their prior negotiating history or on the prior negotiating history of other States whose practices they consider instructive or wish to emulate.

As has been shown in this study, there are strong regional patterns among EIIAs. For example, a country preparing to negotiate an EIIA with the European Community or with EFTA will very likely find investment liberalization, competition policy and intellectual property protection high on the agenda. A country preparing to negotiate an EIIA with a country from the Americas will find liberalization and intellectual property issues on the agenda, but also issues involving many of the kinds of investment protection provisions found in a traditional BIT. Many factors play a role in choosing a country with which to negotiate an agreement, but these

strong regional preferences are one consideration that may influence the choice of potential treaty partners.

As noted also in the introduction, a key driving force behind the conclusion of EIIAs is the insertion of national economies in the globalization process as a means of counteracting the risk of economic marginalization. Thus, for many developing countries in particular, EIIAs may be considered in themselves a development option. This consideration is of critical importance because, as the process of economic integration through an EIIA intensifies, the lock-in effect of the agreement would affect an increasingly wider range of policies and options, thus limiting the policy space available for the adoption (or reconsideration) of appropriate development-oriented strategies (UNCTAD, 2003a; Abugattas, 2004, p. 3). Thus, developing countries negotiating EIIAs must consider how best to incorporate a development dimension into the agreements. At a basic level, this raises the question of how an EIIA contributes to economic development, a question that may not be answered in the same way for all countries. Some countries may be at a stage of development where they regard rapid and extensive integration into the global economy as an appropriate development strategy and will thus be willing to conclude high-standard agreements that apply equally to all parties. Other countries may be at a stage of economic development where integration must be slower and less extensive. They may wish to conclude agreements that have a narrower scope, fewer or weaker commitments, more exceptions, and transitional periods for implementation, and that apply differently to different parties at different stages of development.

Thus the most important development challenge, especially for the negotiation of future EIIAs involving countries at different levels of development, is to strike a balance between the potential for the EIIA to increase investment flows and the flexibility of countries to pursue their particular policy objectives in the light of their characteristics and changing circumstances. Economic development is more complex than merely increasing the total quantity of resources or ensuring their most efficient use. No country promotes economic development through a purely liberal investment policy. As part of their development policies, countries need to balance a series of potentially conflicting interests, some of which advocate in favour of excluding or regulating foreign investment and others of which may advocate in favour of promoting or protecting international investment flows.

This implies, among other things, that the EIIA needs to allow a sufficient level of policy autonomy to national Governments of member countries to pursue their investment objectives. This autonomy may be best reflected in a number of investment issues on which diverging views exist. These include, notably, the substantive scope of the agreement, whether to afford the right of establishment, the scope of the national treatment provisions, regulation of the use of performance requirements and incentives, and competition policy, because they determine whether, and to what extent, preferences can be given to domestic enterprises. The flexibility instruments alluded to before may by specifically applied to these issues (UNCTAD 2003a, p. 173).

Furthermore, all countries have vital non-economic interests, which may be political, social or cultural, that require priority attention. Investment issues, such as the scope of expropriation actions and the recourse to investor-State dispute resolution, are sensitive because they directly affect the sovereignty of the host country to regulate in the public interest and to adjudicate on national public policy issues. As noted in chapter IV, various solutions to these issues are reflected in existing EIIAs (UNCTAD 2003a, p.171).

Indeed, the negotiation of investment provisions in an EIIA often involves difficult policy issues that touch upon a range of social and environmental concerns traditionally thought to belong to the domestic policy domain. As a result, EIIAs are becoming one of the most visible manifestations of the growing internationalization of the domestic policy agenda. This implies that EIIAs need to reflect in a balanced manner the rights and obligations of foreign investors and states. Failure to address this balance, either within the same instrument or by establishing bridges with other instruments, can have important development implications for host countries.

The key point is that economic development is the goal of every EIIA and development concerns must therefore be addressed in every provision of the agreement, although for different countries those concerns might well be addressed in quite different ways. Thus, the value of a given EIIA must be assessed in the light of all the economic circumstances of each party and that party's own economic development policy.

Third, the growing proliferation of EIIAs and other investment agreements is resulting in a multilayered and multifaceted web of interrelated investment rules and commitments, and this is creating increasing difficulties for the interpretation and application of the rules (see the spaghetti bowl figure (figure I.1)). The types of difficulties that arise with the cross-membership of investment agreements of various types and at various levels have been illustrated in the preceding chapter. Other difficulties arising from the complexity and ambiguity of investment rules at all levels are even more difficult to tackle. Some relate, for example, to the lack of comparability in the scheduling of commitments and reservations. Others refer to the lack of consistency in the implementation of rules requiring national policy changes. Yet other inconsistencies may arise from the application of MFN obligations, as MFN clauses differ in their scope and coverage (UNCTAD, 2004a, pp. 237-238).

Several solutions exist to mitigate some of these problems. However, some of the difficulties are likely to persist, and this raises the broader policy issue of whether the elaboration of investment rules could proceed in a more consistent way through the establishment of adequate interpretation mechanisms and institutions.

Clearly, the difficulties of interpretation and implementation created by the interaction of an increasingly complex web of investment rules are particularly problematic for countries suffering from insufficient human resource and institutional capacity to interpret and implement EIIAs. Unclear and complex rules are likely to translate into lengthy and costly disputes and, again, the most directly affected are likely to be the poorer countries. It is therefore crucially important that countries engaging in the negotiation of an EIIA bear in mind these potential difficulties and make provision for avoiding them. In particular, the provision of technical cooperation to the less developed parties of an EIIA should be an important way of ensuring the accomplishment of the EIIA's goals.

In the final analysis, the fundamental policy question becomes whether the proliferation of EIIAs is likely to result in a large number of countries, especially the poorer countries, facing discrimination and exclusion, or whether EIIAs can contribute to the global expansion of investment flows through investment rules that are clear, predictable, consistent and fair. Some existing implementation and interpretation arrangements are already contributing to the latter. But more institutional efforts might still be needed in that direction. In sum, EIIAs are not a substitute for the lack of a multilateral system in the area of investment — just as they are not a substitute for the multilateral trading system established by the WTO — but, in the absence of

such a system, policymakers need to ensure that the expansion of EIIAs is supported by institutional mechanisms that contribute to the elaboration of a clear, predictable, consistent and fair framework of international investment rules for the benefit of all countries.