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Beiträge zum Transnationalen Wirtschaftsrecht

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Investment Protection under WTO-Law
- New Developments
in the Aftermath of Cancún

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Investment Protection under WTO Law – New Developments in the Aftermath of Cancún

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INHALTSVERZEICHNIS

A. Introduction

After the well-known outcome of Cancún, I would like to concentrate on three essential groups of themes: First, an introduction to Bilateral Investment Treaties as seen from a German viewpoint; second, the structure of a possible multilateral investment agreement as prepared for Cancún, and third, some recent developments since Cancún.

Before starting with the first issue, the Bilateral Investment Treaties, it might be useful to recapitulate the dimensions of world-wide investment flows: The increase from 1980 until today is enormous: About six times the annual percentage increase compared with the world-wide trade increase. Of course it fluctuates, depending on the state of the world-wide economy. It marked an absolute peak in 2000 at 1,380 billion US Dollar (mainly due to Mergers & Acquisitions). In 2002, the total volume of foreign direct investment came 'back to normal' at 651 billion US Dollar, of which 25 per cent went to the developing countries.

The world-wide stock of direct investment in 2002 amounted to 7,000 billion US Dollar, distributed amongst 870,000 foreign companies. The added value of foreign subsidiaries of multinational enterprises comes to about 3,400 billion US Dollar, nearly 50 per cent of the total stock. 53 million employees worked for foreign subsidiaries in 2002 – that is three times more than in 1982.

B. Bilateral Investment Treaties

At present, these direct cross-border investments are protected by a network of over 2300 Bilateral Investment Treaties (BITs) and a vast number of provisions in plurilateral and multilateral treaties. BITs have become established in the last decades as a fair and functioning legal framework for international investments. Germany supports foreign direct investments of German enterprises with more than 115 BITs. In 1959, Germany launched its program of Bilateral Investment Treaties in the form of negotiations with Pakistan. Many German BITs are now already in force in a second updated version.

In addition, these BITs constitute the basis for federal guarantees for German investments against political risks like: expropriation, breach of governmental obligations and restrictions on capital transfer. The insured investments cover at present a total stock of some 15 billion EUR. In 2003 alone, Germany insured investments worth 1,7 billion EUR, mainly in developing and newly industrialised countries. With its federal guarantee scheme, Germany offers one of the world's leading investment insurance programs.

C. Multilateral Investment Agreement

In spite of this well-functioning extensive network of Bilateral Investment Treaties and federal guarantee schemes, secondly, the German Government has always supported the development of a multilateral framework of protection for direct invest-

ment. One basic argument is the complexities and difficulties arising out of, for example, the effects of the Most-Favoured-Nation principle embodied in the more than 2300 BITs now in existence. Thus, Germany welcomed the mandate of a *WTO working group on 'Trade and Investment'* at the 1996 WTO ministerial summit in Singapore (which was renewed and specified in Doha in 2001). Let us recall the historical background as well as the interests involved in the issue of multilateral investment protection:

In terms of history: As early as 1947/48, the Havana Charter included rules on investment, but only the GATT provisions on trade were put into force. In 1998 the OECD failed in its efforts for a 'Multilateral Agreement on Investment' (MAI). To some extent, the various reasons for these failures remain important.

With regard to the interests involved: In general both the industrial and the newly industrialised countries are essentially interested in a multilateral investment agreement in order to provide for greater transparency, predictability and stability as well as for better economic efficiency for investments. This interest is supported by confederations of industries, which have far-reaching expectations, with their main interest in an efficient protection of investments.

On the other side, some developing countries, especially India, Thailand and Malaysia, are rejecting or have reservations about a multilateral investment agreement, as they fear dangers of restrictions on their national sovereignty.

After 7 years, more than 20 meetings in Geneva and on the basis of more than 150 written contributions (60 in the past 18 months alone), the *WTO working group on 'Trade and Investment'* discussed the possible content of a multilateral investment agreement. The group fulfilled its mandate and provided several public and substantial reports on this issue.

D. Possible Structure

Even if Cancún in September 2003 failed to mandate the WTO to negotiate a future multilateral investment agreement (mainly because of issues of agricultural policy) and the outlook for such a multilateral agreement is not really promising at present, I would like to briefly outline the possible structure of such a multilateral agreement. With regard to the 7 subject areas according to the Doha mandate, the state of discussion in the *WTO working group on 'Trade and Investment'* was as follows:

a) In terms of the scope and definition of investment, there was a predominant opinion (with the exception of the US) that only 'long-term cross-border investment' should be protected, in line with the explicit wording of the Doha mandate. The additional concept of sufficient influence on the management of foreign subsidiaries would require – according to an IMF definition – an interest of at least 10 per cent of the share capital of the foreign company. Such a scope of long-term cross-border investment would meet the developing countries' concerns of negative consequences if portfolio investment were also protected; furthermore, long-term investment now already constitutes about 80 per cent of private investment flows in developing countries.

b) Transparency does not only mean the publishing of acts and relevant information in the respective host country, but also 'procedural or administrative transparency'. Such an understanding of transparency would mean an increase in the significance of Bilateral Investment Treaties. Recent analysis in the *World Bank* Report 'Global Prospects 2003' shows the strong influence – alongside predictability and stability – of transparency on the distribution of the international flows of investment. However, the developing countries had reservations about such procedural transparency as they fear that such a wider understanding of transparency could restrict their ability to pursue an independent national policy.

c) With regard to Non-discrimination and

d) Modalities for pre-establishment commitments based on a GATS-type positive list approach, the wording of the Doha mandate already indicates the line of thought. According to such a bottom-up approach for protection against discrimination even in the pre-establishment phase each WTO member could negotiate the particular sectors it will open for foreign investors. Even OECD countries might have requests for exemptions. Clearly, this is not the more desirable top-down approach: However, it would mean a second increase in value compared to the European Bilateral Investment Treaties, which do not offer such a commitment in the pre-establishment phase. But again here, the developing countries were sceptical.

e) The Doha mandate leaves open the question of how the Development Provisions should be considered: For many developing countries it seems to be of decisive importance to have a 'right to regulate in the public interest' or a 'policy space': That would allow for 'screening' and 'controlling' of investment according to their national development policy. In the interest of reaching an agreement a political solution should be found here which still contains the basic principles of investment protection.

f) Concerning Exceptions and balance-of-payments safeguards the principle of free transfer should be guaranteed. It may be amended by exemptions through well-defined 'Balance of Payments Safeguards Clauses': They might follow the relevant regulations in international treaties: Art. 119, 120 EC Treaty; Art. XII GATS; Art. 2104 NAFTA; IMF). A restriction of free transfer should be subject to a notification duty to the WTO (similar to GATT and GATS).

g) Finally, with regard to Consultation and Settlement of Disputes between parties, the European Commission is promoting 'state-to-state' dispute settlement, while for example Pakistan and Malaysia are strictly against it. The questions of whether one should stick to (only) a general 'peer review' or a 'state-to-state' dispute settlement within the WTO framework of dispute settlement (DSU) remained open. However, at present it seems impossible to reach an understanding on 'investor-to-state' arbitration, as embodied in Bilateral Investment Treaties, in the ICSID arbitration of the 1965 ICSID Convention, in the NAFTA

and in the Energy Charter Treaty, desirable as it would be. Finally, the question has to be addressed as to how an accepted dispute settlement mechanism relates to those in Bilateral Investment Treaties.

This is the possible first structure of such a multilateral agreement according to the 7 subject areas of the Doha mandate and the state of discussion in the *WTO working group on 'Trade and Investment'*. It should be noted that the issue of protection against direct and indirect expropriation was not included for reasons of consensus-building in the Doha Mandate – this issue should be addressed in the multilateral negotiations at a later stage.

To summarise the possible advantages of a multilateral framework for investment:

- For potential investors, especially small and medium enterprises, it could offer lasting legal security, protect them against unilateral measures and reduce transaction as well as information costs.
- For smaller developing countries it could help them to achieve a greater share in the world-wide flows of investment.
- Complementary increases compared with our Bilateral Investment Treaties could contain a wider understanding of transparency and a commitment to open markets even in the pre-establishment phase.

So much with regards to the detailed preparations of the WTO working group; nonetheless Cancún failed to provide the WTO with a substantial mandate to negotiate such a multilateral investment agreement.

E. Developments since Cancún

Finally and thirdly I would turn to some recent developments and observations after the failure of Cancún. One essential message of Cancún seems to be that the strict consensus principle will be hard to maintain on these issues among the 148 WTO members. Thus, some initiatives have been signalled to unbundle the Singapore issues and aim in a next step at plurilateral negotiations.

What would such a plurilateral agreement mean? According to Article II:3 WTO Agreement such plurilateral agreements are fundamentally possible, and existing examples include the *Agreement on Trade in Civil Aircraft* or *Agreement on Government Procurement.* Such a plurilateral agreement would only be binding for those WTO members which accept it. However, it can be included in the WTO system exclusively and only by consensus of the Ministerial Conference, Article X:9 WTO Agreement.

If an understanding on such a plurilateral agreement could be reached between a *critical mass* of a representative number of WTO members, it would then depend on whether the remaining WTO members would at least not deny the request to include the plurilateral agreement in the WTO system. The charm of this idea would be that first one begins with (plurilateral) negotiations and then offers the WTO a concrete investment agreement. Here, it would indeed be important to have a representative number of WTO members in the plurilateral negotiation group – for example, alongside the industrial countries those newly industrialised and developing countries that

were also supporting multilateral negotiations – and thus to gain political legitimacy. The WTO members with reservations could at any time join the negotiations or later the agreement.

However, one should keep in mind that with regard to investment in services there is a classic *free rider* problem: Via the GATS Most-Favoured-Nation clause the advantages of such a plurilateral agreement would also have to be unilaterally passed on to those countries that preferred to stay away from the plurilateral agreement. An open question – which has not yet been tackled so far – remains the issue of the transition from bilateral to plurilateral or multilateral agreements. But one could imagine that good and generally accepted solutions to these problems will be possible.

At present (February 2004), the European Commission is sounding out whether these ideas of flexibility – unbundling the Singapore issues and plurilateral negotiations – could be of general acceptance to other WTO members.

F. Conclusion

To sum up, the chances for a multilateral or plurilateral investment agreement are not very bright at present: It is doubtful whether a substantial group of members of WTO could be identified which would promote such plurilateral negotiations to form a *critical mass*. In the overall interest of the positive outcome of the Doha Round and in the light of the difficulties that have arisen in connection with the Singapore issues, the interest of many governments in this respect appears to be clearly more limited than before the Cancún Ministerial summit.

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