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Research and Information System
for the Non-Aligned and
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Investment on the WTO Agenda: A Developing Country Perspective and the Way Forward for the Cancun Ministerial Conference

1. Introduction

The Cancun Ministerial Conference of WTO scheduled to be held in September 2003 will be of critical importance for developing countries. Among other issues that will be taken up for discussion at the Conference will be whether or not to launch negotiations on investment. Investment has emerged as the most contentious in the WTO negotiations. At the Fourth Ministerial Conference of WTO at Doha, the finalization of the draft Declaration was held up because differences between the developed and developing countries on investment issue, among others. The Declaration was adopted only following the clarification by the Chairman of the Ministerial Council to the fact that the decision to launch will be taken at the Fifth Ministerial Meeting subject to an explicit consensus on the desirability of the negotiations and merely on the modalities of negotiations. The developing Countries will need to examine the various pros-and-cons of a multilateral framework of the type that the developed countries are seeking to evolve through multilateral trade negotiations for their process of development. They will also need to think about the form and content of possible multilateral framework on investment, should a negotiating mandate be given by the Ministerial Conference.

Against that backdrop, this paper examines the relevance of a multilateral framework on investment from a developing country perspective in the light of the evidence available on the role of FDI in development. It also suggests the policy options that developing countries may

consider at the Cancun Ministerial Conference on the issue of Trade and Investment. It also reflects on the approaches to make different elements of a possible multilateral framework on investment more pro-development and balanced, in case a negotiating mandate is unavoidable at the Cancun.

The structure of the paper is as follows: Section 2 summarizes the broad trends and patterns in global FDI inflows and highlights the nature of North-South dimension in it. Section 3 presents a brief review of literature on developmental impact of FDI on the host economies and the role of host government policy. Section 4 examines the relevance of multilateral framework on investment. Section 5 discusses the possible positions that developing countries could adopt at the Cancun Ministerial Conference including a possible compromise of negotiating a multilateral framework negotiated outside the Single Undertaking of GATT/WTO. Section 6 discusses the issues involved in incorporating the development dimension in different elements of a possible multilateral framework on investment negotiated outside or within the Single Undertaking of GATT. Finally Section 7 makes a few concluding remarks.

2. The North-South Divide in Investment

The attempt of developed countries to seek a multilateral regime on investment through multilateral trade negotiations is a part of their strategy to secure more favourable conditions for overseas operations of their enterprises that use FDI as a mode of servicing foreign markets more than trade now. FDI flows have expanded at an unprecedented rate during the 1990s becoming the most visible and prominent manifestation of the increasing global integration of economic activity. Compared to the average annual growth of trade in goods and services of about 6-7 per cent over the 1990s, FDI inflows have grown at an average annual rate of 20 per cent over 1991-95 and at 32 per cent during 1996-2000 despite the economic crisis in some important regions of the world. As a result, the magnitude of global FDI inflows has increased from US$ 159 billion in 1991 to $ 1.27 trillion in 2000. To a large extent, the recent growth of FDI flows has been fuelled by cross-border mergers and acquisitions (M&As) in North America and Europe as a part of ongoing wave of industrial restructuring and consolidation. However, FDI has become an increasingly important channel of market servicing as a part of the trend of globalization. Sales of foreign affiliates of corporations were roughly of the same order ($ 2 trillion) as world exports in 1982. By 2000,

the affiliate sales had grown to more than two times of the world exports at $ 15.7 trillion compared to world exports of $ 7 trillion. The bulk of FDI flows originate in developed countries and developing countries are on the receiving end most of the time. Top 10 industrially and technologically most advanced countries account for as much as 74 per cent of FDI outflows. Therefore, the North-South divide is quite prominent in the case of investment.

The North-South divide also becomes apparent from the positions adopted by developed countries at the international negotiations concerning investment. Keeping in mind the increasing importance of FDI as a channel of servicing the markets, a favourable international framework for FDI is seen by developed countries as furthering their commercial interests and national competitiveness. Therefore, developed country governments identify themselves with the investors and have tended to protect their interests at these negotiations. As a part of this developed countries have resisted initiatives of the UN System evolving binding Codes of Conduct on corporations in the 1980s and have, on the other hand, been seeking to evolve an international regime guaranteeing an unfettered movement for their corporations through multilateral trade negotiations. Thus, despite the resistance of developing countries, the Final Act of the Uruguay Round included an Agreement on Trade Related Investment Measures (TRIMs). The TRIMs Agreement requires member countries to phase-out performance requirements relating to trade, such as local content requirements and foreign exchange neutrality. The General Agreement on Trade in Services (GATS) provided a framework for liberalization of trade in services including through cross-border commercial presence which is akin to FDI.

Even without waiting for the mandated review of TRIMs becoming due in 1999, developed countries attempted to widen the scope of multilateral regime on investment beyond what is covered in Agreements on TRIMs and GATS. One such attempt was the initiative to establish a Multilateral Agreement (MAI) under the aegis of OECD launched in 1995. The OECD negotiations on MAI, however, could not be successfully concluded and were abandoned in 1998. The MAI negotiations failed because of the failure of OECD members to reach a consensus on the issue. However, even before the experiences of MAI negotiations in OECD were available, an attempt was made to push the investment issue on the WTO's agenda at the First Ministerial Conference of WTO in Singapore where the EU and Canada proposed to create a Possible Multilateral Framework on Investment (MFI) under the auspices of WTO.

However, given the resistance of developing countries, a negotiating mandate could not be obtained on the subject but a Working Group on Trade and Investment (WGTI) was set up in WTO to study the issue without a negotiating mandate[1]. Before the WGTI's study process could conclude its work and recommend the desirability, if any, of a MFI within WTO's ambit, the EU with the support of other industrialized countries pushed the investment issue for negotiations at the Fourth Ministerial Conference of WTO held in Doha in November 2001. Despite the resistance of developing countries who wanted to first complete the study process at the WGTI before agreeing to a negotiating mandate, the Doha Declaration provided for launch of negotiations on the trade and investment after the Fifth Ministerial Conference 'on the basis of a decision taken, by explicit consensus, at that Session on the modalities of negotiations'[2].

3. Developmental Impact of FDI and the Role of Policy Space

FDI usually flows as a bundle of resources including, besides capital, production technology, organizational and managerial skills, marketing know-how, and even market access through the marketing networks of multinational enterprises (MNEs) who undertake FDI. These skills tend to spill over to domestic enterprises in the host country. Therefore, FDI can be expected to contribute to growth more than proportionately compared to domestic investments in the host country. There is now a body of literature that has analyzed the effect of FDI on growth in inter-country framework and another analyzing knowledge spillovers to domestic enterprises from MNEs (see e.g. De Melo 1997, Kumar and Siddharthan 1997, and Saggi 2000, for recent reviews of literature). However, the mixed findings reached by these studies on the role of FDI inflows in host country growth and on knowledge spillovers from MNEs suggest that these relationships are not unequivocal. The primary consideration for expecting a more favourable effect of FDI on growth is externalities of MNE entry for domestic firms. The externalities such as spillovers may not take place in some cases because of poor linkages with the domestic enterprises or poor absorptive capacity, for instance. FDI projects vary in terms of generation of linkages for domestic enterprises. There is also a possibility of MNE entry affecting domestic enterprises adversely given the market power of their proprietary assets such as superior technology, appeal of brand names and aggressive marketing techniques. Therefore, FDI may crowd-out domestic investment and may thus be immiserizing. Fry (1992), for instance, found FDI to have a significant negative effect on

[1] See Singapore Ministerial Declaration, WT/MIN((96)/DEC dated 18 December 1996.

domestic investment or crowding it out. However, this effect varies across countries and in the Pacific basin countries FDI seems to have crowded-in domestic investment. Similarly, Agosin and Mayer (2000) analyzing the effect of FDI inflows on investment rates in host countries over the 1970-95 period found that FDI crowds-in domestic investment in Asian countries, crowds-out in Latin American countries while in Africa the relationship is neutral. Evidence is also available on the adverse effect of foreign ownership on productivity of domestic enterprises in developing countries[3]. A recent G-24 Working Paper brought out by UNCTAD by Hanson (2000) has also highlighted cases where FDI may have lowered host country welfare. A recent study by Maria Carkovic and Ross Levin of the University of Minnesota has found FDI to be having no independent influence on economic growth of host countries. Kumar and Pradhan (2002) in a recent quantitative study covering a sample of 107 developing countries for the 1980-99 period, corroborate that FDI appears to crowd-out domestic investments in net terms, in general, although some countries have had favourable effect of FDI on domestic investments in net terms suggesting a role for host country policies. Therefore, they inferred that policy flexibility is important for developing countries for benefiting from FDI.

Role of Government Policy and Performance Requirements: Experiences and Evidence[4]

It is clear that the effect of FDI on domestic investments and growth depend very much on the nature or quality of FDI. Certain types of FDI tend to have more favourable developmental externalities than others. In that context attention needs to be paid by host countries to the quality of FDI inflows besides attracting greater magnitudes of FDI. Recent work has shown that host country policies have an important bearing on the quality of FDI inflows received (see Kumar 2002, among others). Governments have employed various measures to improve the overall quality of FDI inflows. These include performance requirements (PRs) like local content requirements (LCRs) on MNE affilaites to intensify generation of local linkages or export obligations for expanding the contribution of FDI to expansion of manufactured exports of developing countries.

Developed countries of today have extensively employed PRs in their process of development especially when they were net importers of capital. For instance, Chang (2002, 2003) documents how USA had all kinds of performance requirements on foreign investors

[2] See Doha Ministerial Declaration adopted on 14 November 2001; WT/MIN(01)/DEC/1.
[3] See Brian Aitken and Ann E. Harrison (1999): 605-618.

when it was a capital-importing country in the nineteenth century. The federal government had restrictions on foreigners' ownership in agricultural land, mining, and logging. It discriminated foreign firms in banking and insurance, while prohibiting foreign investment in coastal shipping, reserved the directorships of national banks for American citizens, deprived the foreign shareholders of voting rights in the case of federally-chartered banks, and prohibited the employment of foreign workers by foreign firms. More evidence on the use of PRs by developed countries in the post-World War II period is available. Countries like Australia, Canada, France, Japan, among others have made extensive use of PRs. For instance, Australia imposed 50 per cent domestic ownership requirements in natural resource projects, and also employed offsets policy under which larger government contracts required new domestic activity of 30 per cent of their import content. Canada enacted a Foreign Investment Review Act (FIRA) in the early 1970s under which an extensive set of PRs (called undertakings) were imposed to ensure 'significant benefit' is reaped by Canada from the operations of FDI. France has imposed an extensive set of PRs on foreign investors depending upon the nationality of the investor, economic growth effects including employment, regional balance and promotion of local R&D; competition to French enterprises, and on balance of payments etc. Japan also imposed PRs at the time of approvals depending upon contribution to technology development, exports or import substitution, competition to Japanese industry, 50 per cent foreign ownership and required the president of the joint venture to be a Japanese. In the United States, CFIUS under the Exon-Florio Amendment, has rejected some proposed takeovers and also at times imposed what amounts to PRs (see Kumar 2003 for a more detailed review).

Many of the developed countries have also imposed LCRs in auto industry until recently. For instance, Italy has imposed 75 per cent local content on Mitsubishi Pajero, US has imposed 75 per cent rule on Toyota Camry and UK 90 per cent on Nissan Primera (Sercovich 1998). Australia imposed 85 per cent local content rule on motor vehicles until 1989 (Pursell 1999).

The form of these PRs employed by developed countries in the 1990s was, however, changed in favour of trade policy measures that achieve objectives similar to those of PRs but are consistent with the provisions of TRIMs. These include rules of origin, screw-driver regulations, voluntary export restraints (VERs) and anti-dumping (Belderboss 1997, Moran

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[4] This section is based on another paper which may referred to for more detailed evidence, Kumar (2003).

1998, Safarian 2002). The US government had employed VERs against Japanese exports of cars in 1981. Subsequently EU has imposed VERs on Japanese exports of consumer electronics. The European Union countries have also extensively used the screw-driver regulations which are in effect like local content regulations to deepen the local commitment of Japanese corporations in consumer goods industries in the past. EU countries have also used anti-dumping measures to regulate imports of cars and other products from Japan and South-east Asia, and the US has aggressively used similar measures in attempting to achieve reciprocity (i.e. 'substantially equivalent competitive opportunities') in trade and investment with Japan and other countries (Safarian 2002). In the US provisions of the Buy American Act have also been used as local content requirements. For instance, in order to qualify as domestic product to claim a 25 per cent price preference under the Buy American Act, a Hungarian manufacturer of buses had to buy US made engines, transmissions, axels and tyres (Krugman and Obstfeld 2000:205).

Even currently the industrialized countries especially the EU and NAFTA member countries, taking advantage of RTA exceptions that are available under Section XXIV of GATT, are effectively using the Rules of Origin to increase domestic value addition. Rules of origin determine the extent of domestic content a product must have to qualify as an internal product in a preferential trading agreement. Hence, they have the same effect as the local content requirements. By now considerable evidence is available on the use of rules of origin by EU and NAFTA countries to increase the extent of localization of production by MNEs supplying to them (see Kumar 2001 for evidence).

The East Asian countries like South Korea have also pushed FDI into high technology and export-oriented sectors with selective policies and PRs until recently. The recent intercountry quantitative studies have shown that the LCRs have helped in deepening the commitment of MNE affiliates with host economies and the export performance requirements have enabled them to get hooked up with global production networks of MNEs (see Kumar 2002). The case study evidence on a number of newly industrializing countries in building internationally competitive modern manufacturing industries such as automobiles with the help of PRs has now been documented (see Kumar 2003).

To sum up the above discussion, FDI inflows may have widely diverging developmental effects on their host countries ranging from highly favourable impact by bringing and

diffusing new technologies and market access, besides creation of output and jobs to crowding-out of domestic investments hence immiserizing effects on host economies. The literature has emphasized on the critical role played by host government policies such as screening mechanisms, performance requirements among others to maximize the contribution of FDI to their development and minimize the negative effects. The developed countries of today have extensively employed policies such as PRs throughout their period of development in one form or the other. On the contrary, developing countries have only recently started to use these policy tools for fostering their industrialization and development. It would follow from this that any attempt to curtail the policy space available to the host governments for regulation of FDI is likely to have a bearing on the quality of FDI. TRIMs Agreement has already reduced this policy space. An attempt is being made developed countries to expand the scope of WTO rules beyond what is covered under TRIMs to further restrict the policy space for developing countries.

4. Relevance of a Multilateral Framework on Investment: A Developing Country Perspective

A basic question before entering into any negotiation on an MFI is to determine to what extent there is a need for a new multilateral instrument on investment, and what its costs and benefits for developing country members may be. Against that backdrop, we now make an assessment of the relevance of MFI from a developing country perspective.

Conceptual Relevance of a GATT-Type Framework on Investment

There is a conceptual basis for trade liberalization on the principle of comparative advantage where countries with different comparative advantages benefit from trading mutually. So developing countries trade their labour and raw material intensive goods with more knowledge and capital intensive goods produced by developed countries. On the other hand, FDI flows emerge because of differences in the levels of development and bundles of created assets. Indeed the theory of international firm explains evolution of a national firm into an international corporation in terms of monopolistic ownership of intangible assets that have revenue productivity abroad and which more than offsets the disadvantages of operating in an alien environment. These advantages include proprietary technology, globally reputed brand names, access to cheaper sources of capital, accumulated experience of organizing complex

tasks, among others[5]. From the start, therefore, MNE entrants enjoy an edge over local enterprises, if there are any existing at all, because of their monopolistic ownership advantages. The margin of the edge enjoyed by them is inversely related with the extent of development of local industrial capabilities and hence level of development. It is particularly wide in low-income countries.

Is WTO a Right Forum for Handling Investment?

The inclusion of investment on the WTO agenda has also been justified on the grounds of trade relatedness of investment. However, the trade – investment link, other than what is covered under TRIMs Agreement, is by no means straightforward. The bulk of FDI flows continue to be market-seeking (or tariff jumping) type and actually substitute trade. Therefore, after taking care of possible trade distorting investment policies under TRIMs Agreement, there is very little justification of including a full-fledged investment agreement in the multilateral 'trade' negotiations. FDI, like domestic investment, is a development and industrialization issue rather than a trade issue. Bringing it on the WTO agenda would unnecessarily diffuse the attention of WTO from its main purpose i.e. trade liberalization. WTO also does not have competence to deal with the investment and development issue. This is clear from the fact that the Working Group on Trade and Investment set up as per the Singapore Meeting in 1996 has not been able to complete its work so far. Sharp differences continue to remain between the Members on all the aspects of a framework including its relevance and the scope and definition.

Is One-size-fits-all FDI Policy appropriate for Countries at Different Levels of Development?

It has been shown in the literature that countries at different levels of development receive different types of FDI (e.g. Porter, 1990; Ozawa, 1992). For instance, a country at the beginning of the factor-driven stage will attract resource-seeking or labour-seeking inward FDI and investments in capital and intermediate goods industries in subsequent stages. Naturally the need for policy framework dealing with FDI would depend upon the level of development. The one-size-fits-all approach to FDI policy that is sought to be evolved through MFI in WTO can not serve the best interests of countries at different levels of development.

[5] See Dunning, 1993; and Caves, 1996, for expositions of theoretical approaches to FDI.

Role of Policy Space in Determining the Developmental Impact of FDI

As observed earlier the host government policies have played an important role in extracting the benefits from FDI in developed and developing countries. The countries that pursued selective policies with respect to FDI, for instance, South Korea, Taiwan and China among other Southeast Asian nations (for instance, in channelling FDI into export-oriented and high technology activities) have had a greater success in achieving their developmental objectives with FDI inflow than those that pursued more open policies such as those in Latin American countries. A multilateral regime will take away the ability of the host governments' to direct FDI in accordance with their development policy objectives and the overall 'quality' of any FDI inflows received is likely to suffer.

Will MFI Expand the Magnitude of FDI Inflows?

Proponents of a GATT-type MFI argue that such a framework would help developing countries to increase their attractiveness to foreign investors. However, as numerous empirical studies have shown, FDI inflows are largely driven by the gravity factors such as market size, income levels, the extent of urbanization, geographical and cultural proximity with the major source countries of FDI, and the quality of infrastructure. The policy factors play a relatively minor role at the margin, holding gravity factors constant (see Correa and Kumar, 2003, for a review of evidence, among others). After harmonization of policy regimes across the world as proposed, the concentration of FDI in the industrialized countries may increase further. The irrelevance of government policy regime as a determinant of FDI inflows is clear from the fact that many African countries that have liberalized their FDI policy as a part of structural adjustment programmes administered by the IMF and the World Bank during the 1980s have failed to receive any significant FDI inflows. On the other hand, some countries with much more restrictive policy framework are able to attract sizeable inflows e.g., China attracting over $ 40 billion worth of FDI inflows every year. Despite the fact that US and China do not even have a bilateral investment treaty, the US is the most important source of FDI in China. The same is the case of Brazil. Therefore, MFI is unlikely to make any difference to the level of FDI inflows while it has the potential to affect their quality.

Is Existing Framework for Investment Protection and Dispute Settlement Inadequate?

A general impression that is created by the protagonists is that an adequate framework for protection of investment and dispute settlement does not exist. This impression is completely

flawed. There exists an elaborate framework for investment protection and dispute settlement at the bilateral as well as multilateral levels. There is an extensive network of bilateral investment promotion and protection agreements or treaties (BIPAs or BITs) between different pairs of countries. By the end of 2001, 2,096 such treaties had been signed by 174 countries. Typically these BITs provide protection and national treatment for investments that have been established in tune with the existing national regulations and policies. Hence, they provide flexibility to host countries to pursue their development policy while at the same time giving a sense of security to foreign investors. BITs are much easier to be concluded compared to a multilateral framework as is clear from the fact that the OECD's negotiations for MAI could not be concluded even though all the negotiating parties were developed countries.

Furthermore, there do exist multilateral instruments for protection and guarantee of international investments. These include Multilateral Investment Guarantee Agency (MIGA) under the World Bank which came into being in 1988. The International Convention of Settlement of Investment Disputes (ICSID) also under the aegis of the World Bank has provided a framework for dispute settlement since mid-1960s, besides the UN Committee on International Trade Law (UNCITRAL), and International Chamber of Commerce (ICC) (see Correa and Kumar 2003 for more details).

Finally, contrary to the general impression created by the proponents of MFI, the bilateral investment treaties would still be needed even with a multilateral agreement just as the presence of GATT in trade in good has not substituted the need for bilateral trade agreements.

Balance of Investors' and Host Country Interests

Proponents of MFI are seeking to protect only the rights of investors or corporations. Nothing is being proposed in terms of their obligations or the responsibilities or any other provisions concerning protection of host country interests. FDI flows are generally undertaken by MNEs that command enormous resources and power granted by their gigantic and global scales of operation that are larger than the economies of many of the countries they operate in and was growing faster than size of the economies. This enormous power can be misused to pursue restrictive business practices (see Muchlinsky, 1999: 6-7, for examples of abuses of this power). The glaring lack of a binding international regulation of activities of international corporations has often been noted over the past decade. For instance, the Bhopal tragedy where

the concerned MNC sought to shirk away from the liability arising from actions of its majority owned subsidiary is a case in point. The practice of manipulation of transfer prices for shifting funds across countries to evade taxes is also well known. Furthermore, while the ability of the host governments to impose performance obligations is sought to be curbed, that of corporations to impose restrictive clauses on their subsidiaries that are often trade distorting, is not regulated. According to Bergsten and Graham (1992) an 'ideal accord would grant specific rights to, and simultaneously place certain obligations on, three sets of actors: (a) governments of nations that are host to FDI (including subnational governmental entities), (b) governments of nations that are home to international corporations, and (c) international corporations themselves.'

Balance between Interests of Capital and Labour Exporters

Capital and labour are two mobile factors of production. The proposed framework on investment proposes to liberalize capital movements without providing for the labour mobility and hence would create asymmetry. The economic arguments for free movement of labour are no weaker than those for the free movement of capital (Hoekman and Saggi, 2000). As Panagariya (2000) argues 'symmetry dictates that alongside investment agreement, there also be an agreement on the movement of natural persons. Since the current ethos is unlikely to permit the inclusion of such proposals into the negotiating agenda, there is no reason for inclusion of investment into the agenda either.' The regional blocs such as the EU that provide for free capital movement between the member states generally also provide for labour mobility across the member states.

An evidence of the reluctance of developed countries to liberalize the labour mobility is clear from the lack of commitments made by them in respect of Mode 4 in the GATS that covers the supply through movement of natural persons. Almost all of the market access commitments made by developed countries in respect of market access are subject to limitations such as economic needs test or subject to a specified proportion of the work force. Similarly, 83 per cent of commitments in respect of national treatment made by developed countries are also subject to limitations such as tax treatment or other discriminating treatment that are some times non-transparent. This situation prevails notwithstanding Article IV.1(c) of GATS, viz. "the liberalization of market access in sectors and modes of supply of export interest' to developing countries" (see RIS 2002 for more details). The restrictions on movement of natural persons across regions impose a cost on developed and developing economies far exceeding that of trade restrictions on goods. Winters et al. (2002) have estimated in the

framework of a CGE model that an increase in developed countries' quotas on both skilled and unskilled temporary workers equivalent to just 3 per cent of their labour force will lead to over US$ 150 billion of welfare gains for developed and developing economies.

5. The Way forward for the Cancun Ministerial Conference

The foregoing review of the merit of the proposed framework suggests that a GATT-type multilateral framework on investment (MFI) is justified on neither conceptual or policy grounds. The reduced flexibility to regulate FDI inflows in tune with their development policy objectives resulting from agreeing to a multilateral framework could lead to considerable loss of welfare in developing countries. While the proposed MFI would reduce the policy space available to developing countries, it does not offer any thing in return for this to them. Neither they can expect more inflows of FDI nor any reciprocity in other sectors such as labour mobility. In view of this developing countries resisted a negotiating mandate on investment at the Doha Ministerial Conference held in November 2001.

The final Doha Declaration provides as follows.

> Relationship between trade and investment
>
> 20. Recognizing the case for a multilateral framework to secure transparent, stable and predictable conditions for long-term cross-border investment, particularly foreign direct investment, that will contribute to the expansion of trade, and the need for enhanced technical assistance and capacity-building in this area as referred to in paragraph 21, *we agree that negotiations will take place after the Fifth Session of the Ministerial Conference on the basis of a decision to be taken, by explicit consensus, at that session on modalities of negotiations* (emphasis added).

The Doha Declaration only recognizes a 'case' for but not the 'need' for a multilateral framework. Although the language of the Declaration talks of the need for a consensus on the modalities of negotiations, the Chairman's understanding and clarification that enabled the adoption of the Declaration at the Doha Ministerial suggests that the negotiating mandate would itself be subject to an explicit consensus:

> I would like to note that some delegations have requested clarification concerning paragraphs 20, … of the draft declaration. Let me say that *with respect to the reference to an 'explicit consensus'* being needed, in these paragraphs, for a decision to be taken at the Fifth Session of the Ministerial Conference, *my understanding is that, at that session, a decision would indeed need to be taken by explicit consensus, before negotiations on trade and investment … could proceed.*
>
> *H.E. Youssef Hussain Kamal, Qatari Finance, Economy and Trade Minister, Chairman of Doha Ministerial Conference at the closing plenary session, 14 November 2001* (emphasis added).[6]

Going by the Chairman's understanding the negotiating mandate on investment is yet to be obtained at the Fifth Ministerial scheduled to be held in Cancun in September 2003. In light of that this Section reviews the various options that developing countries can consider at the Cancun Ministerial in September 2003.

In the light of the Doha Mandate, there are three possible options for developing countries as follows.

Most Preferred Option: Resist a Negotiating Mandate at Cancun

Keeping in mind the Chairman's clarification, it is still possible to resist a negotiating mandate on investment. For this to happen the coalition of developing countries would be of critical importance. Developing countries will have to argue their case effectively. They could also draw attention to the practical problems involved in arriving at a consensus on the subject in the light of the OECD's MAI experience when a relatively homogenous group of 29 OECD Member States failed to arrive at a consensus even after negotiations lasting over three years. An earlier attempt to evolve a multilateral framework on investment viz. the UN Code of Conduct on TNCs similarly could not be concluded successfully despite protracted negotiations lasting over the 1977-1992. In a forum like WTO whose membership covers the entire spectrum of high income, middle income, low income and least developed countries, possibilities of arriving at a consensus would appear to be abysmally low. The potential cost in terms of world development and welfare could be substantial while promise of gains in negligible, if at all. Instead developing countries could seek a review of the reasons for failure

[6] http://www.wto.org/english/thewto_e/minist_e/min01_e/min01_chair_speaking_e.htm#clarification

of OECD's MAI and the lessons learnt from that experience as a part of the ongoing study process launched at the Singapore Ministerial in the form of WGTI. This option would be by far the most desirable from a developing country point of view. But it would also be most challenging to achieve given the serious pursuit of developed countries of MFI. Yet, it is feasible depending upon the ability of developing countries to form a coalition on the issue. The recent statements issued by the Trade Ministers of the Least Developed Countries (at their Meeting in Dhaka) and of the African Union Countries (at their Meeting in Mauritius) have expressed their opposition to a negotiating mandate on the Singapore issues including investment.

A Compromise Solution: A Multilateral Treaty on Investment Negotiated Outside WTO

In case developed countries persist with their demand for MFI, a compromise solution could be a multilateral treaty on investment negotiated outside the Single Undertaking of WTO. The objective of proponents of MFI is 'to secure transparent, stable and predictable conditions' for cross-border investments particularly FDI, that can be well served by a freely standing independent multilateral treaty on investment negotiated within the United Nations framework like many other international treaties such as a the Law of the Sea, that have served their purpose well. An independent Multilateral Investment Treaty (MIT) could be modeled in large part on the Bilateral Investment Promotion and Protection Treaties (BIPAs) that provide protection to investments approved under the existing policies. It could also cover some provisions on the obligations of investors among other provisions that are considered necessary. It could link itself with the existing institutional infrastructure on investment protection and settlement of investment disputes in the framework of ICSID, UNCITRAL, ICC and MIGA. Developing countries could argue that WTO does not have necessary expertise to deal with investments which is more a subject dealt by finance ministries or industry ministries and not by the trade diplomats. UNCTAD could probably be a more appropriate forum having inherited the United Nations Commission on TNCs. UNCTAD is also well placed to put development dimension at the core of a MIT.

In case there is an agreement to negotiate a treaty on investment outside the WTO, one alternative could be to resurrect the draft UN Code of Conduct on TNCs which could be adopted with minor amendments. The Draft UN Code was negotiated in the protracted negotiations over the 1977-1992 period. The draft Code represents a balanced approach to a multilateral framework providing the rights and obligations of investors and the host

governments (see Correa and Kumar for more details). The Draft Code could not be adopted because of the differences between developed and developing countries on its legal status and was abandoned in 1992. In view of the fact that considerable negotiating effort has been spent in refining different elements, its balanced treatment of host country, home country and investor interests, and its ability to provide a stable, predictable and transparent framework for FDI, it would serve the objective of both developed and developing countries very ably. It was negotiated within the negotiating platform of the UN Commission on TNCs which is currently serviced by UNCTAD. UNCTAD has the capability to provide the Secretariat of the Code and service its implementation given its work on investment.

The Last Resort: Negotiating a Development-friendly Multilateral Framework in WTO

In case a negotiating mandate on investment is unavoidable at Cancun Ministerial, then developing countries have to ensure that the Framework covers adequate development provisions so that their process of development is not disrupted and sufficient flexibility to pursue their developmental policy objectives is retained. This will be a big challenge and has to be responded by proactive home-work by the developing country negotiators in evolving a development friendly draft of the MFI. In such a draft each and every element will have to be defined in a manner that concerns of developing countries are kept in mind. Some reflections in this regard are discussed in the following Section.

6. Incorporating a 'Development Dimension' in a Possible MFI

In case a negotiating mandate is given by the Ministerial Conference on a multilateral framework on investment within or outside the Single Undertaking, the challenge before developing countries is to define different elements of a MFI in such a manner that their developmental concerns are taken care of. The Doha Declaration places heavy emphasis on the development provisions and a balance of interests in Para 22. A crucial point for the negotiation of an MFI is how to achieve a balance between rights and obligations. In other words, a MFI should not only contain a set of restrictions on Members' policies, but it should also spell out clearly the obligations of investors. Most importantly, developing countries should retain flexibility to pursue selective policy in tune with their development policy objectives and impose performance requirements on foreign investors.

Some considerations for designing a development-friendly framework are as follows[7]:

(a) Scope and Definition

Adoption of broad scope and definition has obvious problems. For instance, a broad assets-based definition and all encompassing sectoral coverage would limit the governments' ability to regulate financial flows and manage the financial crises. Given the frequency of crises in various parts of the world, international financial institutions such as the World Bank are advising caution on the part of the governments with respect to the capital account liberalization[8].

The past experience suggests that a broad and general scope of investment agreements is not able to keep in mind the specific conditions and interests of different countries. Hence, there is need for bringing exceptions. The experience of OECD's Multilateral Agreement on Investment (MAI) is illustrative in this context as it had to be annexed with several hundreds of exceptions despite the fact that the contracting parties were all highly developed OECD member countries. Although bilateral investment treaties adopt broad assets based definitions, their scope is limited to investments undertaken in accordance with the national laws and policies and their purpose is essentially protection. Similarly the investment treaties within the regional integration arrangements (RIAs) such as EU are also generally broad in their coverage. However, the treatment accorded under these treaties is given on discriminatory basis to the member states in the RIA only and these RIAs invariably cover mobility of all the goods and factors of production such as labour along with that of capital.

Keeping in mind the mandate of the Doha Declaration that in Para 20 suggests that the focus is on 'long-term cross-border investment, particularly foreign direct investment, that will contribute to the expansion of trade' following steps can be taken to ensure development dimension:

i) Restrict the Scope to FDI: It is important to focus on FDI because these are generally of long-term in nature. In the WGTI meetings, Japan, among other countries argued for the need to restrict the scope of MFI to FDI[9]. FDI is distinguished from foreign portfolio investments on the basis of whether ownership is accompanied by management control. Therefore, there

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[7] for a more detailed treatment see Correa and Kumar 2003.
[8] See for instance, World Bank, 1999:146.
[9] See Paper submitted by Japan at WGTI, WT/WGTI/W/111, April 2002.

is need to define a threshold of equity ownership that could be used to distinguish FDI from all other types of foreign investments. Different levels of equity ownership are used in different countries for defining controlling stake. Majority ownership is the only objectively defined threshold because only the majority shareholder is able to take all the important decisions. Hence, majority ownership could be employed to define FDI. GATS, CARICOM, and the Statute of a 'European Company' have adopted the majority ownership rule for defining a controlling stake[10].

ii) Limit the Scope to FDI that Contributes to Expansion of Trade

The bulk of foreign direct investment flows continue to be essentially seeking the domestic markets in the host countries and generally substitute trade. Export-platform investments undertaken by MNEs as a part of restructuring of production according to international differences in factor costs have contributed significantly to expansion of world trade over the past three decades. The export-oriented foreign direct investments have evidently helped the East and Southeast Asian countries rapidly build their manufacturing export capabilities. Therefore, theses investments can contribute to expansion of trade besides expediting the development of the host countries. The literature suggests that export-oriented foreign direct investment is a special type of foreign direct investment and is determined by different factors (see Kumar 1994, 1998). Therefore, in view of the language of Para 22 of Doha Declaration, it is worthwhile to argue a case for limiting the scope of possible MFI to export-oriented FDI and not all the cross-border investments.

iii) Limit the Coverage to Green-field Investments that contribute to growth

FDI’s developmental impact on the host country also depends upon whether it takes the form of a greenfield investment or acquisition of an existing enterprise (Brown-field). It may be argued that greenfield investment has the greater potential to contribute to the expansion of trade by contributing to the manufacturing and export capabilities than acquisition of existing enterprises. Therefore, developing countries may wish to exclude acquisitions of existing enterprises from the scope of possible MFI.

(b) Transparency: Seeking a Symmetric Framework

[10] See UNCTAD/ITE/IIT/11; 1999a,: 41-3.

In an effort to attract FDI, developing countries are themselves moving towards making their investment policy regimes more transparent. It is not clear whether binding rules on transparency are necessary. APEC's approach to Non-binding Investment Principles may be adequate. Keeping in mind generally life-long relationship that they entail, governments are more cautious dealing with investments especially FDI than trade. The WTO Secretariat has observed that transparency provisions in existing bilateral and regional investment treaties – where they exist- are generally less detailed and prescriptive than similar requirements in the WTO'[11]. While transparency with respect to FDI policy framework might be unexceptional, some of the procedures for processing and evaluation of proposals might not be made transparent in public interest. The exceptions for confidential information in public interest need to be provided.

In dealing with foreign investors, governments of developing and least developed countries often experience an information asymmetry i.e. availability of little information about the background and track record of the investors in other countries with respect to corporate social responsibility, their involvement in bribery and corruption and restrictive business practices. Recent cases of Enron, Anderson, Xerox are cases in point. In this context, the MFI should provide for transparency on the background and track record of corporations and other investors. Investors and home governments must accept obligations to share information on their involvement in questionable dealings.

(c) National Treatment in Post-establishment Phase: Retaining the Policy Flexibility

As argued earlier, MNE affiliates enjoy several monopolistic advantages such as globally known brand names, proprietary superior technology, captive access to resources and pool of talent, they face different opportunities and pursue different objective functions compared to national enterprises. The margin of the edge enjoyed by them may be particularly wide in poorer developing countries. In low-income countries, because of wide technology gap not only that knowledge spillovers may fail to take place, the foreign entry may some times crowd domestic enterprises out and hence lower host country welfare (see Correa and Kumar 2003 for a review of evidence).

[11] WTO, Working Group on Trade and Investment *Transparency*, WT/WGTI/W/109, 2002, A Note by the Secretariat.

Therefore, in contrast to the argument of the proponents of MFI, the *playing field is already tilted in favour of MNEs*. MNEs when they enter a country are already much ahead of the domestic enterprises in the potential host country especially in developing countries because of their monopolistic ownership of unique assets. Given the differences in corporate strategy and decision-making, special advantages of MNEs, host governments in developing countries often need to adopt policies supporting and nurturing domestic 'infant enterprises' or small and medium enterprises from foreign competition either through selective policies towards FDI or through some measures favouring domestic enterprises. Given the scarcity of public funds that may be committed through tax exemptions or subsidies to promote development-related activities (such as R&D, employment, local value added), governments in developing countries may need to limit the granting of incentives to national firms or to a certain category thereof, for instance, small and medium enterprises. Discriminatory support measures favouring the domestic enterprises in strategic industries are quite common even in the developed world. A well-known example is SEMATECH, a consortium of computer chip manufacturers that has excluded foreign participation and has received substantial subsidies from the US government[12].

The recognition of national treatment as a general principle in an MFI would prevent any future change in legislation aimed at providing some advantages to nationals, not available to foreign investors. The Doha Declaration indicates that any framework should '*take due account of the development policies and objectives of host governments as well as their right to regulate in the public interest*..(emphasis added)[13]'.

To protect the flexibility for developing countries, granting of national treatment in the post-establishment phase may be structured on the basis of a GATS-type positive list approach which is more development friendly and subjected to limitations as considered necessary. The GATS-type approach leaves to the Members the possibility of determining in which sectors the national treatment standard will be applicable.

d) National Treatment in Pre-establishment Phase: Exclude any Commitments

In view of great variation in the quality or developmental impact of different FDI proposals on the host country's economy and in the light of possible adverse impact on domestic

[12] Moran (1996:431).

enterprises and host country welfare, as observed earlier, host governments may wish to protect domestic 'infant enterprises' or small and medium enterprises from foreign competition through selective policies towards FDI. Host governments may also impose, subject to the TRIMS Agreement, performance requirements on foreign entrants to regulate their operations in tune with their development policy objectives. The policy flexibility of governments of developing countries to pursue a selective policy towards FDI and impose performance requirements is very crucial and needs to be retained in any multilateral framework. The Doha Declaration does provide for such flexibility and suggests due regard of development policy and preserves their right to regulate in the public interest[14].

The application of the national treatment principle for pre-establishment would limit host countries' freedom to exclude or restrict foreign investment in specified sectors or activities, stipulate domestic ownership requirements, and adopt other permissible performance measures at the entry of FDI. The pre-establishment national treatment has not been provided under the bilateral investment treaties except for a few treaties signed by the US. Investment agreements as a part of regional integration arrangements (RIA) agreements like EU provide for pre-establishment national treatment. But these are limited to partners on a reciprocal basis and also include full labour mobility along-side capital mobility. MFI, on the other hand, is limited to only capital mobility and not labour mobility.

Therefore, developing countries should resist the national treatment obligation for pre-establishment stage to retain the policy flexibility.

The proponents of MFI argue that a GATS-type approach to pre-establishment national treatment commitment allow adequate policy space to developing countries.[15] In principle, the GATS approach provides the flexibility. However, the experience of GATS suggests that developed countries bring pressure on developing countries to make commitments in the sectors that are of particular interest to them.

(e) Most-Favoured-Nation (MFN): Building Exceptions for Ethnic Investors

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[13] Para 22 of the Doha Declaration.
[14] Doha Ministerial Declaration, para 22.
[15] See Concept Paper on Policy Space for Development by EC and its Member States, WT/WGTI/W/154 7 April 2003.

The extension of the MFN treatment to investment may be seen as a logical requirement in a multilateral system. It may affect, however, the special treatment conferred by many developing countries to "ethnic overseas investors", inspite of their being permanent residents in or citizens of other countries. Therefore, exceptions for a differential treatment for ethnic overseas investors may be retained in a possible MFI.

(f) Development Provisions

Developing countries seek FDI as a resource for their industrialization and development. FDI is supposed to bring to its host country a number of valuable resources for development such as capital, technology, managerial and marketing skills, and some times market access in the case of export-oriented FDI. The knowledge and technologies brought in may diffuse in the host economy and hence be more productive. However, not all the cases of FDI do bring such resources and as is evident from the literature cited in Section 3, FDI may even reduce host country welfare by crowding-out FDI. The evidence also shows the critical importance of host government policies such as performance requirements in maximizing the benefits of FDI and minimizing possible adverse effects. Hence, host governments –developed as well as developing-- generally employed policies that bring the operations of MNCs in consonance with the host country developmental goals.

i) Flexibility to Impose Performance Requirements

Under the Special and Differential Treatment, developing countries should seek flexibility to pursue policies that help them in exploiting the resources of MNCs for their development more effectively. These include policies such as performance requirements. Some of the performance requirements have been phased out as per the obligations of TRIMs Agreements such as local content requirements and foreign exchange neutrality requirements. Others can still be applied. A number of developing countries have sought extensions to the phase-out period for implementation of the commitment under TRIMs[16]. In case developing countries have agreed to negotiate an MFI, they could seek an abrogation of the TRIMs Agreement as the MFI would subsume all the necessary elements for dealing with investment.

ii) Exceptions in Government Procurement

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[16] See Correa and Kumar 2003 for details.

Government procurement has been extensively used, in developed and developing countries, to promote the development of local industries by means of preferential treatment in terms of prices or other conditions of supply. From a developmental perspective, a possible MFI should be flexible enough to permit the use of public purchasing power as an instrument to promote the development of local firms[17].

iii) BOP Safeguards

Safeguards should be built into the possible MFI for periods of BOP difficulties faced by developing countries. BIPAs, have some times incorporated provisions of temporary suspension of remittances of profits and dividends and repatriation of disinvestments proceeds by companies in the periods of BOP difficulties faced by host countries. Such provisions could be built into MFI as well.

iv)A Special and Differential Treatment based on Objectively Defined Criterion for Development

The special and differential provisions for developing countries should be based on the level of development rather than additional transition years. For instance, these provisions and policy flexibility could be linked to developing countries reaching a threshold of per capita manufacturing value added (MVA per capita). This way the concept of graduation is built into as countries crossing the development threshold will cease to enjoy the special and differential treatment. As in the case of the Agreement on Subsidies and Counterveiling Measures (SCM), a threshold level could be defined, of MVA per capita. Keeping in mind the world average of the MVA per capita at US$ 1000 (MVA accounting for roughly 20 per cent of the GDP and a average per capita income for the world of US$ 5000 for 2000AD). A country should retain the policy flexibility that it deems desirable to pursue its development policy objectives so long as it has not crossed the threshold of US$ 1000 of MVA per capita, This way the SDT will be based on an objective criteria will also introduce a concept of graduation. The countries below the MVA threshold should have complete freedom to apply performance requirements and other policies to maximize the contribution of FDI to their development.

[17] In contrast, the draft MAI did not affect the right of a State to establish or maintain State (or private) monopolies, but prevented discrimination against foreign investors with regard to the sale of goods and services made by a monopoly, as well as with respect to its purchase of goods and services from third parties, except to the extent that the purchase were not made with a view to commercial resale or for use in the production of goods and services for commercial sale.

(g) Balancing the Host Country and Home Country Interests

The Doha Declaration indicates the need for balancing the host and home country interests. However, no indications have been made on the way to balance the interests of developed and developing countries. A balancing of interest between all the stakeholders could be ensured with rights and obligations of all the stake-holders and by ensuring a symmetry between capital and labour mobility.

i) Seeking Binding Investors' Obligations

The proponents of the MFI have been seeking rights of foreign investors which the host country governments should commit to provide. However, nothing is being said about the obligations of the investors or the home countries. Any multilateral framework on investment has to be a balanced one defining the rights and responsibilities of all the actors involved. The Doha Declaration indicates need for a balanced framework covering host and home country interests. China, Cuba, India, Kenya, Pakistan and Zimbabwe have made a joint submission to the WGTI on Investors' and Home Government' Obligations.[18]

Some of these obligations and others that could be considered for incorporation appropriately in a possible MFI include their contribution to development, generation of employment, non-interference in internal affairs of the host country, and inter-governmental relations, environmental and consumer protection, fair treatment of employees, restraint from imposing restrictive clauses on their affiliates with respect to sourcing of inputs and marketing of output, accepting obligations for disclosures on the financial as well as non-financial information on the structure, policies and activities of the MNE as a whole as well as that of the local affiliate, to cooperate with the host government in the period of BOP crisis among others.

ii) Seeking Provisions for Transfer of Technology by Foreign Investors

For developing countries and LDCs, the access to foreign technology is a critical issue which has not been adequately addressed so far in the WTO agreements. There are limitations of the national regulations in effecting technology transfer from MNEs, as is clear from the

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[18] See WT/WGTI/W/152, 19 November 2003.

evidence that is available[19]. As mentioned, an attempt was made in the 1980s to establish an International Code of Conduct on Transfer of Technology under the auspices of UNCTAD, but these negotiations have failed.

If an MFI is to be negotiated, an important target for developing countries may be to include provisions relating to transfer of technology, so as to ensure that foreign investment effectively contribute to the technological development of the host country. Issues to be considered in this framework may include:

- requirements of transfer of technology as a condition for entry or operation of a foreign investment;
- obligations to train and employ local personnel; and
- performance requirements related to a given level or value of research and development;
- restraints on the MNEs from imposing restrictions on their overseas affiliates that adversely affect the process of absorption of technology and diversify sources of capital equipment and services;
- measures for attracting FDI in R&D activities;
- grant of subsidies and tax benefits in developed countries to promote the transfer of technology (including associated equipment) to developing countries and LDCs[20].

iii) Dealing with Market Power and Restrictive Business Practices of MNEs

The concern about market power of MNEs and possible abuse of it has attracted the attention of the international community. MNEs have been found to have engaged in a number of anti-competitive arrangements with other firms. These include horizontal international marketing and price-fixing cartels, vertical international distribution systems established by MNEs for the sale of their products and the use of joint ventures with other firms[21]. The national competition policy may have limitations in dealing with the abuse of market power by MNE affiliates that have operations transcending national boundaries. As observed earlier, these

[19] See Muchlinsky (1999) p. 447 giving Nigerian experience with transfer technology regulation that has been largely ignored by foreign and local investors when entering into technology licensing contracts.

[20] The establishment of this type of incentives may require appropriate adjustments to the Agreement on Subsidies and Countervailing Measures. It should also be noted that under article 66.2 of the TRIPS Agreement, developed countries are bound to provide incentives domestically to promote the transfer of technology to LDCs.

[21] See Muchlinsky (1999: p. 387).

concerns led to adoption of the Set of Multilaterally Agreed Equitable Principles and Rules for Control of Restrictive Business Practices (RBPs) under the auspices of UNCTAD in 1980. The Set provides for collaboration between governments and an international mechanism to facilitate control of RBPs. Enterprises are obliged to refrain from RBPs defined to include price fixing, collusive tendering, market or customer allocation arrangements, allocation of sales or production quota, concerted refusal to deal or supplies to potential importers, collective denial to access to an arrangement. The enterprises are also required to refrain from abuse of market power in the form of predatory behaviour, discriminatory pricing or terms, joint ventures, M&As, and refusal to deal, among other provisions. It also to facilitates appropriate action taken at multilateral level. However, the Set is not a binding instrument. An effective regulation of RBPs and other anti-competitive practices through binding provisions should form an integral part of the MFI if it is negotiated.

iv) Seeking binding Home Country Obligations

In a balanced framework, the home governments should also accept some obligations. The home governments policies do have influence on the behaviour of TNCs originating in their territories. Some home governments, e.g. the US have asserted their power to restrict exports of goods by the overseas subsidiaries of US enterprises. Home governments must accept an obligation not to impose such trade or investment related restrictions on the overseas affiliates of corporations based in their territories. They should also undertake to provide information regarding the involvement of TNCs in any questionable dealings and other information on their background that may be useful for the host government at the time of approval. The home governments should also cooperate with the host governments in control of RBPs, transfer-pricing manipulation, and in recovery of the liabilities of TNCs resulting from their mis-conduct in host countries.

v) Seeking Commitment on Labour Mobility

MFI is a framework for liberalization of capital flows and will benefit developed countries. Developing countries could seek a reciprocity in the form of a multilateral framework for liberalization of labour flows. This would make it a balanced framework. As observed earlier, the restrictions on the movement of natural persons are imposing substantial costs in terms of

the world welfare. Facilitation of labour mobility would yield substantial efficiency gains benefiting both home as well as the host countries[22].

vi) An International Discipline on Incentives

A number of investment incentives are granted by developed and some developing countries as a part of their industrial, technological and other policies. It has been demonstrated that these incentives distort investment patterns in favour of developed countries as developing countries are at a disadvantage to provide matching incentives. Because of the prisoners' dilemma inherent in the investment incentives competition, an international discipline to limit the investment-distorting incentives would maximize the collective welfare of the participating countries. Such a discipline should form a part of any possible MFI. However, exceptions allowing developing countries and LDC to use such incentives to promote such policy objectives as industrial development and regional development of backward regions have to be built into such a discipline.

(h) A Cautious Approach to Dispute Settlement and Investor Protection

Standards relating to investor protection, such as general treatment, compensation in cases of expropriation, protection from strife, free transfer of payments, and subrogation are generally contained in BITs and regional agreements on investment. Those standards are by and large accepted and established in bilateral and regional treaties. The implications of a possible inclusion of those standards in an MFI will largely depend upon the scope of the adopted definition (particularly important with regard to the free transfer of payments) and to the extent to which protection would be an absolute standard, or subject to a "contractual approach" as suggested above, that is, to compliance by the concerned investor of the host country's laws and regulations.

The right to initiate a dispute should be limited to Member States as currently provided under applicable rules for dispute settlement. Investor to State disputes would not acceptable in an MFI negotiated in the WTO framework.

Furthermore, there is need to adopt a cautious and restrictive definition of expropriation or taking in the light of evidence on litigations brought by affiliates of US corporations against

[22] See Winters et al. 2002.

the Canadian Government under Chapter 11 of NAFTA seeking compensation for the government regulations and actions affecting the business prospects of companies as amounting to regulatory takings. For instance, the United Parcel Service (UPS) has sued the Canadian government under this Chapter of NAFTA for $230 million over what it alleges is unfair cross-subsidization by Canada Post of its Xpresspost and Priority Courier operations[23]. Regulatory actions of host governments for pursuing their development policy goals, environmental and social objectives in broad public interest should be specifically excluded from the scope of expropriation or regulatory takings.

7. Concluding Remarks

This paper has reviewed the options open to developing countries on investment at the Cancun Ministerial Conference of WTO which is to decide whether or not to launch negotiations on a multilateral framework on the subject. Given the high opportunity cost of the policy flexibility for the process of development and no reciprocity or gains even in the form of higher inflows of FDI, the most prudent option for developing countries would be to resist a negotiating mandate on investment at Cancun. In view of the clarificatory statement by Chairman of Doha Ministerial that led to adoption of the Declaration, it may still be possible. However, this would require effective coordination among developing countries and their ability to put up a strong coalition against the negotiating mandate.

A compromise solution could be to negotiate a multilateral treaty on investment on the lines of bilateral treaties outside the WTO. Or better still would be to resurrect the UN Code of Conduct on TNCs a draft of which exists and could be adopted as a binding UN instrument. The draft UN Code provides a multilateral framework balancing the host country, investor and home country interests and could serve the purpose of the protagonists of the MFI very well.

In case a negotiating mandate at the Fifth Meeting is unavoidable, then efforts should be made to ensure that developing countries concerns are built into each element of the proposed framework. We have outlined different elements of a possible MFI capturing development dimension to aid preparations of developing countries in negotiations. This is to be secured by limiting the scope of MFI to trade-oriented FDI, resisting commitments on pre-

[23] See *National Post* 24 July 2002, posted at http://www.tradeobservatory.org/news/index.cfm?ID=3695.

establishment national treatment and adopting a GATS-type approach for post-establishment commitments, providing for flexibility to pursue selective policy and impose performance requirements by developing countries, incorporating investors obligations and home country obligations, providing for transfer of technology, control of RBPs and competition policy, among other provisions to balance the host country and home country interests. This way developing countries would be able to minimize the damage that an MFI has the potential to bring about in terms of effect on their development.

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