INVESTMENT FACILITATION AGREEMENT IN WTO:
What it Contains and Why India should be Cautious?

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*[**Abstract**: There has been discussion in WTO on initiating negotiation on an investment facilitation agreement during the 11th Ministerial Meeting of WTO which will take place on 10-13 December in Buenos Aires, Argentina. The proposals submitted in WTO indicate that the agreement aims to smoothen the process of cross-border investments by making the process transparent and efficient. The agreement, however, does not intend to incorporate substantive provisions which has been the demand of advanced countries. It also does not aim to address the challenges caused by large number of bilateral investment treaties, which has been the demand of many counties. Therefore, the agreement in its current form unlikely to enthuse most Members of WTO. It seems that the proponents of the agreement may align with advanced countries to make a headway. In that case, substantive provisions will have to incorporated into the agreement which will result in erosion of policy space of foreign investment hosting countries. India has adopted a cautious approach to the proposal and has not consented to initiate the negotiation. Preliminary assessment of India's FDI inflows and outflows shows that India should continue to maintain a cautious approach to the proposed agreement].*

Introduction

Fifteen countries of World Trade Organization (WTO) have submitted proposals in WTO which are aimed at initiating negotiations on an investment facilitation agreement (IFA) during the 11th WTO Ministerial Conference scheduled for 10-13 December 2017 in Buenos Aires, Argentina. The proponents of IFA underscore the positive impact of foreign investment on development to emphasise the importance of IFA. Interestingly this proposal has come from a small group of countries, consisting mostly of developing countries and economies in transition. This paper brings out major features of IFA and makes a critical assessment of the contribution it makes to the global governance of cross-border investment. It also critically reviews India's approach to IFA.

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Major features of the proposed Agreement on Investment Facilitation in WTO

Fifteen Members of the WTO have kick started an informal discussion on an IFA in the WTO, by underscoring the growing linkages between international trade and investment and its mutually reinforcing role in facilitating global development. There are five submissions from these countries of which two are collective proposals: one from "Friends of Investment Facilitation for Development" (FIFD)[1] and the other is from "MIKTA"[2] which has organised a workshop on trade and investment in the WTO on 20 March 2017. The proposal by FIFD aims to launch an open-ended and informal dialogue in WTO on investment facilitation to which all Members of WTO are encouraged to participate. The dialogue is expected to examine possible elements of IFA in the areas of "improving regulatory transparency and predictability, streamlining and speeding up of administrative procedures, enhancing international cooperation and addressing the needs of developing members"[3]. The proposal clarifies that IFA will not address well known controversial issues such as market access, investment protection, and dispute settlement clauses especially investor-state dispute settlement (ISDS). The proposal by MIKTA while recognising the dynamic link between trade, investment and development and the need for greater coherence between trade and investment policy, exhorts that discussions at WTO should add value to the related work in other forums including G-20, APEC, UNCTAD and OECD. On the link between investment and development, it states that "FDI is a vital source of funding to close the $2.5 trillion development investment gap to achieve sustainable development goals" and that "with the right policy settings, recognising the trade-investment nexus, investment can advance inclusive, broad based growth, promote and enable sustainable development and responsible business conduct"[4]. The proposal by MIKTA, like the proposal by FIFD, suggests that sensitive issues such as ISDS and investment protections should be avoided from IFA. It highlights that different agreements of WTO – GATS, TRIMS, Agreement on Subsidies and Countervailing Measures and Agreement on Government

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1. Argentina, Brazil, Chile, China, Colombia, Hong Kong, Kazakhstan, Mexico, Nigeria and Pakistan; *Proposal for a WTO Informal Dialogue on Investment Facilitation for Development*, Joint Communication from the Friends of Investment Facilitation for Development, WTO Document JOB/GC/122.
2. Mexico, Indonesia, Korea, Turkey and Australia; *MIKTA Investment Workshop Reflections*, WTO Document JOB/GC/121.
3. Para. 1.3, n.1.
4. Page 1, n.2.

Procurement (plurilateral agreement) covers investment in a piecemeal manner. Interestingly, it states that "TRIPS provisions are relevant to the legal environment affecting foreign investment" which indicates the likely treatment of the term 'investment' in IFA. No linkage has been made between TRIPS and investment till now in WTO. But this linkage has already been made in IIAs which define investment very broadly[5].

The other three proposals have been submitted by Russia, China, Argentina and Brazil: Russia[6] and China[7] made individual submissions and Argentina and Brazil[8] made a joint submission. These three proposals provide more details of key elements of the proposed IFA. According to the Argentina-Brazil proposal, IFA would encompass "the set of policy measures and activities aimed at making it easier for investors to establish, maintain and expand their investment in host countries as well as to conduct their day to day business"[9]. The main elements of IFA as coming out from the three proposals are given below.

1. *Scope of IFA*: It covers investment in the production of goods and supply of services.
2. *Transparency*: In order to have transparent laws and regulations regarding investment matters, WTO Members are required to report to WTO all laws relating to investment policy. They are also called for considering to provide opportunity for investors and other stakeholders to comment on measures related to investment.
3. *Processing of Applications*: In order to establish a stable, predictable and efficient framework for investors, a common set of principles for processing and screening of investment proposals would be established.
4. *Single Electronic Window*: Access to competent authorities by investors in the host countries would be through a single window electronic system.

[5] IIAs include bilateral investment treaties and treaties with investment chapters.

[6] *Communication from the Russian Federation*, Investment Policy Discussion Group, WTO Document JOB/GC/120.

[7] *Possible Elements of Investment Facilitation*, Communication from China, WTO Document JOB/GC/123.

[8] *Possible Elements of a WTO Instrument on Investment Facilitation*, Communication from Argentina and Brazil, WTO Document JOB/GC/124.

[9] Section 1.4, n. 7.

5. *National Focal Points*: National focal points or ombudsperson would be established. They will provide all required information to investors. Cooperation between national focal points of different countries would help in preventing disputes between Members.
6. *Fees and Charges*: Fees and other expenses which investors have to incur while processing their applications should be made publicly available and be commensurate with the actual cost of services extended by the concerned authorities.
7. *Investors' Principles and Standards*: Members could encourage investors to adopt certain principles and standards for responsible business conduct. Adoption of these principles and standards would be voluntary on investors.
8. *Special and Differential Treatment*: Developing countries and least developed countries (LDCs) would be given special provisions given their special economic and development needs. LDCs would not be required to implement any obligations arising out of IFA, but they will be encouraged to do so.
9. *Technical Assistance*: Technical assistance will be provided to developing countries and LDCs to strengthen their institutional and regulatory capacities to facilitate investment.
10. *Regulatory Space*: Regulatory space of members would be protected.

In two areas—dispute settlement and protection of outward investment, however, the proposals do not have a common position. While FIFD, MIKTA, Argentina and Brazil have the view that sensitive issues like dispute settlement should not be addressed in IFA, Russia proposes that there should be mechanisms within the jurisdiction of the Member state such as judicial, arbitral or administrative procedures to prevent and amicably settle investment related grievances. Russia had amended its model Bilateral Investment Treaty (BIT) in 2016[10] which requires foreign investors to exhaust local remedies before initiating international arbitration. It may also be noted that Russia is the only country among the 15 countries which is not part of FIFD or MIKTA initiatives. China's proposal is silent on dispute settlement provisions. But it contains a provision for the protection of outward investment to developing countries

[10] Regulation of Entering into International Treaties on the Encouragement and Mutual Protection of Investments (Investment Protection Regulation 2016).

and LDCs in the form of investment insurance and guarantees, political risk coverage, etc. While all the three detailed proposals, i.e., by Russia, China and Argentina and Brazil, provide for special and differential treatment within IFA, it is only China which seeks protection of outward investment to respond to the needs of developing countries and LDCs. China is demanding protection of outward investment, probably because it is the most outward FDI (OFDI) oriented country among the 15 countries. Between 2010 and 2015, Chinese FDI stock in LDCs tripled to reach $31billion, making it the largest investor of FDI in LDCs[11] (UN-OHRLLS 2017). Table 1 provides the share of 15 countries, the IFA proponents, in global OFDI.

Since the rationale of IFA lies in the impact that cross-border investment has on global development, it is important to understand the relationship between foreign investment and development. Dynamics of this relationship differ across countries and such differences have led to the failure of earlier attempts to at various forums such as the UN and WTO to establish an international regime on foreign investment.

Relationship between Foreign Investment and Development

The term 'development' does not mean the same to everyone. For some, it is the mere economic growth of a country; the growth of GDP. For them, the implications of economic growth on human beings and environment are not of major concern. For some others, it is the development of human beings; development in areas of health, education and poverty. The more recent conception of development is centred on sustainability which implies development of world's poor in a manner that "meets the needs of the present without compromising the ability of future generations to meet their own needs"[12]. In all conceptions of development, economic growth is central to development.

Creation and diffusion of productive knowledge is critical for economic growth. It includes technical knowledge (R&D, design and process engineering) as well as knowledge of management, organisation, inter-firm and international relationships,

[11] More than a third of its investment went to Cambodia, Lao PDR and Myanmar.

[12] *Our Common Future, Chapter 2: Towards Sustainable Development*, Report of the World Commission on Environment and Development, 1986. Accessed at http://www.un-documents.net/ocf-02.htm.

much of which are tacit in nature (UNCTAD 1999). Productive knowledge is important both in modern high-tech industries as well as traditional activities in the primary sector (UNCTAD 1999). Capital allows investment in the generation of new knowledge and technology which enables an economy to attain higher levels of growth. Although foreign and domestic capital contributes to the development of new ideas, Foreign Direct Investment (FDI) is considered to have a much better impact as it comes with a package of capital, technology, know-how and managerial, organisational and marketing skills. Multinational Companies (MNCs), which are the main source of FDI, are much better placed as compared to domestic firms in terms of the 'associated advantages'. Therefore, inviting FDI into a country, especially developing country of LDC, is expected to fasten the pace of augmenting the productive knowledge base of that country.

The dynamics of investment-development relationship vary across countries depending upon various factors. For those countries which use FDI as a means for enhancing their base of productive knowledge, whom we call host countries, FDI has the potential to introduce advanced technologies, better management and marketing practices, augment human skills, and secure market access for host country products apart from supplementing domestic capital. Foreign Portfolio Investment (FPI), on the other hand, does not contain the advantages which FDI has and will only supplement domestic capital. Therefore, FDI is considered to be a desirable source of finance especially for those countries which are 'catching up' in development.

What distinguishes FDI from FPI is the motivation of the investor. The OECD Benchmark Definition of FDI (OCED 2008), which is the widely used definition of FDI, makes it clear that in FDI the foreign investor would have a lasting interest in the direct investment firm. This in in many cases, if not in most cases, results in the former having an influence or controlling stake in the management of the latter. The influence or control which the foreign investor or MNC would have on the management of a domestic firm is likely to result in better decisions and strategies. But on the motivation of FPI, OECD (2008) states that "the investor's focus is mostly on earnings resulting from the acquisition and sales of shares and other securities without expecting to control or influence the management of the assets underlying these investments...Portfolio investors do not have as an objective any long-term relationship. Return on the assets is the main determinant for the purchase or sale of their securities" (pp.22-23). The FDI Policy of India also makes this distinction clear: “Foreign Direct Investment, as distinguished from portfolio investment, has the connotation of establishing a ‘lasting interest’ in an enterprise…”[13].

Impact of FDI on development would be different depending on whether the inflow of investment is through Mergers and Acquisitions (M&As) or greenfield projects. FDI through M&As is likely to result in mere change in the ownership and need not bring in advantages associated with typical FDI as we have seen in the case of Daiichi’s takeover of Ranbaxy in 2008. But greenfield FDI which establishes new facilities in the host country is very likely to result in enhanced economic activity, creation of additional job opportunities and export avenues and introduction of advanced technologies. Domestic enterprises may benefit from greenfield FDI through various forms of spillovers, for example through collaboration, movement of personnel, demonstration effects, etc. The approach of host countries to the nature of entry of FDI will have an impact on their development.

The role of the host country governments is also significant in influencing FDI to yield desired outcomes. A survey of literature on 'FDI, Intellectual Property Rights (IPRs) and technology transfer' undertaken by Dhar and Joseph (2016) shows that MNCs will introduce advanced technologies in the host country only when there are competing firms in the host country. In the absence of competing firms, MNCs will tend to introduce obsolete technologies in the host country. Even the introduction of liberal IPR policy, which is in favour of MNCs, will not result in more inflow of FDI or introduction of latest technologies in the host country. Therefore, existence of a vibrant domestic industry is an important requirement for benefitting from FDI in terms of advanced technologies. This is also a requirement for taking advantage of spillover effects. In many cases, granting access to market for FDI was made conditional on certain

[13] Chapter 1.1.1 of *Consolidated FDI Policy* (effective from August 2017), Department of Industrial Policy and Promotion, Government of India, http://dipp.nic.in/sites/default/files/CFPC_2017_FINAL_RELEASED_28.8.17.pdf

performance requirements such as employment of local people, introduction of advanced technologies, etc.

China is a recent example of using FDI for development through extensive use of performance requirement strategies. A study conducted by Long et.al. (2003) among 442 FDI firms found that 84% of them trained personnel in China and 21% trained personnel abroad. Ninety percent of those received training left the foreign funded firms to either start a new venture or to join competing firms. In technology front, 27% firms introduced most advanced technology of their parent firms, 2% introduced technologies which were not previously used in China and 35% introduced technologies which were considered to be most advanced in China. The economic history of advanced countries shows that they used a number of performance strategies to make MNCs to contribute to their development process. In the automobile sector, Italy had imposed 75% local content on Mitsubishi Pajero, US – 75% on Toyota Camry and UK – 90% on Nissan Primera (Sercovich 1998). Although China has been restrained from using certain performance requirement strategies on account of its commitments under TRIMS agreement since its joining WTO in 2001, it still uses performance requirement strategies to meet its development goals. The 'China Manufacturing 2025' strategy which was finalised in the beginning of 2017, uses technology transfer in exchange for market access (EUCCC 2017). Thus, benefitting from FDI depends on the requirements imposed on foreign investors by the host country governments.

Contribution of FDI to development of host countries also depends on the policy measures adopted to address challenges impacting development which need not be directed specifically at FDI. Countries adopt various measures for meeting objectives such as the protection of environment, prevention of tax avoidance, reduction in disparities in regional development, promotion of public health, etc. Such measures are binding on all investors, irrespective of their being foreign or domestic. Countries which employ such policy measures will experience better development outcomes from investment, including FDI, as compared to others which do not implement such measures. Therefore, in negotiations on a multilateral treaty on foreign investment, the demands of host countries have been centered on safeguarding their policy space and imposing certain obligations on MNCs towards the development of host countries.

The dynamics of investment-development relationship is very different in those countries from where FDI originates, whom we call home countries. The efforts of these countries are primarily focused on facilitating opportunities for investment of their investors by ensuring access to foreign markets along with measures to protect the investments and the returns earned. Profits generated in foreign countries will be repatriated to home countries and invested in the further creation of productive knowledge. This process enables the home countries to maintain their advantage in the productive knowledge. Even if the profits are not repatriated and invested in host countries for the creation of productive knowledge, IPR laws enable the MNC or the foreign investor to own and control the productive knowledge created elsewhere. Overseas investments with motivations of resource seeking and knowledge augmenting benefit the home countries by way of access to resources and new knowledge. Therefore, the focus of home countries in negotiations on a multilateral regime on foreign investment has always been on securing access to foreign markets and the protection of investments by their investors abroad.

This difference in the dynamics of investment-development relationship has been the major reason for the failure of global community in establishing a multilateral regime on foreign investment. During the negotiations on a United Nations Code of Conduct on Transnational Corporations (Code) under the aegis of UN Commission on Transnational Corporations (UNCTC), developed countries and developing countries, which are majorly home and host countries respectively, held very divergent positions. Developing countries wanted a Code that established binding commitments on MNCs and did not agree to binding investment protection measures as they would curtail their policy space to regulate foreign investors. Developed countries, on the other hand, wanted the developing countries to accept customary international law as the minimum standard for the protection of investors and investment. Developing countries did not accept this as they were not part of the development of this law (Sauvant 2015). Developing countries, especially the Latin American countries, which were influenced by the Calvo Doctrine, insisted that foreign investors should be given the same treatment as that of domestic investors and therefore both should be covered by national law of the host countries. Due to this diverging positions the Intergovernmental Working Group on a Code of Conduct, which was constituted during the second session of UNCTC in 1976, could never arrive at a consensus view on the provisions of the Code.

This division also resulted in the non-initiation of formal negotiations on an investment agreement in WTO, as part of Singapore issues, as proposed by major developed countries. The proponents of the investment agreement wanted an agreement which defines investment very broadly to include FPI and IPRs, restricts host countries from using performance requirements, protects the right of investors to fund transfer and establishes the right to entry and establishment by foreign investors in host countries. Developing countries, on the other hand, were not prepared to negotiate on a new topic until the implementation issues in the WTO are resolved. In any case, they were not agreeable to the demands of proponents and wanted the definition investment to be restricted to FDI and scope of the treaty to provide maximum flexibility to developing countries to regulate investors (Khor 2007). The right of foreign investors to entry and establishment would constrain the ability of host countries to regulate foreign investors.

Failure to conclude a multilateral treaty on foreign investment in the way the developed countries had wanted resulted in the spurt of Bilateral Investment Treaties (BITs). The first BIT was signed in 1959 between Germany and Pakistan. Over the years the number of BITs increased from 371 at the end of 1980s to 1862 by the end of the 1990s and to 2950 by the beginning of 2017[14]. BITs define investment very broadly and have provisions for national treatment, most-favoured nation, fair and equitable treatment, adequate and effective compensation upon expropriation, right to repatriate profits and ISDS. These treaties were concluded mostly between developed and developing countries; in other words between home and host countries. They have considerably limited the policy space of host countries to regulate investors, including the exercise of performance requirement strategies. The US Department of State makes it clear that one of the core principles of BITs is to limit the "circumstances in which

[14] There are 372 treaties with investment chapters, making total number of IIAs 3322. Data on number of IIAs is compiled from various issues of IIA Issue Note, UNCTAD. Ninety five percent of IIAs was concluded before 2010 (IIA Issue Note, June 2017).

performance requirements can be imposed”[15]. The ISDS process, centred on which the demand for reforming the governance of IIAs has come up, has been mired with ‘legitimacy crisis’ due to the non-transparency in procedures, inconsistency in the interpretation of same clause by different tribunals and lack of provisions for appeal. As developed countries also increasingly began to become targets of ISDS disputes, the call for reforms gained momentum. Developing countries were compelled to embrace BITs due to the pressure which the debt crisis of the 1980s exerted on them: they had realised that FDI is better as compared to debt creating borrowings and expected that BITs would help in bringing in more FDI. They were also of the view that in bilateral arrangements they would be better positioned to preserve the policy space as compared to multilateral arrangements.

However, studies show that there is no one-to-one relationship between IIAs and FDI inflows. UNCTAD (1998) and Rose-Ackerman & Tobin (2005) find no association between IIAs and FDI. The US and China do not have a BIT, still US is a leading investor in China[16]. Carim (2015) points out that Japan, a major source of FDI, has only four IIAs. In fact, studies show that establishing a stable business environment is important in attracting FDI and IIAs could only complement such an environment and not substitute it (Hallward-Driemeier 2003; Rose-Ackerman and Tobin 2005). Although the benefits from IIAs at the best were doubtful, the host countries have to pay huge price on account of ISDS disputes. Libya had to pay US$905 million as compensation to an investor who invested only US$ 5 million in Libya. Ecuador had to pay US$ 1.1 billion to an US investor which was equivalent to 90% of Ecuador’s social welfare budget in 2015 (Eberhardt 2016).

Having faced the challenges caused by BITs, a number of developing countries including India, Indonesia, South Africa, Bolivia and Ecuador have terminated a large number of BITs they already had concluded. The US amended its model BIT in 2012 with the objective of advancing public interest and ensuring that it does not grand greater substantive rights to foreign investors in US than what has been granted to US investors

[15] US Department of State, *Bilateral Investment Treaties and Related Agreements*, https://www.state.gov/e/eb/ifd/bit/

[16] It may be possible that US investors are routing their investments through third countries with whom China has BITS. However, there are difficulties in establishing this empirically.

in US under the constitution of US. The European Commission (EC) came out with the proposal of an Investment Court System (ICS) in 2015 to replace the ISDS, based on which the investment chapter of EU-Canada Comprehensive Economic and Trade Agreement (CETA) was amended, to address the legitimacy crisis facing the ISDS in IIAs.

In order to make FDI cater to global development, the framework of global governance of foreign investment established by a large number of IIAs needs to be reformed to restore the policy space to regulate FDI. In the light of complex dynamics of FDI-development relationship, IFA does not propose anything that would really enhance the policy space of host countries to channel FDI for development. Unlike cross-border trade, the effects of which can easily be controlled through border measures, the effects of foreign investment depend on various factors and are complex in nature. Therefore, controlling the effects of foreign investments is much more complex and calls for regulatory autonomy of host states. For these reasons, IFA is likely to face a lot of challenges and resistance from fellow WTO Members.

Challenges for IFA
An incoherent group of IFA proponents

The IFA proponents are a group of 15 countries at different levels of development. Most of them are developing countries and half of them are members of G-20. All developing country members of G-20, except India and Saudi Arabia, are members of this group. The IFA proponents account for 17.2% of the global OFDI stock in 2016 as compared to 4.9% in 1990 and 23.6% inward FDI stock in 2016. Although the growth in the share of these countries in the OFDI stock is remarkable, it has been primarily contributed by one country – China; mainland China and Hong Kong. China accounts for almost two-third of the OFDI by IFA proponents. *Table 1* provides more details of the IFA proponents.

More than half of the IFA proponents – Kazakhstan, Argentina, Pakistan, Nigeria, Columbia, Indonesia, Chile and Turkey have very negligible share in the OFDI. They account for only 7% of the OFDI by the IFA proponents in 2016. In the case of Chile, OFDI is very significant as the share of OFDI stock in 2016 is almost half of its GDP in that year, although it is not an important contributor in global OFDI[17]. It is not clear what these countries (except Chile) would gain from IFA. If they expect to receive more FDI, they can implement the measures proposed in the IFA even without becoming partners to IFA.

Table 1: Characteristics of TFA Proponents

Country	*Characteristics of Country*	*OFDI Stock*			*FDI Stock*		
		Value in 2016 ($Mn.)	*Share in Global OFDI in 2016 (%)*	*Share in Global OFDI in 1990 (%)*	*Value in 2016 ($Mn.)*	*Share in Global FDI in 2016 (%)*	*Share in Global FDI in 1990 (%)*
Australia	Developed; G-20	401505.8	1.5	1.7	576036.6	2.2	3.7
Kazakhstan	Transition Economy	20731.0	0.1	0.0#	129772.8	0.5	0.1*
Russian Federation	Transition Economy; G-20	335791.5	1.3	0.1*	379035.1	1.4	0.0*
Argentina	Developing; G-20; G-77	38814.3	0.1	0.3	88221.7	0.3	0.4
Brazil	Developing; G-20; G-77	172441.4	0.7	1.8	625876.2	2.3	1.7
Chile	Developing; G-77	110089.6	0.4	0.0	238557.2	0.9	0.7
China	Developing; G-20	1280974.6	4.9	0.2	1354404.0	5.1	0.9
Colombia	Developing; G-77	51816.3	0.2	0.0	164249.0	0.6	0.2
Hong Kong, China	Developing	1527880.4	5.8	0.5	1590808.5	6.0	9.2
Indonesia	Developing; G-20; G-77	58890.0	0.2	0.0	234961.0	0.9	0.4
Republic of Korea (S. Korea)	Developing; G-20	306145.0	1.2	0.1	184969.7	0.7	0.2
Mexico	Developing; G-20	148643.2	0.6	0.1	473520.0	1.8	1.0
Nigeria	Developing; G-77	12999.2	0.0	0.1	94184.1	0.4	0.4
Pakistan	Developing; G-77	2052.0	0.0	0.0	39017.2	0.1	0.1
Turkey	Developing; G-20	38020.0	0.1	0.1	132882.0	0.5	0.5
Total for all 15 countries		4506794.2	17.2	4.9	6306495.1	23.6	19.4

Notes: * Refers to 1993. # Refers to 1995. G-77 website lists China as a Member of it, but China does not consider itself to be a Member of G-77. Classification of countries as developed, developing and transition economy is based on UN classification of countries as provided by UNCTAD.

Source: Author's compilation based on UNCTAD (2017), G-20 Website (www.g20.org) and G-77 website (www.g77.org)

[17] Chile's OFDI stock in 2016 constituted 45% of its GDP in 2016.

The other half of IFA proponents – Australia, Russia, Brazil, China, Hong Kong, South Korea and Mexico account for bulk of the OFDI and FDI by the IFA proponents; 97% of OFDI and 83% of FDI in 2016. Australia is the only country which had a better share in OFDI and FDI in 1990. All other countries have significantly enhanced their share in OFDI and FDI by 2016 as compared to 1990[18]. This half of IFA proponents, except for Australia, is a new class of countries emerging from developing countries and economies in transition, which have become host as well as home countries for foreign investment. They were already recipients of considerable FDI and now they have become important source of OFDI as well. Their experience as developing countries or former socialist countries, while makes them convinced of the need to maintain policy space in a multilateral agreement on foreign investment, their status as growing source of OFDI compels them to have in place a multilateral agreement that smoothens the process of accessing foreign markets.

Although IFA proposes to maintain policy space, it doesn't have anything that would ensure the policy space. Currently the policy space has been severely curtailed by IIAs and IFA proposes neither to address the challenges caused by IIAs nor to establish an alternate mechanism for the global governance of foreign investment. Due to this, IFA would not be adding any value to the existing system of global governance of foreign investment. But IFA would help in meeting the interests of the 'new class' of countries as the treaty would smoothen the process of market access even without binding commitments on market access. It is surprising that the proponents of IFA do not propose to have some responsibility fixed on investors towards host countries despite the fact that more than half of the IFA proponents are from G-77. The G-77 was established by a group of 77 developing countries in 1964 during the first session of the UNCTAD to articulate and promote the collective economic interests of developing countries. It was G-77 which took the lead in the negotiations on the UN Code. As negotiations progress, it is very likely that a division within IFA proponents emerge in the lines of the division during negotiations on the Code and Investment Agreement in WTO.

[18] With the exception of Brazil whose share in OFDI declined from 1.8% in 1990 to 0.7% in 2016.

Addressing of substantive and controversial issues

Most of the challenges to IFA would come from its handling of substantive and controversial issues. To avoid this challenge, it has been proposed that IFA would not contain any substantive provisions and it would avoid controversial and sensitive issues. This may be a wise strategy for the new class of countries, but the conventional host and home countries are likely to oppose a neutral treaty that does not address their concerns. As the interests of this new class of countries are more akin to the interests of developed countries in matters related to foreign investment – facilitate market access for their outward investments, it is possible that the IFA might incorporate provisions for binding commitments on market access and investment protection.

There is a view that developed countries have arrived at a consensus on their approach to global rules on foreign investment. According to Berger (2016) one sign of this convergence is the *Statement of EU and US on Shared Principles for International Investment* adopted in 2012 in the context of Transatlantic Trade and Investment Partnership (TTIP) negotiations. The shared principles point out that the essential elements in the EU and US approach to rules on foreign investment consist of broad market access to foreign investors, strong protection for investors and investments and fair and binding dispute settlement[19]. If IFA incorporates substantive issues, it may receive the support of advanced countries. Securing market access for their investments and protection of their investors and investments are in the interests of the new class of countries. The transition of China from a developing country host country to an emerging economy home country best illustrates the transition in the approach of new class of countries. In its first generation IIAs (from 1982 to 1998) when China was a net capital importing country, it adopted a restrictive approach to ISDS: exhaustion of local remedies was a pre-condition and ISDS was limited to disputes concerning compensation amount for expropriation. But as China experienced phenomenal growth in the outflow of foreign investment[20], its approach to ISDS also

[19] *Statement of European Union and United States on Shared Principles for International Investment*, http://trade.ec.europa.eu/doclib/docs/2012/april/tradoc_149331.pdf

[20] During the period between 2000 and 2014, OFDI (stock) from China grew 2527% whereas FDI (stock) grew at 461%. This calculation is based on FDI inflow and outflow data of China (mainland) provided in World Investment Report 2015.

changed. China's post-1998 IIAs do not insist on exhaustion of local remedies and it is open to all sorts of claims (Berger 2008)[21]. Except Brazil, all the other TFA proponents already have ISDS in their IIAs[22].

But when it comes to dispute settlement provisions, one is not able to judge how the advanced countries would respond. Although EU and US have declared the shared principles, there is considerable divergence in the views of the two sides on a desirable dispute settlement mechanism. The uneasiness of US to the new approach of EU that investor-state dispute settlement (ISDS) should be transformed into the form of a court system, i.e., International Investment Court (IIC), with permanent judges and provision for appeal reveals the emerging divergences in the approaches of EU and US. According to EU, a court type mechanism is required to overcome the legitimacy crisis facing the ISDS today, i.e. to ensure transparency, consistency of interpretations and predictability of interpretations of various provisions. The investment chapter of EU-Canada Comprehensive Economic and Trade Agreement (CETA) has been amended to incorporate the provision for an IIC for the purposes of settlement of disputes. It was reported that EU and Canada initiated an informal discussion during the World Economic Forum at Davos during 17-20 January 2017 on having a Multilateral Agreement on Investment (MAI) in WTO with IIC provisions[23]. US is wary of IIC because it fears that the new system would undermine the advantage US has with the current ISDS system, i.e. in the words of then US Trade Representative Michael Froman "because of the high standards and safeguards in our agreements, there have been very few cases against the U.S., and to date, the government has never lost"[24].

[21] It requires investors to exhaust local administrative review to determine the proper and legal conduct of Chinese administrative agencies. This, however, does not involve judicial process (Berger 2008).

[22] Brazil has adopted a different approach to IIAs as they limit state's right to regulate and discriminate between foreign and domestic investors. The IIAs of Brazil, which it calls Cooperation and Facilitation Investment Agreement (CFIA), are built on a cooperative approach taking into consideration the mutual benefit of investors and state. The national focal points or ombudsperson are expected to sort out the issues an investor may face and in case the issues have not been sorted out at the national focal point level, CFIA provides that the state involved may initiate international arbitration.

[23] "Multilateral Investment Pact: India against Canada EU bid on investment agreement at WTO", *Indian Express*, 24 January 2017. Available at http://indianexpress.com/article/business/business-others/multilateral-investment-pact-india-against-canada-eu-bid-on-investment-agreement-at-wto-4488472/

[24] "US wary of EU Proposal for Investment Court in Trade Pact", http://www.reuters.com/article/us-trade-ttip/u-s-wary-of-eu-proposal-for-investment-court-in-trade-pact-idUSKCN0SN2LH20151029

IFA may not receive support from advanced countries and developing countries with its current provisions. The support of EU, Norway, Japan and Switzerland in the WTO General Council for the adoption of IFA as an agenda item for the upcoming ministerial meeting need not be seen as support to IFA in its current form. It was most likely a move to get a modified version of the failed multilateral agreement on investment (MAI) of OECD into WTO in the backdrop of IFA[25]. The US, however, is opposed to IFA. Even if IFA proponents manage to receive the support of advanced countries, dispute settlement is going to be the hard nut to crack. The developing countries, the host countries, are not likely to support IFA with its current provision or with substantive provisions.

Definition of Investment

The definition of investment has become central to the investment-development linkage debate. A broad definition of investment along with strong investment protection measures will considerably squeeze the policy space of the host countries.

Although two Agreements of WTO – TRIMS and GATS cover investment, the term investment has not been defined in WTO. As the scope of investment in these agreements is limited, absence of definition of investment was not felt to be a major problem. TRIMS covers only trade related investment measures and GATS covers only FDI in services through commercial presence (mode 3).

Even though the scope of IFA is limited to investments for the production of goods and services, a number of new issues are now coming up which were not the case with GATS and TRIMS. Would a proprietary technology used in the production of goods or supply of services be considered as investment? The IIAs define investment very broadly to cover every asset an investor may possess. The EU-Canada CETA defines investment as "every kind of asset that an investor owns or controls, directly or indirectly, that has the characteristics of an investment, which includes a certain

[25] General Council meeting held on 10 May 2017. Due to the objection of Members like India, Uganda, Ecuador and Bolivia, TFA was not made a part of the agenda. This does not mean at this stage that IFA will not be considered for negotiation in the upcoming Ministerial Meeting.

duration and other characteristics such as the commitment of capital or other resources, the expectation of gain or profit, or the assumption of risk"[26]. It clarifies that investment could be in the forms such as shares, stocks and other forms of equity participation in an enterprise, IPRs, etc. Similar is the definition of investment used in the investment chapter of the Regional Comprehensive Economic Partnership (RCEP) to which four of the IFA proponents are parties to the negotiations. The implication of a broad definition of investment is that commitments that Members have accepted in other agreements such as TRIPS will also come under the purview of IFA as IPRs will be treated as investments. It is precisely for this reason that mentioning of TRIPS in the submission of MIKTA becomes significant.

A broad definition of investment may not distinguish between FDI and FPI which have very different implications for development. The reference to TRIPS as having significance for investment in the submission of MIKTA indicates that IFA might take a broad view in defining the term investment. During the earlier informal negotiations on an investment agreement within WTO, the advanced countries have been demanding a broad treatment to the term investment. Any inclination of IFA to define investment broadly is likely to face stiff resistance from developing countries. Defining investment has been a tough task in WTO that the Working Group of Trade and Investment which was established in 1996 and mandated to define investment did not arrive at a definition so far.

India's Response to IFA

India is not opposed to investment facilitation *per se*, but it is opposed to a multilateral IFA under the aegis of WTO. In the last BRICS summit which was held in September 2017 in China, India along with other BRICS countries approved the key aspects of investment facilitation among BRICS countries. The priorities of investment facilitation are in enhancing transparency, improving efficiency and promoting cooperation[27]. In July 2017, India and EU established an investment facilitation mechanism to promote and facilitate EU investment in India (MoCI 2017). The press release states that this

[26] Article 8.1.

[27] *Outlines for BRICS Investment Facilitation*, 31 August 2017, https://www.brics2017.org/wdfj/201708/t20170831_1829.html

mechanism includes "identifying and putting in place solutions to procedural impediments faced by EU companies and investors in establishing or running their operations in India"[28].

India has serious concerns on the likely shape the IFA would take once the formal negotiation is permitted in WTO. An agreement with binding commitments on market access and ISDS would amount to surrendering of policy space to decide on FDI norms and arbitration clauses. Due to this concern, India has made clear while agreeing to participate in the investment facilitation mechanism of BRICS that the negotiations at the BRICS forum would not be used for a similar agreement in WTO. When EU and Canada initiated an informal discussion on a possible multilateral investment agreement in WTO with ISDS, India outrightly rejected the idea[29]. The support of leading advanced countries to IFA in the WTO General Council meeting lends weight to India's apprehensions. In the WTO General Council meeting held on 10th May 2017, India opposed the inclusion of IFA in the agenda of upcoming ministerial meeting (Raghavan 2017).

There is a counterview expressed by some scholars that India should join efforts to an agreement on investment in WTO. A major reason to support this view is the fact that India has emerged as a capital exporting country. Ranjan (2017) while suggesting that India should join the efforts of EU and Canada to establish a MIA, points out that India's OFDI has grown tremendously in the last one and a half decade; from less than \$1billion in 2000-01 to more than \$21billion in 2015-16[30]. Growing recognition of India as an exporter of capital is also manifested in the decision of the UNCTAD journal - *Transnational Corporations* to have a special issue dedicated to outward investments

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[28] *ibid.*

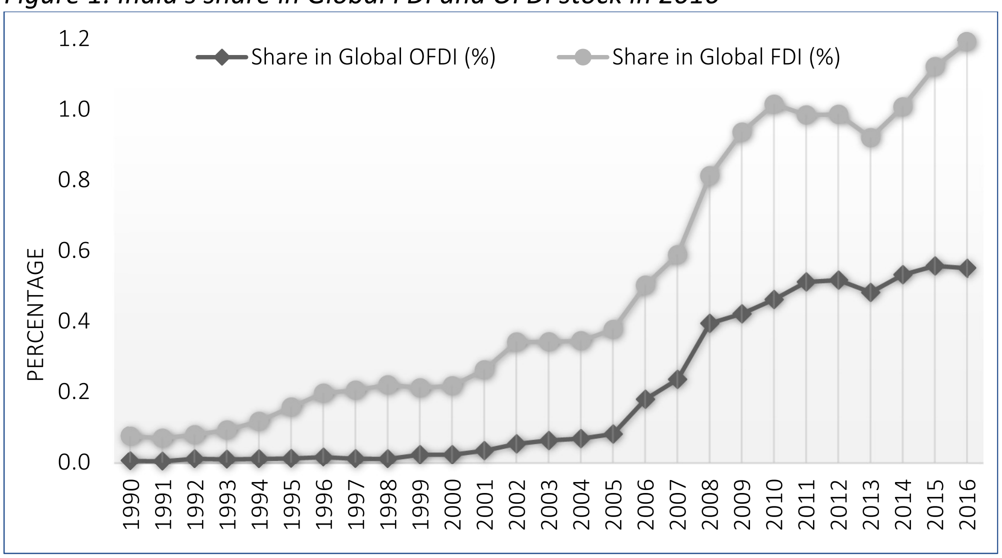
[29] "Multilateral Investment Pact: India against Canada EU bid on investment agreement at WTO", *Indian Express*, 24 January 2017. Available at http://indianexpress.com/article/business/business-others/multilateral-investment-pact-india-against-canada-eu-bid-on-investment-agreement-at-wto-4488472/

[30] It seems that the data which Ranjan (2017) has cited is taken from RBI's 'Data on Overseas Investment'. This data of RBI includes loans and guarantees issued apart from the investments in equity or direct investments. In 2015-16, equity investments constituted only 21.5% of the total oversees investments: Investments in equity was \$4.8billion and total overseas investment was \$22billion. These figures are based on the RBI data on overseas investment compiled by Prof. K.S. Chalapati Rao, ISID.

from India[31]. This counterview may imply that as an exporter of capital, a home country, India needs to do the needful to facilitate the efforts of its investors to get access to market in foreign territories which in turn will facilitate development in India.

A preliminary analysis of India's ODFI data suggests that India should continue to have a cautious approach to IFA. *Figure 1* shows that although India's contribution to global OFDI has grown in the last one and a half decades, its share in the investment inflows is growing at a higher pace. This indicates that India is still banking on import of capital rather than export of capital to meet its development requirements. The gap between India's OFDI stock and FDI stock in 2016 is $174.4billion[32]. Therefore, it may not be in India's interest to become party to a treaty, the future course of which is highly unpredictable at this stage.

Figure 1: India's share in Global FDI and OFDI stock in 2016



Source: Author's compilation based on UNCTAD (2017).

Concluding Remarks

Although IFA has been proposed in the background the positive impact foreign investment has on development, it contains nothing significant that would provide the policy space that is required for development. The assurance it attempts to make on protecting the regulatory autonomy of sovereign countries does not make much sense

[31] Vol 24, No.1, 1 April 2017

[32] Calculation based on FDI and OFDI data provided by UNCTAD (2017).

since the large number of IIAs has already substantially curtailed the policy space of host countries and IFA does not aim to address it. India should move very carefully in dealing with the proposal. There is a view that India should become party to this treaty as India is emerging as an important source of OFDI. But the fact of the matter is India relies on FDI much more than OFDI for meeting its requirements.

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