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Research Report

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The futile debate over a multilateral framework for investment

by

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One of the recurrent debates on international investment rule-making relates to the question whether it is possible to establish a multilateral framework for investment (MFI). Proponents argue that growing foreign direct investment (FDI) from emerging countries, especially China, contributes to a new consensus on global investment rules.¹

The crucial question however, should not be whether it is possible to negotiate an MFI (function follows form) but whether an MFI would be the right institutional form to align investment rule-making with sustainable development (form follows function).

If we follow the latter logic, we may realize that we already have elements of a multilateral investment law on the basis of bilateral investment treaties (BITs),² which decreases the need for a formal treaty. Furthermore, an MFI may not necessarily be the best institutional fix to tackle the most pressing challenges in the current investment regime. These include the ineffectiveness of BITs to promote FDI, their undue restrictiveness on host countries' policy space and the incoherence of investment rules.³

First, an MFI would only lead to more FDI – as a result of lower transaction costs for foreign investors – if it supplants existing BITs. As this consolidation seems unlikely, an MFI would merely add another layer to an already complex and fragmented system. Second, it seems unlikely that an MFI would help to increase host countries' policy space to enhance the contribution of FDI to national development. Even if developing countries could use their collective voice in a multilateral forum to establish development-friendly investment rules, this might lead to a pullback by capital-exporting countries. Potential confrontations at the multilateral level could undermine policy changes already underway at the regional level. Third, a standalone MFI would not lead to greater coherence of investment rules in relation to other economic as well as public policies. Finally, with the WTO in deep crisis and unable to integrate investment into a comprehensive set of new trade rules, it remains uncertain in which forum an MFI could be negotiated.

Against this background, policymakers should instead focus on the regional level to address the shortcomings of the international investment regime. The regionalization of investment rule-making is already in full swing and has reached a new level with the negotiations of

major preferential trade and investment treaties (PTIAs) such as the Trans-Pacific Partnership, the Regional Comprehensive Economic Partnership among ASEAN+6 countries and the Transatlantic Trade and Investment Partnership.

The combination of investment, trade, service, and intellectual property rights disciplines in PTIAs better reflects current economic realities in which business is increasingly conducted in the framework of complex value chains. The embedding of investment rules increases the potential to increase coherence across different disciplines. PTIAs often include more balanced obligations and establish exceptions, which encompass environmental and labor protections and enhance host countries' policy space. Furthermore, most of these agreements entail market access provisions to improve the agreements' effectiveness in promoting FDI flows.⁴

Of course, moving the negotiation of investment rules from the bilateral to the regional level alone is no panacea. It must be ensured that the increasing number of PTIAs leads to a consolidation of substantive and procedural investment rules. Traditional capital-exporting countries and emerging markets need to agree on the right balance between the protection, liberalization and regulation of FDI flows, investment by state-owned enterprises, and the integration of sustainability standards.

In view of the institutional crisis of the WTO and past failures of the OECD and the United Nations, the current global governance system seems ill-equipped to forge a global consensus on the above-mentioned topics. Fresh thinking about consensus-building processes is needed. The *Perspective* by Karl P. Sauvant and Federico Ortino is a good starting point for such a debate.⁵

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¹ See e.g., World Economic Forum, "Foreign direct investment as a key driver for Trade, growth and prosperity: The case for a multilateral agreement on investment", available at: http://www3.weforum.org/docs/GAC13/WEF_GAC_GlobalTradeFDI_FDIKeyDriver_Report_2013.pdf.

² Stephan Schill, *The Multilateralization of International Investment Law* (Cambridge: Cambridge University Press, 2009).

³ See Axel Berger, "Do we really need a multilateral investment agreement?," German Development Institute (DIE) Briefing Paper 9/2013 (Bonn: DIE, 2013), available at: [http://www.die-gdi.de/CMS-Homepage/openwebcms3.nsf/%28ynDK_contentByKey%29/ANES-96PAL3/\\$FILE/BP%209.2013.pdf](http://www.die-gdi.de/CMS-Homepage/openwebcms3.nsf/%28ynDK_contentByKey%29/ANES-96PAL3/$FILE/BP%209.2013.pdf).

⁴ Axel Berger, Matthias Busse, Peter Nunnenkamp, and Martin Roy, "Do trade and investment agreements lead to more FDI? Accounting for key provisions inside the black box," *International Economics and Economic Policy* (April 2012), DOI: 10.1007/s10368-012-0207-6.

⁵ "The need for an international investment consensus-building process," *Columbia FDI Perspectives*, No. 101, August 12, 2013.

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