BIAC Thought Starter

A Proactive Investment Agenda

The creation of the OECD Working Party on Responsible Business Conduct represents an opportunity for the Investment Committee and its Working Party on Investment to focus their attention on investment protection and liberalization issues and to have an in-depth discussion on high-priority projects that need to continue as well as new work that should be undertaken in this context. BIAC would therefore like to submit its suggestions for a “pro-active investment agenda,” which we would be pleased to discuss with the OECD Investment Committee.

Introduction

Investment liberalization has been an essential prerequisite for economic growth worldwide over the past decades. However, in the light of resurgence in economic uncertainty, new restrictive measures are being introduced and foreign investors are witnessing a revival of restrictive foreign investment regulation and protectionist rhetoric. In 2012, global foreign direct investment (FDI) inflows declined by 18%, to an estimated US$1.3 trillion, due mainly to macroeconomic fragility and policy uncertainty for investors which was marked by fears of sovereign debt crisis in Europe and a slowdown of growth in major emerging market economies.

Restrictions on FDI through various forms of investment protectionism can have significant adverse economic consequences for the global economic system overall and as a consequence for job creation, which is urgently needed. Hence, it is necessary to shed light on the issue of investment protectionism both at the national level and through international dialogue and cooperation. BIAC believes that the OECD can play an important role by highlighting the benefits of foreign investment and in addressing protectionist actions. In this context, we would like to draw attention to the following areas of concern:
Home country issues

- Increasing criticisms towards outward investment

In times of economic uncertainty, there is a considerable risk of countries resorting to protectionist investment measures when addressing FDI. As highlighted by the 2012 UNCTAD Investment Report, a number of countries have taken a more critical approach to outward investment, including restrictions on FDI and incentives to repatriate FDI. In the light of rising or high unemployment in a number of countries, concerns are increasingly being expressed that outward FDI can contribute to job exports and a weakening of the domestic industrial base. However, this reflects a fundamental misunderstanding of the benefits of both inward and outward investments as they contribute to companies’ overall competitiveness and thus the economic well-being of a country’s economy and its citizens.

For example, investment outflows enhance the competitiveness of multinational parent companies by allowing them to better serve foreign markets. Further, they can complement important parent activities such as exports. These findings suggest that the labour market impact of reduced export of goods and services produced domestically is more than offset by a positive scale effect due to improved competitiveness and better market access abroad. The ability of companies to make a positive contribution in their home economy is enhanced, not reduced, by companies’ global engagement. In this context, we would like to underline that the OECD’s ongoing work on Measuring Trade in Value Added and Global Value Chains contributes significantly to a better understanding of the new realities of international trade and investment, including its costs and benefits.

We encourage the OECD to contribute to a more balanced understanding of the effects of outward investment in home countries and to highlight the benefits at high political level.

Host country issues

- Forced localization requirements

Industry is increasingly concerned with forced localization requirements that companies are facing around the world. The issue of forced localization can take various forms as there are a variety of ways to force foreign companies to invest, procure, export from, or otherwise locate economic activity in those foreign jurisdictions. Such practise of forced localization has been exacerbated with the global economic downturn. Furthermore, as is the case with other forms of protectionism, forced localization in one country encourages the spread of forced localization to other countries, to the detriment of global commerce and domestic economies alike.

The OECD could play an important role by cataloguing and analyzing specific examples of the requirements companies are facing, thus helping to address them and increasing transparency on forced localization practices.
Investment and cloud computing

One recent concern for investors relates to the location of data storage, servers and information. Increasingly, global businesses are taking advantage of technology to centralize and regionalize data storage in order to remain competitive in the market. But many governments are proposing new legislation based on privacy or national security considerations, and demanding investors to use data storage facilities inside national borders, thus raising costs and reducing agility, integration, responsiveness and competitiveness for global companies.

We encourage the OECD to carry out fact-based analysis on policy concerns expressed by governments and the legitimate interests of business.

Investment screening and national security

Investment screens for the purpose of national security are legitimate. However, broad and sweeping definitions of national security can provide governments with the possibility to block investment to serve protectionist measures. While protecting national security must be a top priority for governments, it is also important to keep in mind the negative impact of tighter investment procedures on cross-border investment, growth and job creation. Rules should not be tightened for national security reasons without seriously exploring all possible alternative measures. The legitimate concerns about protection of national security should not be used as a cover for protectionism. In times of economic uncertainty, there is a considerable risk of countries resorting to protectionist investment measures when addressing FDI and referring to “national security” in an increasingly politicized context. Nonetheless, it is important to bear in mind that most foreign investments do not raise real national security concerns.

The OECD should help identify international best practices in addressing security concerns in a manner consistent with open investment policies and include this issue in their 2013-2014 program of work.

Bilateral issues

Criticism of Bilateral Investment Treaties

International companies are prepared to deploy great sums of capital in pursuit of international investment opportunities. However, as the volume of money invested rises, so does the risk. Investors need to mitigate those growing risks if potential FDI flows are to be realized. Bilateral Investment Treaties (BITs) have been used as an important tool for attracting and protecting international investment and ensuring a predictable and fair treatment of investors. BITs typically guarantee certain standards of treatment for foreign investors, such as fair and equitable national treatment for foreign investors in accordance with international standards, which is one of the key basic principles of foreign investment.
protection. They are therefore a crucial instrument and an important element in international investment decisions by companies.

Unfortunately, BITs have increasingly come under attack and have been subject to criticism from some political parties and NGOs, who allege that they are mainly designed to protect foreign investors and do not sufficiently take into account obligations and standards to protect the environment, human rights, labour rights and social provision. However, these statements are to a large extent based on misconception without sufficient proof to support these arguments and without taking into account the real nature of BITs which aim to avoid discriminatory treatment of foreign investments.

**We encourage the OECD to carry out fact-based analysis on the role of BITs to create an open international investment climate and provide protection for investments in uncertain environments, and to objectively analyse criticism according to which they might limit the policy space of host countries. The informal expert meeting on BITs is an important first step in this direction.**

✧ **Criticism of Investor-State Dispute Settlement**

Investor-State Dispute Settlement (ISDS) provisions are a primary component of investment treaties. ISDS allows individual investors to initiate dispute settlement proceedings against a host State on a neutral international arbitration forum, without requiring the investor to seek relief in local courts or tribunals. This independent arbitration is fundamental to investment protection to offer an alternative for the local judicial regime and resolve potential disputes over breaches of contracts and agreements.

ISDS is an essential element in major international investment decisions. ISDS can provide businesses with a better leverage for proper discussions with host governments to resolve problems. For investors, ISDS affords promise of a fair, unbiased resolution for disputes outside the potential control of the host government which could be a party, directly or indirectly in such disputes. Without ISDS, investors have no resort to protect global investment and business activities from unreasonable exercise of states’ authority.

**BIAC calls on the OECD to highlight the importance of strong ISDS in investment treaties and international agreements, including for many developing countries.**

✧ **Conflicting requirements and extraterritorial effects**

OECD member countries have adopted the *Declaration on International Investment and Multinational Enterprises* in 1976, with the aim of avoiding or minimising the imposition of conflicting requirements on multinational enterprises by governments. The Declaration consists of four elements: (1) National Treatment, (2) Conflicting requirements, (3) International investment incentives and disincentives and (4) the Guidelines for Multinational Enterprises.
Nevertheless, the recommendation on conflicting requirements is rarely given much visibility and often overlooked in practise. However, a significant rise in the use of extraterritorial jurisdiction as well as application of conflicting rules are burdensome to multinational activity and hence, poses a serious obstacle to international investment. It raises concerns for the international business community because the exercise of direct extraterritorial jurisdiction, in particular, may create an unlevel playing field as well as increase the risk of litigation and transaction costs.

**BIAC therefore encourages the OECD to safeguard the full effect of the OECD Council recommendation on conflicting requirements and monitor its application on a yearly basis.**

- Using Aid to Leverage Private Investment for Development

Recognising that Overseas Development Aid (ODA) cannot single-handedly bring about strong, sustainable and inclusive development in developing countries, private sector investment is essential. This was clearly recognised at the Fourth High-Level Forum on Aid Effectiveness in Busan in 2011 – in both the main Busan Partnership Document (available here) and also the joint public-private statement on Expanding and Enhancing Public and Private Co-operation for Broad-based, Inclusive and Sustainable Growth (available here).

Increasing focus is now therefore being placed on using aid to leverage private investments, such as through public-private partnerships (PPPs) and other innovative financing mechanisms. At the same time, it is crucial for developing countries to create the enabling policy environments conducive to business activities. These are the sorts of issues that the new Global Partnership for Effective Development Co-operation seeks to address, and the OECD can play a significant role in contributing its expertise.

**BIAC sees a clear role for the OECD Advisory Group on Investment and Development to examine and share lessons learned about the use of aid to leverage private investment for development and create an enabling business environment. We are eager to engage in the proposed review of the Policy Framework for Investment.**

- Clear, stable and predictable tax frameworks for promoting investment

An important element of an investment environment is the framework for taxation. Clear, stable, transparent tax policies and tax administrations that support and do not impede investment are critical to support investment. OECD tax instruments such as the OECD Model Tax Convention and the OECD Transfer Pricing Guidelines are important underpinnings of global FDI. Tax policy is also a key factor in domestic resource mobilisation supporting economic development. The OECD with its expertise in both taxation and investment should ensure that tax policies are not used for protectionist purposes, hampering cross-border trade and investment.
In the context of current global economic challenges and evolving business models, we need to be careful about radically changing tax principles that have served to enhance global growth and jobs over the past 50 years. However, it seems clear that in some areas international tax rules have not kept pace with globalised business practices. We believe that the project on Base Erosion and Profit Shifting (BEPS) the OECD CFA is about to undertake is the best way to look at the complete range of issues holistically, rather than focussing on just one small piece of the puzzle. BIAC intends to engage constructively in this project.

**BIAC recommends that OECD work in taxation be coordinated with OECD work on Freedom for Investment where relevant, and work to ensure that tax policies do not overtly or inadvertently lead to protectionism and do support growth.**

- **Competitive neutrality and state-owned enterprises**

Ensuring competitive neutrality is a key issue for the OECD business community. BIAC has therefore repeatedly expressed its strong support for an ambitious work program in this area, bringing together the expertise of different OECD committees. Building on the 2012 OECD report “Competitive Neutrality: Maintaining a Level Playing Field” we encourage the Investment Committee to get actively involved in future work in this area. Such work could include, for example, an inventory of state aid practices and an analysis of their effects on investment, which should detail financial, non-financial and other advantages which accrue to SOEs by virtue of their ownership by the state. Due consideration should be given to the cross-linkages between investment protection, liberalization and competitive neutrality.

As much of the global growth is taking place in emerging markets, activities on this issue should not be limited to OECD countries. The OECD can make an important contribution by providing a deeper and wider understanding of the key challenges and opportunities, while fostering capacity building by sharing its analysis with emerging economies and engaging in a constructive dialogue with them.

**BIAC encourages the Investment Committee to contribute to a robust, broad-based and evidence-based OECD work program on competitive neutrality, which would usefully complement work carried out by other parts of the Organization.**

- **OECD data and analysis**

The effectiveness of investment promotion depends heavily on the accuracy and reliability of FDI data. Objective and reliable data pave the way for more effective policy making and provide investors with the necessary data to make informed decisions. Therefore, it is essential to highlight the importance of raising the visibility of OECD data. The OECD plays a critical role by providing data and data analysis for policymakers to formulate sound
policies. In the generation of high streams of data every day, it is necessary to build a more concerted effort to promote transparency and raise visibility of these data beyond the OECD, including at the G20 level.

Further, we are witnessing a number of trends that are reshaping international investment patterns. For example, emerging markets have become increasingly important sources of international investment. International investment by SOEs has been growing rapidly. There is a growing dialogue of cross-sectoral exchanges across national borders towards achieving sustainable economic development. In the evolving global landscape for international investment, it remains inevitable to develop improved data and empirical analysis of emerging new trends in order to meet the demand for the kinds of data and analysis needed to support in the changing investment climate.

**A clear role for the OECD**

At their last summit in Los Cabos, G20 Leaders expressed their firm commitment to open trade and investment, expanding markets and resisting protectionism in all its forms. Recognizing the importance of investment for economic growth, BIAC calls on policy makers to put in place a supportive business environment and refrain from putting protectionist measures in place. Truly open investment flows require:

- adherence to the rule of law and to effective dispute settlement;
- assurance of fair and non-discriminatory treatment for foreign investors;
- freedom to own and control one’s own investment;
- adherence to key principles and declarations, such as the OECD Declaration on International Investment and Multinational Enterprises.

BIAC believes that the OECD should play a leading role in the international debate on freedom of cross-border investment which is at the core of the OECD mission and provide leadership to shape further understanding about the issues that are at stake. We urge the OECD to embark on an ambitious pro-active investment program and confirm the Organization’s leading role in ensuring that markets are kept open for foreign investment, with a view to boost economic growth and foster job creation. We count on the OECD to speak up and highlight its analysis and policy recommendations both at national and international levels.

Apart from its leading role in analysis and policy recommendations, BIAC also sees an important function for the OECD in examining individual cases in which the freedom of investment seems to be jeopardized by policy action of Member States, in providing a forum for discussion with Member States in the Investment Committee on such cases, and in raising these issues at a high level within governments.