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CHAPTER VI

HOME COUNTRIES AND INVESTORS

The investment process involves host countries, home countries and TNCs making investments. In general only the host country has been addressed in IIAs, with the most important and sensitive aspects reviewed in the preceding chapters. In future IIAs consideration should especially also go to home countries, actual parties to such agreements, to encourage FDI flows to developing countries and help increase the benefits from them. It is against this background that this chapter takes up home country measures and good corporate citizenship.

Home country measures (HCMs) seek to facilitate—partly in the interest of home countries themselves—FDI flows into developing countries by helping to overcome various problems that developing countries face when seeking to attract FDI and increasing benefits from it. Good corporate citizenship makes relations harmonious between investors and the economies they operate in—and it can help advance development. How future IIAs will deal with these matters is an open question. The analysis here explores options for governments to consider.

A. Home country measures

Outward FDI from developing countries increased rapidly in the late 1990s, but they remain net importers of FDI. Developed countries, by contrast, have a more balanced pattern of inward and outward flows.[1] So the focus for most developing countries and economies in transition is to attract inward FDI and benefit more from it. Measures that facilitate more and better FDI into developing countries—and that address concerns related to such investment—would do more than help developing countries. They could also be undertaken by "self-enlightened" home countries to create new investment and trade opportunities for their business communities.

Many developed home countries already have in place a wide range of unilateral policies and measures in this area. But IIAs have traditionally paid limited attention to them. Possible options range from hortatory policy declarations that recognize the need for home countries to promote FDI into developing host countries—to mandatory assistance and cooperation obligations set out in the agreements themselves. Binding commitments might make HCMs more transparent, stable and secure than if they are entirely voluntary, the norm today.

1. Broad scope of measures

Many types of HCMs can influence the magnitude and the quality of FDI flows to developing host countries.

- General aid-based development assistance to strengthen a host country's business environment.
- Improving the access of goods and services produced by developing countries to the markets of the developed countries.[2]

While aid-based measures and market access are important, the focus here is on measures directly related to FDI,[3] many of them already undertaken by home countries (UNCTAD 2001a, pp. 8–11):

- *Liberalizing outflows*. Home countries can remove obstacles to FDI outflows.
- *Providing information*. They can assist developing countries in collecting and disseminating information related to investment opportunities through cooperation with investment promotion agencies (IPAs), the provision of technical assistance, the organization of investment missions and seminars and the like.
- *Encouraging technology transfers*. Home countries can promote technology transfer by providing assistance to strengthen a host country's technological base, its capacity to act as a host to FDI in technology-intensive industries and its capacity in reaching specific technology-intensive goals.

- *Providing incentives to outward investors.* Various forms of financial and fiscal incentives can be provided to outward investors or to support feasibility studies and environmental assessments.
- *Mitigating risk.* Home countries can help to mitigate risk—say, by providing investment insurance against losses arising from political or other non-commercial risks that may not normally be covered through the private insurance market.

In addition, some new issues are being raised. These require the use of a home country's legal and regulatory system to ensure that TNCs based there conform to certain standards of good corporate citizenship through the sanctions of such home country laws and regulations. Of significance has been the increasing demand to apply home country liability rules to parent companies for the wrongful acts of their foreign affiliates in developing countries (Muchlinski 2001a, 2001b). This has already occurred in the course of litigation, mainly in the United States and United Kingdom, where foreign claimants have sought redress for wrongs allegedly committed against them in the host country by foreign affiliates (United States Court of Appeals Second Circuit 1987; United Kingdom House of Lords 2000). Cases have been brought in the United States for alleged violations of fundamental human rights standards by United States-based TNCs in their foreign operations, under the Alien Tort Claims Act (Muchlinski 2001a, 2001b, 2002; United States Court of Appeal for the Ninth Circuit 2002).[4]

Other areas of concern to home countries, as the principal regulators of parent company activities, may include combating corruption by penalizing TNCs that use corrupt practices to further their FDI activities and regulating fraudulent behaviour and unacceptable corporate accounting practices that may adversely affect the global operations of TNCs.[5] Other possible action arises for the global environmental practices of TNCs, ranging from control over trade in hazardous technology to determining responsibility for environmental damage.

In addition, it might be possible for current policies of international cooperation to evolve in ways that assist developing countries. For example, if developing countries could gain access to the competition enforcement systems of the EU and the United States, this would empower them, in dealing with anticompetitive practices of TNCs, to use the stronger regulatory and institutional frameworks of developed countries. And developed home countries could perhaps do more to assist developing countries by sharing information about the "track record" of an investor, to alert host countries about firms with a poor record of business probity.

Such approaches do have problems. Under what conditions do claimants in a host country have the right to bring a claim before courts in the parent company's home country? Can they show that the parent firm was sufficiently involved in the alleged wrongdoing to be itself liable? Or in the absence of direct involvement in an alleged wrongdoing, can the parent firm nonetheless be held liable on the basis of "piercing of the corporate veil" between itself and its overseas affiliate?[6] Such litigation could however undermine the attraction of the home country as a base for TNCs, indeed encourage "floods of litigation" that the courts of a given home country might be unable to deal with (Lord Hoffmann 1997).

On some of these measures, a potential problem is that action by a home country involves an assertion of an extraterritorial jurisdiction to prescribe legal standards for operations that, by definition, occur in the territory of another sovereign State. This increases the risk of conflicting requirements, especially where policies and laws in the home and host countries diverge. The problem arises not only where there is a divergence of approach to the resolution of a common problem, but where different procedural policies apply. For example, disputes have arisen between the United States, European countries and Japan over extraterritorial prescription and enforcement of United States regulatory laws on foreign affiliates of United States companies and on non-United States companies that were allegedly involved in breaches of United States laws (Muchlinski 1999, chapter 5; Wallace 2002).

2. Current use by developed countries

All home countries have measures that affect FDI flows to developing countries. In general, developed countries have removed most national obstacles on outward FDI. But policy declarations aimed at encouraging outward FDI are seldom linked to specific international commitments to that effect (UNCTAD 2001a). With some exceptions, assistance remains at the discretion of each country and is commonly shaped to serve a home country's business interests and general development objectives. This home country perspective is especially evident in the design of financial or fiscal assistance programmes as well as preferential market access measures.

Information on the investment climate is an important element for FDI decisionmaking. Home country assistance can be offered to gather, publish and disseminate basic information on a country's regulatory framework, macroeconomic conditions, sectoral conditions and other factors that affect investment opportunities. Although host developing countries do compile many of these data, their efforts can be supported, particularly in the dissemination stage, by home country governments and relevant international institutions. Indeed, a number of home countries provide assistance of such a kind. For example, the Swiss Organisation for Facilitating Investments facilitates matchmaking between Swiss and foreign enterprises in developing countries and economies in transition and supports the transfer of know-how. At the international level, various programmes strengthen the capabilities of developing country IPAs and disseminate information about investment opportunities.[7]

Some HCMs are geared specifically to facilitating the transfer of technology (see IV.G), and several international agreements contain clauses in this regard. The measures include (UNCTAD 2001f):

- Supporting technology partnerships between firms from developed and developing countries to strengthen the technological capabilities of the latter, either through facilitating access to advanced technology or learning in the interaction between firms. Supported by various initiatives, such partnerships can take many forms, ranging from sharing technology on an ad hoc basis to entering long-term contractual or business engagements. The Business Linkages Challenge Fund of the United Kingdom is one such approach (box VI.1).
- Promoting the transfer of specific technology (such as telecommunications, energy production and environmental protection technologies) is at the heart of several developed country initiatives.
- Targeting measures for R&D at specific technological problems of developing countries can provide a venue for public-private cooperation in promoting transfers of technology.

Box VI.1. The Business Linkages Challenge Fund

Established by the Department for International Development in the United Kingdom, the Business Linkages Challenge Fund provides grants for the development of innovative business linkages that transfer the technology, skills, information and market access necessary for LDC enterprises to compete in the global economy and bring benefits to the poor. Grants of £50,000 to £1 million are allocated on a competitive basis, and bids must be led by private sector partners. All grant awards have to be matched by an equal or greater contribution from the linkage partners.

Projects must be implemented in LDCs. The target are countries in central and southern Africa and in the Caribbean. One leg of the partnership must fall within a targeted country. But because the United Kingdom qualifies as a targeted country, linkage partnerships between United Kingdom companies and developing country counterparts can be supported. Similarly, partnerships between companies in South Africa and companies in developing countries outside the Fund's target regions are also eligible, hence the project in the United Republic of Tanzania linking with BP South Africa.

The programme has been running in sub-Saharan Africa and the Caribbean since 2001. To date, 32 projects have been supported, with total grants of £8 million and more than £10 million of private sector resources mobilized. In the United Republic of Tanzania, the Fund supports a project that aims to develop links between BP Tanzania and other major local corporations, and local SME suppliers. The project builds on BP's experience working with local suppliers in South Africa to develop their capacity to latch onto the supply chains of large corporations. BP Tanzania's major partners include Kahama Mining Corporation, Kolombero Sugar Company, National Microfinance Bank, Sumaria Group, Tanga Cement Company and Tanzania Breweries. In 2002 the eight participating corporations spent 35% of their $60 million purchasing budget on supplies from SMEs. The objective of the project is to increase this proportion and gradually ratchet up the quality and complexity of goods and services bought locally, developing the "missing middle" of the Tanzanian economy.

Other project examples include linkages between a sports management company in the United Kingdom and South African partners, to expand the capacity in South Africa to host and staff major sporting events; linkages between small fruit farmers in Mozambique and South Africa to increase access to export markets in Europe; and linkages between a large cocoa cooperative in the Dominican Republic and a Swiss chocolate manufacturer to develop a supply of high-quality organic cocoa.

Source: United Kingdom, Department for International Development (DFID).

Many developed countries have specialized agencies to provide long-term financing for private sector development in developing and transition economies.[8] This assistance is usually channelled through development finance institutions that provide both loan and equity financing for FDI projects in developing countries, sometimes by taking minority equity positions. For example, the mission of the Overseas Private Investment Corporation (OPIC) of the United States is to mobilize and facilitate the participation of United States private capital and skills in the economic and social development of developing countries and economies in transition to complement the development assistance objectives of the United States. OPIC's main instruments are investment funds and medium- to long-term financing, but it also provides political risk insurance (see below). Several public organizations in developed countries support outward FDI by SMEs. The Swiss "Start-up Fund", for example, offers loans for studies, pilot projects, purchases of machinery and technology transfer.

Complementing these unilateral efforts are various schemes of international institutions that provide financial assistance for projects in developing countries (for a summary see Hughes and Brewster 2002). Within the World Bank Group, the International Finance Corporation and its decentralized instruments for the Caribbean and the South Pacific provide various forms of financial and technical assistance to promote private enterprise. The regional development banks use a range of instruments to facilitate investment in developing countries.[9] The Commonwealth Private Investment Initiative has established several investment funds.

In mitigating risk, investment insurance to alleviate non-commercial risk is particularly important. Some of the largest official bilateral insurers are OPIC (United States), the Export Insurance Department of the Ministry of Trade and Industry (Japan), HERMES and Treuarbeit (Germany), the Compagnie Française d'Assurance pour le Commerce Exterieur (France) and the Export Credit Guarantee Department (United Kingdom). Similar institutions exist in Australia, Canada, Italy, the Netherlands, Spain and Sweden (Mistry and Olesen 2003, pp. 212–213). In general, such insurers will only insure investment in developing countries with which their own countries have a bilateral investment treaty (BIT). In 2001, bilateral institutions insured outward FDI of some $20–25 billion (ibid.).

Of multilateral institutions, the Multilateral Investment Guarantee Agency (MIGA) is the most important, with a capital base of almost $2 billion in 2001.[10] The regional development banks and other institutions, such as the Inter-Arab Investment Guarantee Agency, also provide non-commercial risk insurance. In the EU, the European Investment Bank has established an "Investment Facility" to provide risk capital and guarantees in support of domestic and foreign investment, loans and credits (Cotonou Agreement, Article 76, Annex II, Article 2).

The trade policies of home countries—even though not FDI-specific—can also have an important effect on the scope for especially export-oriented FDI in developing countries. Non-reciprocal preferential schemes are particularly important here, including the Generalized System of Preferences, and trade preferences under the Cotonou Agreement, the Caribbean Basin Initiative, the EU's Everything-but-Arms Initiative and the United States' African Growth and Opportunity Act. The Government of Japan also grants certain LDC exports (corresponding to 99% of industrial products) duty-free and quota-free access to its market. Such schemes remain important for the location of export production but do not—in and by themselves—provide either a sufficient or a sustainable basis for developing competitive export industries. Home countries also use a variety of trade and industry policies to restrict access to their markets. These include anti-dumping and safeguard measures as well as targeted subsidies in developed countries.

3. Effectiveness

Lack of information and difficulties in isolating the influence of other factors complicate the evaluation of the effectiveness of the wide range of HCMs. In addition, the use and impact of HCMs is a vastly under-researched area. But some important considerations can be identified for enhancing the effectiveness of HCMs as a development tool.

A stronger link between the explicit needs of developing countries and the design and execution of HCMs would likely enhance the beneficial impact of such programmes on development. As noted earlier, most HCMs remain at the discretion of each developed country and are commonly shaped to serve a home country's own business interests along with general development objectives. Moreover, the awareness among developing countries of HCMs is generally low. Interviews with IPAs from developing countries indicate that HCMs are not yet regarded a strategic complementary element to their own promotion efforts. This may imply that the measures have not been well advertised or that they are not perceived to be very effective. It may also

suggest a need for closer developing country involvement in the design and execution of future HCMs.

For the dissemination of investment information, there is a clear need for assistance, especially for the least known FDI locations (such as LDCs) and for informing SMEs. For the 49 LDCs, investment guides of the sort produced by international consulting firms are available only exceptionally.[11] Nor do available sources always match the requirements of investors. The information revolution has in some ways aggravated the situation by sharpening the contrast between the LDCs and other countries—which can update information available through the Internet, for example.

On mitigating financial cost and risks, there are many examples of investments that have benefited from home country or international schemes for financing and investment insurance.[12] But it has also been argued that such efforts often do not trickle down to those countries that need assistance the most (Hughes and Brewster 2002). While most international finance institutions have policy statements that acknowledge the need to focus on such countries, LDCs tend to lag far behind the rest of the developing world in the use of finance and insurance schemes. One of the reasons is that many of the investment funds are publicly funded only in part and therefore tend to be managed on commercially based criteria, with less focus on the least developed investment locations as a result.

Interestingly, there seems to be a trend towards making HCMs more development-oriented. For example, the Government of Norway has obliged the Norwegian Investment Fund for Developing Countries to invest at least a third of its capital in LDCs, with the obligation to have Norwegian co-investors abolished.[13] A similar shift has been noted for OPIC (United States), which specified in its 2003 budget request that it would continue to refocus its efforts on providing support to projects in locations and sectors in which the developmental impact will be greatest.

HCMs could result in policy conflicts between host and home countries. One general issue is the potential for extraterritorial control. For example, home country tax policies and transfer pricing regulations sometimes influence FDI flows to developing countries. Some countries employ a residence-based system of taxing foreign source income and claim tax revenues on income generated worldwide. Such extraterritorial tax policies are based on a general principle that tax reductions should not encourage FDI from the home country—and may in effect offset the impact of lower tax rates or tax holidays offered by developing countries as an incentive to attract FDI. To counter such effects, several developed countries have adopted tax-sparing treaty practices. A contracting State agrees to grant relief from residence taxation for source taxes that have not actually been paid (taxes that have been "spared"). Because such clauses may induce firms to engage in sophisticated tax planning and avoidance behaviour, OECD guidelines include the specific inclusion in treaties of an anti-abuse clause and the setting of time limits for any tax-sparing relief (OECD 1998c).

4. The IIA dimension

Traditionally, HCMs have attracted little attention in IIAs, which have instead emphasized the obligations of host countries to protect inward FDI through their standards and guarantees. But with the investment process involving home countries, it is relevant to consider if and how HCMs are—and could be—addressed in IIAs. This question has implications for the potential development impact of such agreements and for the effectiveness of various HCMs. Arguably, the stronger the policy commitments in international agreements—running along a continuum from hortatory declarations to binding obligations accompanied by detailed implementation plans (backed by financial resources) and monitoring mechanisms—the bigger the likely impact of HCMs. Just as countries see advantages in complementing unilateral efforts in trade and investment liberalization with commitments in international agreements, IIA provisions addressing HCMs could lend greater transparency, predictability and stability to the way HCMs address development concerns (UNCTAD 2001a, p. 53).

Some emerging trends may be the basis for further developments in this field. These go beyond simple general exhortations for the parties to an IIA to promote investment through appropriate measures, which may, by implication, include investment-promoting HCMs.[14] They encompass, first, the emergence of a cooperation process expressed through international agreements involving multiple developed and developing countries and containing specific provisions on HCMs. Second, a number of IIAs contain cooperation provisions concerning technology transfer, possibly the most common type of HCM provision in these agreements. Third, regional and multilateral investment insurance schemes (such as that of MIGA) complement national insurance schemes.

For instruments involving multiple developing country participants, the key example is the Cotonou Agreement between the EU and the ACP countries, the successor to the Fourth Lomé Convention (UNCTAD 2001c, p. 441). It includes detailed provisions related to investment promotion, investment finance and support and investment guarantees (box VI.2). Moreover, in the area of investment protection, the Community and the ACP States affirm the need for such protection and the importance of concluding investment promotion and protection agreements, which could also provide the basis for investment insurance and guarantee schemes (Article 78). The parties also agree that special agreements on particular projects may be concluded, with the Community and

Box VI.2. Support for investment and private sector development in the Cotonou Agreement

Article 74

"Cooperation shall, through financial and technical assistance, support the policies and strategies for investment and private-sector development as set out in this Agreement."

Article 75: Investment promotion

"The ACP States, the Community and its Member States [...] shall:

(a) implement measures to encourage participation in their development efforts by private investors [...];
(b) take measures and actions which help to create and maintain a predictable and secure investment climate as well as enter into negotiations on agreements which will improve such climate;
(c) encourage the EU private sector to invest and to provide specific assistance to its counterparts in the ACP countries under mutual business cooperation and partnerships;
(d) facilitate partnerships and joint ventures by encouraging co-financing;
(e) sponsor sectoral investment fora to promote partnerships and external investment;
(f) support efforts of the ACP States to attract financing, with particular emphasis on private financing, for infrastructure investments and revenue-generating infrastructure critical for the private sector;
(g) support capacity-building for domestic investment promotion agencies and institutions involved in promoting and facilitating foreign investment;
(h) disseminate information on investment opportunities and business operating conditions in the ACP States;
(i) promote [...] private-sector business dialogue, cooperation and partnerships [...]."

Article 76: Investment finance and support

"1. Cooperation shall provide long-term financial resources, including risk capital, to assist in promoting growth in the private sector and help to mobilise domestic and foreign capital for this purpose. To this end, cooperation shall provide, in particular:

(a) grants for financial and technical assistance to support policy reforms, human resource development, institutional capacity-building or other forms of institutional support related to a specific investment, measures to increase the competitiveness of enterprises and to strengthen the capacities of the private financial and non-financial intermediaries, investment facilitation and promotion and competitiveness enhancement activities;
(b) advisory and consultative services to assist in creating a responsive investment climate and information base to guide and encourage the flow of capital;
(c) risk capital for equity or quasi-equity investments, guarantees in support of domestic and foreign private investment and loans or lines of credit [...];
(d) loans from the Bank's own resources. [...]."

Article 77: Investment guarantees

"[...] 2. Cooperation shall offer guarantees and assist with guarantees funds covering the risks for qualified investment. Specifically, cooperation shall provide support to:

(a) reinsurance schemes to cover foreign direct investment by eligible investors; against legal uncertainties and the major risks of expropriation, currency transfer restriction, war and civil disturbance, and breach of contract. [...]
(b) guarantee programmes to cover risk in the form of partial guarantees for debt financing. [...]
(c) national and regional guarantee funds, involving, in particular, domestic financial institutions or investors for encouraging the development of the financial sector.

3. Cooperation shall also provide support to capacity-building, institutional support and participation in the core funding of national and/ or regional initiatives to reduce the commercial risks for investors [...].

4. [...] The ACP and the EC will within the framework of the ACP-EC Development Finance Cooperation Committee undertake a joint study on the proposal to set up an ACP-EC Guarantee Agency to provide and manage investment guarantee programmes."

Source: UNCTAD 2001c, pp. 452–454.

European enterprises contributing to their financing. These provisions represent the most comprehensive instrument on HCMs concluded to date at the international level. But a careful evaluation of the implementation of these provisions (and the corresponding ones under Lomé IVbis) has still to be made. The prime instruments are the Investment Facility and Proinvest of the European Investment Bank.

Apart from the Cotonou Agreement, certain intra-regional cooperation agreements between developing countries introduce various home country commitments to promote investment in host countries party to the agreement. For example, the Treaty Establishing the Caribbean Community differentiates between the more and less developed countries among its membership, establishing a special regime for financial assistance "with a view to promoting the flows of investment capital to the Less Developed Countries" (chapter VII, article 59(1)). The Agreement on Investment and Free Movement of Arab Capital Among Arab Countries endorses a policy in article 1(a) that "Every Arab state exporting capital shall exert efforts to promote preferential investments in the other Arab states and provide whatever services and facilities required in this respect". As a follow-up mechanism to this commitment, the Convention Establishing the Inter-Arab Investment Guarantee Corporation provides investment insurance as well as other promotional activities designed to stimulate FDI.

Provisions encouraging development-oriented transfer of technology go beyond the sharing of know-how in most development assistance programmes and require a more substantial application of technology to business operations.[15] Most provisions dealing with this issue have tended to be non-binding hortatory provisions (see section IV.G).

For regional, interregional and multilateral investment insurance schemes, an early and continuing example is the Convention Establishing the Inter-Arab Investment Guarantee Corporation, which established an intra-regional insurance scheme for use by investors from an Arab home country in an Arab host country. More recently, as noted, the Cotonou Agreement has reaffirmed the importance of investment guarantee insurance. To this end, the Agreement calls for the ACP-EU Development Finance Cooperation Committee to "undertake a joint study on the proposal to set up an ACP-EU Guarantee Agency to provide and manage investment guarantee programmes" (Article 77(4), Cotonou Agreement in UNCTAD 2001a, p. 38). The only multilateral instrument in this field is the MIGA Convention approved in 1988. Its objective, under Article 2, is "to encourage the flow of investments for productive purposes among member countries, and, in particular to developing member countries". This is done by reducing investor concerns about non-commercial risk through a multilateral investment insurance fund to arrange cover against such risk.[16]

5. Enhancing the development dimension

Greater attention in IIAs to the role of HCMs by developed countries would help incorporate the "second point" of the triangular relationship between host countries, home countries and TNCs—and enhance the development dimension of FDI.[17] In the WTO Working Group on Trade and Investment, for example, some developing countries put the issue on the table. It has been argued that "Home governments should undertake obligations: (1) to refrain from policies or measures that influence [TNCs] originating in their territories to have operations or behaviour in host members that are adverse to the interests of the host members; (2) to institute measures that influence and oblige [TNCs] originating in their territories to behave and operate with full corporate responsibility and accountability in their operations in host members, and to fulfil their [...] obligations to the host member and government, in accordance with the objectives and policies of the latter."[18]

In a non-binding, hortatory approach a general expression of commitment to improving investment flows to developing country parties could be included, though its practical effect might be questioned. More concrete, but still non-binding, would be to link general policy language with more specific commitments to HCMs, possibly project-by-project. And commitments could be made on "soft" cooperation such as cooperative information exchange, assisted outreach to home-country business groups, FDI seminars and general education on business opportunities in developing countries.

An alternative approach is to introduce binding obligations to give assistance to host developing countries in promoting FDI. As noted, many developed countries—either unilaterally or through intermediaries—are already offering various measures. But such a step would give IIAs more balance in the distribution of rights and obligations of parties involved and could strengthen their impact as development-promoting instruments—while in most cases also serving the self-interest of home countries. In this situation, home countries would accept obligations, recognizing the real difficulties associated with turning the aspiration of host developing countries

for more investment into reality. The inclusion of obligations would seek to offset some of the locational disadvantages of developing host country parties not only through—in a defensive way—enhanced investor protection provisions of IIAs, but through proactive economic and commercial policies aimed at facilitating more and better FDI to developing countries, particularly the least developed.

Where possible, commitments should be linked to follow-up implementation programmes and specific mechanisms to monitor implementation. Practical outcomes are more likely if an agreement's general statement of policy principles is followed by provisions containing a more detailed list of measures or a specific implementation process that will translate policy into practice, including actions involving other types of HCMs. Some IIAs include for this purpose a provision for a "Supervisory Committee" to ensure the proper implementation of what has been agreed.[19] A forum is put in place for the future development of more specific policies of home country assistance for investment in host developing countries. The recent decision to introduce a monitoring mechanism to implement Article 66.2 of the TRIPS Agreement is an interesting step in this direction (box IV.7). Review and monitoring through follow-up mechanisms help create an organic progression in policy development through dialogue and the sharing of common experience. Indeed, as cooperation proceeds, more "hard" commitments, involving specific or general assistance through funded programmes, could become feasible. The utility of the organic development of cooperation in this field should not be overlooked.

A further issue is whether HCMs should be directed to a particular group of developing countries, such as the LDCs, under special and differential treatment provisions. LDCs are likely to need disproportionate help from home countries in attracting FDI. One recent study identified measures that home countries can take in the short, medium and long terms to mitigate risks and unblock FDI flows to LDCs by addressing both the entry-cost and post-entry risk barriers for investors (box VI.3). The Commonwealth Secretariat has

Box VI.3. Home country measures to mitigate risk linked to FDI in LDCs

In a study commissioned by the Government of Sweden on ways to mitigate risk associated with investing in LDCs, a number of measures were identified, some of them listed here:

Short-term measures to extend risk mitigation capabilities

- Increase funding of multilateral risk insurance agencies (such as MIGA and the political risk insurance facilities being opened up in regional banks) specifically to cover LDC political and other non-commercial risk through a special purpose capital or guarantee pool provided.
- Create more effective regional risk cover capacity either by: (a) regionalizing more effectively the operations of MIGA and transforming it into a more independent global facility; or (b) create separate MIGA-like regional multilateral political risk insurance capacity affiliated with the regional development banks.
- Increase the non-commercial risk insurance capacity of bilateral Export Credit Agencies and Official Bilateral Insurers through specific funding or subsidies for covering a much wider range of non-commercial risks in LDCs.
- Provide project-related subsidies to cover part of the premium costs for PRI or NCRI for specific projects being undertaken by OECD source country or eligible developing country firms in LDCs.
- Encourage the development of public-public partnerships between official bilateral insurers and their nascent counterparts in key developing countries that are becoming major home countries for FDI in neighbouring LDCs.
- Establish credit enhancement arrangements for mobilizing available domestic funding (in order to reduce currency risk) in developing countries (particularly LDCs).

Other short-term measures to increase FDI to LDCs

- Provide full (100%) or large partial (50–80%) tax credits, rebates or deductions for the equity invested by home country companies in LDCs against their tax liabilities in their home countries.
- Establish special-purpose "FDI-in-LDCs" investment promotion departments (with commensurate budgets) within bilateral aid or investment agencies thus ensuring that support for FDI flows would be as important a bilateral priority as any other in aid programmes. They could extend the limited capacity of LDC-IPAs by enabling them to leverage their limited resources. Their activities could include: determining investment priorities; targeting specific companies in their home countries; informing them of opportunities in LDCs; helping to finance environmental and social impact assessments; helping to prepare documentation

/...

suggested that a new facility be set up in the form of a dedicated and separate fund owned by international finance institutions but legally distinct from them. The fund would focus specifically on LDCs and other small and vulnerable economies. It would assist private investment in the production of traded goods and services in eligible States by offering domestic-currency loans, quasi-equity investment capital and guarantees—and by retailing a specially simplified form of MIGA cover for political risk (Hughes and Brewster 2002).

Dealing with HCMs is a new but potentially important aspect of how to make the evolving architecture of IIAs more development friendly. It is by no means an easy task, especially because the degree and extent of binding commitments on the part of home countries in IIAs have been rather limited. But all developed countries have already put various HCMs in place on their own. At the multilateral level, the Doha Declaration (paragraph 22) recognizes the need for any framework to "reflect in a balanced manner the interests of home and host countries". The same principle could apply to IIAs at other levels as well. This suggests that future IIAs should contain commitments for home country measures, building on the experience to date.

Box VI.3. Home country measures to mitigate risk linked to FDI in LDCs (concluded)

(such as Memoranda of Understanding, Letters of Intent) and institutional capacity building in partner-IPAs.

- Explore the possibility of establishing a small special purpose LDC Infrastructure Investment Fund that would provide equity and debt financing as well as mobilize domestic currency resources for lending to infrastructure projects in LDCs.

Medium-term initiatives by home countries

- Working with multilateral partners and the private sector to develop financial systems and capital markets of LDCs more rapidly than currently envisaged.
- Bilateral aid agencies can make a unique contribution over multilateral counterparts in engaging in intensive "regulatory-partnership" arrangements between financial system regulators in particular donor countries with regulatory agencies in LDCs to ensure not only that sound laws, rules and regulations are developed, but that they are applied and enforced.
- Bilateral aid agencies can provide seed funding to encourage their non-banking institutions to establish a presence in LDC financial systems that would be shunned by the private sector.
- Bilateral donors (especially members of the EU) can do more to provide open access to their domestic consumer markets to all products of LDCs; encourage their domestic firms through favourable tax treatment or through grant support for partial cost coverage to develop supply sources so that LDCs can take advantage of the preferential access they have but are not availing of and encourage developing country investors to invest in LDCs to take advantage of privileged access to donor markets.
- Set up an International Commercial Court specifically designed to resolve disputes between LDCs (not all developing countries) and foreign investors, especially where complex infrastructure investments involving regulatory risk are concerned.

Long-term options for home countries to consider

- Providing sustained long-term institutional and human capacity building assistance for LDC accounting, legal and judicial systems to improve their performance and capacities when it comes to dealing with foreign investors swiftly, impartially and equitably. Such assistance could be provided through counterpart accounting, legal firms and judiciaries in partner donor countries through long-term partnership programmes that would be partly funded by aid.
- Providing similar support for political and broader governance institutions, that is, government machinery and ministries, especially the law and justice ministries as well as for parliament and parliamentary institutions for the effective functioning of democracy and representative civil society institutions that can exert additional checks and balances in ways that even parliamentary systems in developed countries cannot. In some LDCs it may be appropriate to take a pause in pushing through successive rounds of fur ther economic reforms that are unlikely to work unless they can be embedded in political and judicial reform.
- Supporting the future evolution and development of political and non-commercial risk insurance capacity in their own domestic markets and in the wider regional European market through more productive public-private partnerships between official bilateral insurers and private risk insurers

Source: Mistry and Olesen 2003.

B. Good corporate citizenship

To what extent can foreign investors themselves complement the efforts of host (and home) countries and help especially developing countries to reap maximum benefits from FDI? There has been an increasing number of international instruments on this, but most of them are voluntary. Moreover, most instruments deal with social and environmental issues, leaving economic development issues out of their scope. Indeed, there has been a notable lack of debate on issues pertaining directly to the economic development interests of developing countries.

Even so, there are rising expectations that TNCs can contribute directly to the advance of development goals as one aspect of good corporate citizenship. Such firms are expected not only to abide by the laws of the host country, but also pay greater attention to contributing to public revenues, creating and upgrading linkages with local enterprises, creating employment opportunities, raising skill levels and transferring technology. But how could IIAs contribute to enhancing such good corporate practices, especially with international treaties normally focusing on State conduct, not on the conduct of non-State actors?

1. The concept

With liberalization and globalization, there is a greater mutual interest for host country governments and TNCs to cooperate with each other to achieve their public and private goals. Firms benefit from the more open, market-oriented and business-friendly policy frameworks of the recent decade. Host countries expect, in return, to draw net economic and social benefits from the presence of TNCs. As these firms have transnationalized, their impact on host countries has increased. A case can be made therefore that the increased role of TNCs, as the most important actors in the global economy, should be accompanied by an increased recognition of their responsibilities towards the countries in which they operate.

The concept that captures the essence of a cooperative relationship between TNCs and their host countries, aimed at achieving a balance of public and private objectives and benefits, is good corporate citizenship. It can complement actions of developing countries and home countries to maximize the benefits of FDI, while minimizing the costs. To ensure full support, however, the content of this concept should be defined with the full involvement of all stakeholders, beginning of course with business.

Good corporate citizenship encompasses standards of business behaviour that apply to domestic companies as well as TNCs. Still, TNCs are seen to have special responsibilities (especially in developing countries) because of their economic power and because they get rights under IIAs that can go beyond those available to domestic firms and because the capacity of many host developing countries to introduce and implement certain laws is limited.[20] Good corporate citizenship differs from the concept of "corporate social responsibility"[21] in that it addresses economic aspects more explicitly.[22] Normally, a company is a legal entity and thus the subject of direct rights and obligations under the law. But compliance with the law is little more than a minimum standard necessary for a company's existence and operation, especially in developing countries. Corporate citizenship commitments that extend beyond compliance with the letter of the law are particularly important to meet societal expectations, especially in the absence of fully developed legal frameworks and the capacity to enforce them.[23]

The discussion of how the responsibilities of companies should be defined is as old as the idea of free enterprise, evolving over time. The emergence of an increasingly diverse civil society illustrated by a growing number of interest groups in developed and developing countries confronts firms with growing societal expectations. Increasingly, companies are held responsible not only to shareholders but also to other stakeholders, including creditors, employees, consumers—and more generally to those directly or indirectly affected by their business activities (*WIR99*, chapter XII). For TNCs, the underlying intellectual foundation for good corporate citizenship is complicated by the fact that they operate in multiple societies around the world and thus have to respond to different—sometimes conflicting—expectations.

The global goals of TNCs do not always coincide with the social and developmental goals of the individual countries they operate in. In fact, the responsibility of foreign affiliates is not only to their host countries, but also to their parent firms. Yet governments welcome TNCs with the expectation that they contribute to national economic and social objectives, while benefiting from their global strategies and capabilities. TNCs, on their part, have a self-interest in maintaining a mutually supportive relationship with their host countries—to avoid revocation of their enhanced rights and freedoms. They also have a self-interest

in keeping a good reputation and the value of their brands, to prevent competitors from gaining advantages from irresponsible behaviour.

The range of issues considered under the umbrella of good corporate citizenship is broad. It includes developmental responsibilities, socio-political responsibilities, environmental protection, employment and labour relations, ensuring competition and refraining from restrictive business practices, consumer protection, corporate governance, corruption, disclosure and reporting requirements and respect for human rights (UNCTAD 2001b, pp. 4–12; OECD 2001a). But the discussion focuses on environment, human rights and labour rights, at least in developed countries.[24] Their dominance may be a function of the societal preferences of these countries, the emergence of influential civil society interest groups that challenge companies to engage in a dialogue on their policies and performances and the fact that globally agreed standards on these issues exist. A number of companies accept this challenge as these groups are often able to influence the decisions of consumers, business partners, financiers and employees. Even if companies do not feel responsible for certain issues, they might need to engage in a dialogue with stakeholders as to how they handle certain issues, being aware that refusing to do so might have economic consequences for their core businesses.[25]

There is, however, little debate about issues pertaining directly to the economic development interests of developing countries.[26] This is curious for at least two reasons. One, the first and foremost impact of companies is economic—after all, they are business entities. Two, this impact has increased in recent years with the expansion of FDI, particularly for developing countries (*WIR99*). The matter is complicated, however, by the fact that there is no single model for successful development. Nor is there a single internationally agreed instrument from which one could derive specific development obligations, as in human rights. But there are societal expectations about the potential developmental contributions of TNCs, not often fully captured by either competitive market disciplines or (insufficient) government regulation. The resulting governance void poses a challenge for good corporate citizenship (*WIR99*, chapter XII).

The starting point is that TNCs (like other firms) need to respect in good faith the laws of their host countries. They should not be tempted to take advantage of weak legal and administrative systems—say, by engaging in anticompetitive practices (especially restrictive business practices) or corrupt practices.[27] On the contrary, they might be expected to go beyond the local law to meet important needs of host developing countries where legal norms relating to good corporate citizenship may be absent or underdeveloped.

Beyond that, TNCs can make a difference in advancing development goals by making an effort in addition to what they already do, while still serving their own corporate objectives:

- *Contributing to the public revenues of host countries.* Domestic public revenues are one of the principal sources of financing development, especially when it comes to infrastructure and basic services. Tax minimization can have serious repercussions for the development needs of host developing countries. TNCs are thus expected to abide by the spirit of a country's tax law and to meet their tax obligations in good faith—and not purposely shift revenues through abusive transfer pricing to deny the governments of taxes on income originating in their territories.[28] To that end, they are expected to cooperate with the tax authorities of relevant countries and provide appropriate accounting data and tax reconciliation records for tax inspections when required.
- *Creating and upgrading linkages with domestic firms.* Forging linkages between foreign affiliates and local firms—for example, through supplier and other sub-contractual relations—enhances the competitiveness of the domestic enterprise sector, especially where this is consistent with a dynamic comparative advantage. This requires a strong and long-term commitment by foreign affiliates to integrate into the local economy, source locally and increase over time the technological sophistication of their production in developing countries. An often-cited example of a proactive, long-term collaboration between public authorities, local business and TNCs has been the electronic industry cluster in Penang, Malaysia (*WIR01*). In this case, foreign affiliates also made a considerable contribution to Malaysia's exports.
- *Creating employment opportunities and raising local skills level.* In addition to employing and training people directly, TNCs that create linkages with local companies can have a multiplier effect in creating jobs and raising skill levels. Corporate commitments in these respects can generate important positive spillovers for the host economy and thus enhance its development prospects. Parent companies are also expected to cooperate to reduce negative effects that would result, for example, from decisions to close down large existing operations

(*WIR99*, chapter IX). This is also recognized in the OECD Guidelines.[29]

- *Transferring technology*. TNCs can help bring important developmental benefits to host countries by cooperating with local suppliers, private institutions and host governments in the transfer and dissemination of technologies and management skills. They can contribute to upgrading local technological capabilities through various modalities that do not put at risk their technological edge vis-à-vis competitors (*WIR99*, chapter VII).

There are, of course, other ways for TNCs to make a positive contribution to development. For example, they can seek to influence home country governments to open their markets more for imports from developing countries. They can help create a business-enabling environment by actively participating in public-private fora on improving investment conditions in a given country. And they can also serve on advisory panels to national governments and regional bodies.[30]

2. Its international dimension

In many respects, good corporate citizenship is linked to liberalization and globalization (Picciotto 2002). The more that companies expand their operations beyond national boundaries, the more the debate about good corporate citizenship shifts from the national level to the international. The growth of civil society groups around the globe, with enhanced means of sharing information on corporate activities, facilitates this process.

Yet the issue is not new. The ILO adopted its Tripartite Declaration of Principles Concerning Multinational Enterprises and Social Policy in 1977. The purpose of the declaration (article 2) is "to encourage the positive contribution which multinational enterprises can make to economic and social progress and to minimize and resolve the difficulties to which their various operations may give rise [...]". But the OECD Guidelines for Multinational Corporations, adopted in 1976, are probably the most comprehensive instrument for corporate citizenship issues of interest to developed and developing countries alike.[31] The Guidelines have been revised over the years (the latest revision dates from 2000) and adapted to reflect changing priorities (box VI.4).

Developmental standards—stressing duties of enterprises to contribute to economic and social developmental objectives, encouraging local capacity building or encouraging human capital formation, among others—can also be found in the International Chamber of Commerce Guidelines for International Investment of 1972, as well as the World Development Movement's Core Standards of 1999. But responsibilities on economic matters, which were prominent in the past, are receiving less attention in recent international instruments, reflecting the general tendency to leave economic matters to the discipline of market forces (*WIR99;* UNCTAD 2001b, p. 11).

International standards of good corporate citizenship are for the most part embodied in voluntary instruments or codes of various types, including those prepared by NGOs and individual companies. The scope, content and formality of these instruments vary considerably, especially the arrangements for monitoring compliance.[32] And there are few legally binding provisions, mainly because treaties normally entail binding obligations on States not firms. Even though they can also be drawn up to create obligations for individuals, the procedure for creating binding law for individuals or firms at the international level is cumbersome and uncertain (Picciotto 2002, p.16). The growing number of international conventions and declarations dealing with labour, human rights, environmental, ethical and other social issues—as well as regional efforts to harmonize relevant national laws—shows that companies are operating under clearer national and international frameworks on key good corporate citizenship issues. They are thus bound (directly or indirectly) by relevant minimum standards. This aspect is stressed in the 1999 initiative by the Secretary-General of the United Nations for "A Compact for the New Century". The Global Compact calls on world business to embrace and enact—both in their individual corporate practices and in support of their appropriate public policies—nine universally agreed values and principles derived from United Nations instruments (Kell and Ruggie 1999).

The question is whether and how IIAs can address the issue of good corporate citizenship of TNCs in a way that combines best the interests of host developing countries and TNCs. Several approaches and instruments, direct and indirect, can be considered:

- *To enshrine good corporate citizenship principles in non-binding instruments*. The OECD Guidelines for Multinational Enterprises are an example of an inter-governmental instrument containing voluntary recommendations for TNCs. Similarly, the Asia Pacific Economic Cooperation (APEC) Non-Binding Principles contain specific provisions for investor behaviour. This "soft-law" approach offers advantages to countries that recognize the need for international standards in this area, but

are not ready to negotiate binding rules. It also offers advantages to TNCs by allowing them flexibility in adapting to different conditions and practices in developing countries, rather than being locked into one standard to be applied everywhere. Voluntary standards can be monitored through formal and informal means.

- *To link voluntary instruments to legally binding ones*. For example, countries adhering to the OECD Guidelines for Multinational Enterprises could sign a binding commitment to promote them among TNCs operating in or from their territories. The same approach was, at one point, proposed for the draft OECD Multilateral Agreement on Investment. The Joint Declaration in the Chile–EU Agreement reminds, in hortatory language, the TNCs of these countries "of their recommendation to observe the OECD Guidelines for Multinational Enterprises, wherever they operate".
- *To prescribe that treaty benefits are granted only to investments made in accordance with the national laws and regulations of the host country*. Alternatively, a treaty can prescribe that the admission, establishment and operation of foreign investors is subject to the national laws and regulations of the host country. The model BIT used by the People's Republic of China, for example, in article 1.1, states that "'investment' means every kind of asset invested by investors of one Contracting Party in accordance with the laws and regulations of the other Contracting Party in the territory of the Latter…" (UNCTAD 1996b). In this approach—reflected in the majority of BITs—good corporate citizenship issues are not explicitly mentioned in an IIA. Nor are voluntary corporate actions—an integral part of good corporate citizenship—affected. But to the extent that the laws of the countries parties to an IIA reflect certain good corporate citizenship standards, these become part of the obligations investors have to observe if they want to benefit from treaty coverage (which may even become relevant in dispute settlement procedures). As mentioned earlier, firms may even be expected to exceed the requirements of local laws. And the inclusion of this type of provision in an IIA—however indeterminate and indirect—offers guarantees to foreign investors that such standards would need to be applied in a manner consistent with the protection standards (such as non-discrimination, fair and equitable treatment) granted in the same agreement.
- *To include a reference to the importance the parties attach to observing good corporate citizenship objectives in the preamble of IIAs*. Preambular language is not part of the operational provisions of an agreement. Instead, it reflects the context, objectives and philosophy behind it. It can therefore influence the interpretation of provisions in a manner consistent with development concerns.
- *To create mandatory procedural obligations for governments* to encourage firms to comply with substantive good corporate citizenship standards and to provide a mechanism for follow-up. This is the case with the OECD Guidelines for Multinational Enterprises.
- *To incorporate legally binding provisions into IIAs* to deal with good corporate citizenship issues. Transfer-of-technology provisions in various international agreements are examples (chapter IV.G).

Both binding and voluntary approaches have their advantages and shortcomings. The effectiveness of both approaches depends on appropriate monitoring mechanisms (which public pressure may increasingly demand). In the future, it is likely that both will be pursued in parallel or in combination with each other, on the national and international levels. IIAs cannot be expected to set out comprehensive rules for business activities. Nor can they substitute for voluntary corporate citizenship actions, NGO instruments or specific international agreements. But IIAs are the instruments that focus on the investment process, and that process involves TNCs. So IIAs could in principle address all relevant actors.

How that is done, and how far negotiations can go, is a function of the interests of the actors and the negotiating process. But in a time when the societal implications of corporate actions are receiving more attention and scrutiny, good corporate citizenship—especially when it combines the interests of host countries and firms—deserves a careful examination in future IIAs.

Box VI.4. The OECD Guidelines for Multinational Enterprises

"II. General Policies

Enterprises should take fully into account established policies in countries in which they operate and consider the views of other stakeholders. In this regard, enterprises should:

- Contribute to economic, social and environmental progress with a view to achieving sustainable development.
- Respect the human rights of those affected by their activities consistent with the host government's international obligations and commitments.
- Encourage local capacity building through close co-operation with the local community, including business interests, as well as developing the enterprise's activities in domestic and foreign markets, consistent with the need for sound commercial practice.
- Encourage human capital formation, in particular by creating opportunities and facilitating training opportunities for employees.
- Refrain from seeking or accepting exemptions not contemplated in the statutory or regulatory framework related to environmental health, safety, labour, taxation, financial incentives or other issues.
- Support and uphold good corporate governance principles and develop and apply good corporate governance practices.
- Develop and apply effective self-regulatory practices and management systems that foster a relationship of confidence and mutual trust between enterprises and the societies in which they operate.
- Promote employee awareness of, and compliance with, company policies, including through dissemination of these policies, including through training programmes.
- Refrain from discriminatory or disciplinary action against employees who make *bona fide* reports to management or, as appropriate, to the competent authorities, on practices that contravene the law, the *Guidelines*, or the enterprise's policies.
- Encourage, where practicable, business partners, including suppliers and subcontractors, to apply principles of corporate conduct compatible with the *Guidelines*.

Abstain from any improper involvement in local political activities."

Other chapters of the Guidelines deal with disclosure, employment and industrial relations, environment, combating bribery, consumer interests, science and technology and competition and taxation. The science and technology chapter reads as follows:

"...endeavour to ensure that their activities are compatible with the science and technology (S&T) policies and plans of the countries in which they operate and as appropriate contribute to the development of local and national innovative capacity."

Source: UNCTAD 2001c, p. 34 and p. 40; OECD 2002.

Notes

1 The stock of outward FDI from developing countries increased rapidly since the 1990s and stood at $849 billion in 2002. (It was, however, only about a third of the inward stock of about $2.3 trillion.) The 10 largest developing economy sources—with Hong Kong (China), Singapore, Taiwan Province of China and the Republic of Korea in the top four positions—accounted for 85% of the outward stock. Only 13 of 116 developing economies for which data are available reported outward stocks of more than $10 billion in 2002.

2 Market access regulations in home countries can affect—negatively or positively—the scope for export-oriented FDI in developing countries. Measures that inhibit domestic market access for exports from overseas facilities (such as anti-dumping regulations, countervailing measures and technical barriers to trade), or conversely grant favoured treatment to imports from selected countries, affect the comparative profitability of FDI in various developing country locations.

3 Issues related to foreign affiliates themselves will be dealt with in the next section on good corporate citizenship.

4 Such cases may be of particular relevance where evidence exists of a systematic abuse of fundamental labour rights or the abuse of child labour contrary to international law and international conventions.

5 For example, the United States Sarbanes-Oxley Act (2001) has been passed to deal with such practices on an international level in the wake of the Enron scandal.

6 To date only one case, decided in the United States in 1984, has found the parent to be liable for the wrongs of its foreign affiliates, both as a direct wrongdoer and as a result of the parent subsidiary relationship between itself and its operating subsidiaries: Amoco Cadiz (1984). In recent cases in the United Kingdom claimants have been granted the right to bring proceedings against a United Kingdom-based parent company where the host country's courts and legal system can be shown not to be capable of ensuring that substantive justice is done to the claim (United Kingdom, House of Lords, 2000).

7 Assistance is provided, for example, by UNCTAD, the World Bank (MIGA and FIAS) and the World Association of Investment Promotion Agencies. The "Proinvest" programme of the EU is dedicated to making IPAs in the ACP countries more effective and efficient in attracting FDI and making FDI achieve national development objectives. One of its tasks is to link outward investment promotion agencies in Europe with IPAs in the ACP countries.

8 In Europe alone, there are at least 12 development finance institutions (see, for example, http://www.edfi.be).

9 The regional development banks include the African Development Bank, Asian Development Bank, Caribbean Development Bank and the Inter-American Development Bank.

10 MIGA was established in 1988 and works as a complement to national and regional FDI guarantee programmes as well as private insurers to issue guarantees, including co-insurance and re-insurance. Since 1990 MIGA has provided $11 billion in coverage and has facilitated $45.8 billion in FDI to developing countries. Other relevant World Bank institutions include the International Finance Corporation and ICSID.

11 A compilation by UNCTAD found only five exceptions in 1999—hence UNCTAD's project (with the ICC) to produce such guides; see UNCTAD-ICC 2000a– Ethiopia, 2001a – Mali, 2000b – Bangladesh, 2001c – Uganda, 2001b – Mozambique, 2003–Nepal, and forthcoming – Cambodia.

12 For example, the Norwegian Norfund has committed 265 million kroners to 17 projects across 15 countries, many of which are in Africa, Asia and Latin America (Torp and Rekve, 2003). The Overseas Private investment Corporation has reportedly helped host developing countries develop more than 600,000 jobs over its 30-year history and as of September 2001 was managing a portfolio of 133 active finance projects and 254 active insurance contracts. And MIGA has issued more than 500 guarantees for projects in 78 developing countries since 1988. According to the MIGA website, total coverage issued exceeded $9 billion in June 2001, bringing the estimated amount of FDI facilitated since inception to more than $41 billion. The agency mobilized an additional $153 million in investment coverage in fiscal 2001 through its Cooperative Underwriting Program, encouraging private sector insurers into transactions they would not have otherwise undertaken, and helping the agency serve more clients.

13 The corresponding financing institutions in Denmark have 12% and of their investments in LDCs and those in Sweden 7% (Torp and Rekve 2003).

14 For examples of such general policy exhortations, see UNCTAD 2001a, pp. 13–18.

15 For a compilation of provisions in international arrangements for the transfer for technology, see UNCTAD, 2001h.

16 See further the MIGA website at www.miga.org.

17 Although a number of developing countries too have emerged as home countries, the principal purpose of HCMs in the context of IIAs is to enhance investment flows from developed to developing countries.

18 See "Investors' and home governments' obligations", Communication from China, Cuba, India, Kenya, Pakistan and Zimbabwe (WTO doc. WT/WFTI/W/152).

19 See for example Chapter 1, Article 8 of the Agreement between Japan and Singapore for a New Age Partnership (box III.2).

20 This raises an issue that deserves consideration, namely that private entities (primarily from developed countries) are implicitly called upon to take on functions (such as upholding certain norms) that are normally reserved for governments.

21 For a fuller discussion on the nature, scope and content of the corporate social responsibilities of TNCs, see *WIR99*, chapter XII, and UNCTAD 2001b.

22 The Monterrey Consensus (paragraph 23), adopted in 2002 by the Financing for Development Conference, uses "good corporate citizenship". This is not to say that issues relating, for example, to the environment and social matters (such as industrial relations) are not also an integral part of development. Here, the focus is on economic issues themselves. In any event, it should be noted that the concept does not cover corporate philantrophy as this has in a strict sense little to do with a company's core business.

23 Good corporate citizenship should be distinguished from "corporate governance", which is limited to issues of how a corporation should be structured or organized to achieve effective control over its activities in the interests of shareholders and other direct stakeholders such as employees and creditors. But corporate governance is beginning to interact with "corporate social responsibility" to the extent that the interests of indirect stakeholders—that is, groups affected by the activities of a company, but without direct economic ties to it—may seek a formal role in the organizational structure of a company.

24 In these areas the elaboration of good corporate citizenship standards has received increased attention in recent years, both in general instruments (such as the OECD Guidelines) as well as specialized ones developed by international and regional organizations (such as the United Nations and its specialized agencies, the OECD, international federations of business, trade unions, professional associations and individual companies). Examples of increasingly detailed and sector-specific standards are numerous (UNCTAD 2001b, g; Karl 1998). The development of corporate standards in these areas is facilitated by broadly accepted international conventions and supported by civil society groups. A current effort in this area is being undertaken by the Working Group on the Working Methods and Activities of Transnational Corporations of the Sub-Commission on the Promotion and Protection of Human Rights, see its draft "Norms on the Responsibilities of Transnational Corporations and Other Business Enterprises with Regard to Human Rights" (E/CN.4/Sub.2/2002/13, annex).
Several new issues are emerging in the international good corporate citizenship sphere. One is corporate governance for which standards are being clarified and strengthened in, for example, the OECD Principles of Corporate Governance (1999). The Principles aim at reinforcing the rights of minority shareholders, while giving increasing recognition to the rights of other stakeholders and stressing duties of proper reporting and consultation.

25 The way parts of the good corporate citizenship agenda is set may constitute a problem for policymakers in developing countries. While some standards (such as ILO labour standards) are globally

set, there is also a tendency towards the establishment of standards involving only companies or industry associations on the one hand, and NGOs on the other. Governments are sometimes bypassed when these standards are set. At the same time, however, standards negotiated without government participation might have concrete effects on where companies are locating their investments, with which suppliers they choose to do business and other decisions with a concrete bearing on a country's trade and investment performance and, ultimately, their economic development. An example of this is the United States Fair Labor Association (FLA). This body was formed by 11 leading apparel companies (including Nike, Patagonia and Liz Clairborne) as well as NGOs such as the Lawyers Committee for Human Rights and the National Consumers League. FLA members have developed a code that prohibits forced as well as child labour and supports freedom of association, minimum wages, limits on working hours and a plethora of similar rights (Garten 2002). While such codes and standards are often meant to raise and harmonize production standards in the industry worldwide, they can have side effects, too. The negotiated standards might help to divert trade and investment flows from countries that do not yet meet these standards without, however, their being involved in setting them. While some countries may benefit from such business-NGO partnership initiatives in terms of additional FDI, other countries might loose out. Thus, the emergence of these non-governmental standard setting initiatives poses a challenge to policymakers particularly in developing countries.

26 A number of companies, in their own materials, however, make reference to such matters as tax returns, local development and local business partners.

27 This is actually one of the most common commitments that TNCs make publicly; see OECD 2001b. The situation is, however, more difficult when national laws do not reflect the spirit of internationally accepted standards, such as in the case of the apartheid regime in South Africa. Good corporate citizenship would, in these cases, require different behaviour than just "playing by the rules".

28 The OECD and ISAR, for example, have guidelines concerning transfer pricing (OECD 2001b; UNCTAD/ ISAR 1998). It should be noted that tax competition between countries invites TNCs to shift tax burdens across borders.

29 "Enterprises should:... In considering changes in their operations which would have major effects upon the livelihood of their employees, in particular in the case of the closure of an entity involving collective lay-offs or dismissals, provide reasonable notice of such changes to representatives of their employees, and, where appropriate, to the relevant governmental authorities, and co-operate with the employee representatives and appropriate governmental authorities so as to mitigate to the maximum extent practicable adverse effects." (UNCTAD 2001c, Section IV (6)).

30 Such advisory councils exist in Malaysia, Singapore and South Africa, as well as for ASEAN. UNCTAD and the International Chamber of Commerce established an Investment Advisory Council for LDCs.

31 Other instruments were negotiated during the 1970s and early 1980s but not completed. These include the draft United Nations Code of Conduct on Transnational Corporations and the draft Code of Conduct on the Transfer of Technology. They tended to reflect the concerns of developing countries at that time.

32 For a comprehensive review of voluntary codes of conduct, their current status and prospects of future expansion and effectiveness, see Sethi 2003.

PART TWO CONCLUSIONS

THE CHALLENGE OF THE DEVELOPMENT DIMENSION

Most host countries conclude international investment agreements (agreements that address, at least in part, investment issues) mainly to help attract FDI to further their development. Most home countries conclude them mainly to make the regulatory framework for FDI in host countries more transparent, stable, predictable and secure—and to reduce obstacles to future FDI flows. Because the regulatory framework for FDI—at whatever level—is at best enabling whether FDI actually flows depends mainly on the economic determinants in host countries.

The number of IIAs has greatly increased in the past decade, particularly at the bilateral and regional levels, and more are under negotiation. They reflect and complement national policies which have become more welcoming to FDI. They also set parameters for national policies, putting investment at the interface of national and international policies in the globalizing world economy.

Issues relating to IIAs are coming to the fore in international economic diplomacy regardless of what will or will not happen at the multilateral level, simply because of what is happening now at both the bilateral and regional levels. But if negotiations should take place at the multilateral level, these issues will acquire even greater importance. Whether governments negotiate IIAs—and, if so, at what level and for what purpose—is their sovereign decision. This *WIR* has sought to throw light on issues that need to be considered when negotiating IIAs, seeking to clarify them from a development perspective.

What are the issues?

The most important challenge for developing countries in future IIAs is to strike a balance between the potential for IIAs to increase FDI flows and the ability of countries to pursue development-oriented FDI policies—as an expression of their right to regulate in the public interest. This requires maintaining sufficient policy space to give governments the flexibility to use such policies within the framework of the obligations established by the IIAs they are parties to. The tension is obvious. Too much policy space reduces the value of international obligations. Too stringent obligations overly constrain the national policy space. Finding a development-oriented balance is the challenge.

When negotiating IIAs, this challenge is addressed in respect to the objectives of IIAs, their structure, content and implementation. Their content is central as the quest for a development friendly balance plays itself out in the resolution of issues that are particularly important for the ability of countries to pursue development-oriented national FDI policies and that are particularly sensitive in international investment negotiations, because countries have diverging views about them in light of their own predominating objectives.

From a development perspective, these issues are: the definition of "investment", because it determines the scope and reach of the substantive provisions of an agreement; the scope of national treatment (especially as it relates to the right of establishment), because it determines how much and in which ways preference can be given to domestic enterprises; the circumstances under which government policies should be regarded as regulatory takings, because this involves testing the boundary line between the legitimate right to regulate and the rights of private property owners; the scope of dispute settlement, because this raises the question of the involvement of non-State actors and the extent to which the settlement of investment disputes is self-contained and the use of performance requirements, incentives, transfer-of-technology policies and competition policy, because they can advance development objectives. (Other important matters also arise in negotiations of IIAs, especially MFN, fair and equitable treatment and transparency. But these appear to be less controversial in investment negotiations.)

For each of these issues, more development friendly and less development friendly solutions exist. From the perspective of many developing countries, the preferable approach is therefore a

broad GATS-type positive list approach that allows each country to determine for itself for which of these issues to commit itself to in IIAs, under what conditions, and at what pace, commensurate with its individual needs and circumstances.

In pursuit of an overall balance, furthermore, future IIAs need to pay more attention to commitments by home countries. In fact, all developed countries (the main home countries), out of their own self-interest, already have various measures to encourage FDI flows to developing countries in place. And a number of bilateral and regional agreements contain commitments. Developing countries would benefit from making home country measures more transparent, stable and predictable in future IIAs.

TNCs too can contribute more to advancing the development impact of their investment in developing countries, as part of good corporate citizenship responsibilities, whether through voluntary action or more legally-based processes. Areas particularly important from a development perspective are contributing fully to public revenues of host countries; creating and upgrading linkages with local enterprises; creating employment opportunities; raising local skill levels; and transferring technology.

These issues are all complex. Because the potential implications of some provisions in IIAs are not fully known, it is not easy for individual countries to make the right choices. The complexities and sensitivities are illustrated by the experience of NAFTA for the regional level; that of the MAI negotiations for the interregional level and that of the GATS and the TRIMs Agreement for the multilateral level. Given the evolving nature of IIAs, other complexities tend to arise in applying and interpreting agreements. Indeed, disputes may arise from these processes, and their outcome is often hard to predict.

That is why governments need to ensure that such difficulties are kept to a minimum. How? By including appropriate safeguards at the outset to clarify the range of special and differential rights and qualifications of obligations that developing country parties might enjoy. Moreover, the administrative burden arising from new commitments at the international level is likely to weigh disproportionately on developing countries, especially the least developed, because they often lack the human and financial resources needed to implement agreements. This underlines the importance of capacity-building technical cooperation to help developing countries assess better various policy options before entering new agreements and in implementing the commitments made.

The overriding challenge for countries is to find a development-oriented balance when negotiating the objectives, content, structure and implementation of future IIAs at whatever level and in whatever context. The development dimension has to be an integral part of international investment agreements—in support of national policies to attract more FDI and to benefit more from it.