

Towards a Repository of Policy Options for IIA Reform

Research Project

TTIP and TPP Agreements: Emerging Investment Rules and their Implications on Developing Countries¹

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This paper was presented at a conference on Mega Trading Blocs organized by the Commonwealth Secretariat and UNCTAD. The objective of the paper was to **highlight the investment rules emerging under the new mega regional agreements such as the Transatlantic Trade and Investment Partnership (TTIP) as well as the Trans Pacific Partnership (TPP) and the implications of such rules on non-signatory developing countries**. From an investment perspective, the relevance of these arrangements stems from firstly, the **volume of FDI associated with these arrangements**. Secondly, member countries of TTIP and TPP, in particular the EU countries, US and Japan still account for **more than half of the global FDI outflows**. UNCTAD data indicates that over half of the top twenty investing countries of the world are either member of TTIP and/or TPP. Given the economically dominant positions of these countries, any trade and investment agreement between these countries will inevitably **impact facets of global economic governance**. Thirdly, unlike bilateral investment treaties (“BIT (s)”) that are more focused on investment protection, investment chapters in free trade agreements (“FTA”s) also include investment liberalization. TTIP and TPP agreements are FTAs having a comprehensive scope, and will require harmonization and a common approach in several legal and policy areas impacting investment. Fourthly, **developing countries** not negotiating either of these mega agreements (“non-member developing countries”) **have limited share in global FDI**. UNCTAD data indicates that over half of the top twenty recipient countries of FDI are either TTIP and/or TPP members. The other countries on the list include Brazil, China and India, which amongst other factors have the benefit of a large market. The fact that there is limited presence of non-signatory developing countries on this list is critical. **Absent significantly distinguishing features, these countries are likely to face strong competition in attracting FDI, in a post TTIP and TPP world**. Though there is mixed evidence on the link between investment treaties and investment flows, it is known that companies particularly those that are efficiency seeking and closely linked to global value chains, are sensitive to governance, legal and regulatory frameworks of potential host countries. Thus, **where all other factors that determine attractiveness are similar in two countries, the quality of governance, legal and regulatory frameworks can distinguish one from the other**.

The paper reviewed various drafts that have either been released by governments or by other sources. These drafts, along with publicly stated negotiating objectives and recent agreements signed by the member countries (“reviewed drafts”) provide some guidance on the likely content of these mega-agreementsⁱⁱ. Amongst the key provisions that may likely be included are - a wide asset based definition of investment that includes the categories of tangible and intangible property; national treatment and most favored nation treatment (exceptions for procurement, subsidies); restrictions on select types of performance requirements (exceptions for compulsory license, government procurement, health and environment); protection against direct and indirect expropriation. Some reviewed drafts also tried to provide interpretative guidance on provisions such as fair and equitable treatment. The TPP leaked text stipulates that treatment of aliens should be as per customary international law, while EU’s TTIP leaked text stipulates that government measures should not lead to –“...a. Denial of justice in criminal, civil or administrative proceedings; or b. Disregard of the fundamental principles of due process; or d. Targeted discrimination on manifestly wrongful grounds, such as gender, race or religious belief; ...f. A breach of legitimate expectations of investors arising from a government’s specific representations or investment-inducing measures; or g. A disregard of the

¹ The opinions expressed in this paper are those of the author and do not necessarily reflect the views of the UNCTAD Secretariat or its Member States.

principle of effective transparency in any applicable administrative or judicial procedures.” There continues to remain much uncertainty on whether ISDS will find its way into the mega agreements. Notably, EU’s TTIP leaked text does not include a specific provision on ISDS, but provides a set of guidelines. The guidelines prescribe that ISDS should not apply to market access commitments and the process should encourage amicable settlement. They also state that the agreement should include provisions - dealing with *manifestly unjustified claims*, allowing appeals on questions of law, preventing excess compensation and multiple claims against State. Some of the reviewed drafts also included specific provisions on environment and corporate social responsibility (“CSR”).

The challenge with some of the rules that are likely to be introduced is that they are fairly difficult to implement for developing countries, given their institutional frameworks and resources. Mere adoption of new rules without implementation could in fact make developing countries more vulnerable to domestic as well as international disputes. **An example of a valuable principle which requires high level of institutional capacity and coordination is transparency. Similarly, the restriction on performance requirements can also be burdensome** - developing countries frequently use these tools to “quickly” achieve specific policy objectives like increasing local employment or use of local raw materials, technology transfer. **Aligning domestic laws and policies with the new global rules on investment will require re-consideration of these performance requirements. On a positive side, this could also be viewed as an opportunity for non-member developing countries to re-assess and upgrade their investment rules to increase investor confidence, minimize potential for discrimination and institutional inefficiencies, in a manner most suitable for their stage of development and capacity.** The growing importance of global value chains involving complex and interconnected cross border flow (of goods, capital, people, knowledge) and increased linkage between trade and investment, makes innovative and deeper policy/law making essential. **The TTIP and TPP arrangements may just provide the thrust needed to drive developing countries to transform their policy/legal environment to better address these emerging economic realities.** The paper also reviewed select investment treaties signed by Sub-Saharan African and Caribbean countries. It found that most proposed rules are not new and treaties, for example, between Mozambique, Netherlands and Luxemburg already include a transparency provision. Some investment treaties even seem to go beyond what may be stipulated under the TTIP and TPP agreements. For example, the UK-Ghana investment treaty provides that compensation for expropriation should be paid within six months, after which interest will be charged until date of payment. Some developing countries with slower processing times, may find such timelines quite stringent. In this context, the new rules envisaged under TTIP and TPP will not add to the existing obligations of the non-member developing countries.

It is clear that ISDS in its current form needs very significant reform. Irrespective, ultimately it is in the interest of developing countries to encourage investor confidence. In the absence of an efficient, non-discriminatory domestic legal system, investors can practically only look to ISDS as an effective, depoliticized means of dispute resolution. **Other alternatives such as political risk insurance add costs to doing business, and stabilization agreements can constrain States and also need effective enforcement.** The mere threat of ISDS has in recent times also pushed countries to pursue dispute prevention policies, a positive agenda that can greatly benefit countries. In this context, the choice for developing countries is limited - **either adopt ISDS or greatly improve their domestic legal environment to make domestic dispute settlement a viable alternative for investors.** An apparent geopolitical implication of the TTIP and TPP arrangements is the stimulus they provide towards investment agreements between non-member countries (e.g. Regional Comprehensive Economic Partnership). Through these mega agreements, select countries of the world are aiming at writing the global rules on investment. This raises questions around the possibility of a more equitable outcome, had investment been a subject of multilateral deliberations.

ⁱ The paper is a Commonwealth Secretariat working paper. The views expressed in this note are solely the author’s and do not represent views of the World Bank or the Commonwealth Secretariat.

ⁱⁱ Agreements reviewed are US Model Investment Treaty, 2012, TPP’s leaked investment text, EU’s leaked TTIP investment chapter, ASEAN Comprehensive Investment Agreement, 2009, Australia-Chile Free Trade Agreement, 2008, Trilateral Agreement between China, Japan and South Korea, 2012, EU-Canada FTA.