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Direct Investment and the Future Agenda of the World Trade Organization

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A key question facing the member nations of the World Trade Organization (WTO) is whether to negotiate and implement a new Agreement on Direct Investment (ADI) in the coming years. There is widespread feeling that, in light of the growing importance of foreign direct investment (FDI) and the linkages between the operations of multinational firms and international trade, such an agreement would be a desirable addition to international commercial law.

Such an agreement would help foster free flows of direct investment across national boundaries. This direct investment is important not so much for its own sake but because it is the primary (though not the only) means by which firms extend their activities internationally.[1] Seen in this light, what really matters is not the magnitude of the annual flow of direct investment,[2] but rather the business activity that this investment generates. At the end of 1995, the total FDI stock worldwide (based on home-nation reporting) was over $2.73 trillion, invested in more than 200,000 affiliates of multinational firms (UNCTAD 1996). These affiliates generated about $6.02 trillion in net sales, a figure somewhat greater than the total value of all exports of goods and nonfactor services in that year (about $4.8

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1. Otherwise put, the main importance of direct investment lies apart from the fact that it is a ''long-term capital flow'' figuring in a country's balance of payments.

2. This annual flow amounted to $227.5 billion in 1994, the most recent year for which data are available and the highest flow ever recorded in a single year. Previously, the highest flow in a single year was $211.4 billion in 1990.

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trillion). During the past 10 years, the rate of growth of FDI and related activity has consistently grown faster than world trade,[3] and world trade has grown faster than world output.

The benefits of FDI and related activities are almost without dispute. Among these are increased competition within national markets, transfer of technology, and spillovers associated with this transfer.[4] This last item is of special note. The existence of spillovers implies that FDI is associated with increases in domestic firms' productivity. These domestic firms can be suppliers, distributors, or even competitors of the multinational firms.

Such benefits are of particular relevance to developing nations. In particular, developing countries having strong international investment and trade ties with OECD nations tend to have higher productivities and higher rates of growth than do countries with weaker ties (see, e.g., Borzenstein, Gregorio, and Lee 1994; Coe, Helpman, and Hoffmaister 1994). But because trade ties between developing and OECD nations tend to be strongly correlated with investment ties, it is difficult to determine causality from international comparisons: the higher productivities and growth rates could be the result of technology transfer by multinational enterprises (MNEs), of importation of capital goods embodying the newest and best technologies, or of some combination of the two. Exactly what is the mix of the two is not clear, but ''micro'' studies confirm that the effects of technology transfer are significant, including the effects of spillovers associated with this transfer. Some of the strongest evidence indicating that direct investment does indeed generate significant spillovers comes from China, where town and village enterprises (TVEs) located in areas with a heavy foreign investor presence tend to outperform TVEs in areas without such a presence (Wei 1996).

Recognition of these benefits has led a worldwide shift in official attitudes toward direct investment and multinational enterprises. Twenty years ago, the developing nations almost unanimously condemned multinational firms as agents of Western imperialism. Today, however, in light of the very favorable economic performance of many developing nations that have maintained open policies toward inward direct investment, many nations that were only recently hostile to this investment now welcome it with open arms. The result has been a shift in these countries' policies from restrictive to relatively open regimes.[5]

One unfortunate consequence of the move to open policy regimes is that there is an increasing potential for governments' policies to conflict with one another in ways that are harmful to overall economic gains.

3. That is, this is true regardless of whether FDI is measured by flows or stocks or by activity of overseas affiliates of multinational firms.

4. A review of the evidence is provided in Graham (1996, appendix 1).

5. Policy liberalization in the developing nations is discussed in some depth in UNCTAD (1996).

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One possibility is that governments will offer subsidies to attract direct investors and that these subsidies may distort the benefits of the investment activity. Governments also might use other measures (e.g., performance requirements) to tilt the benefits of direct investment to their economies but at the expense of some other economy. Finally, governments might attempt to use multinational firms as vehicles for achieving political ends—for example, via efforts to apply law and policy extraterritorially. The latest example of such an effort is the US Helms-Burton law, which would sanction certain non-US firms for doing business in Cuba. International rules could help to prevent or to attenuate such potential conflicts.

In recognition of the importance of direct investment, its contribution to the welfare of nations, and the need to head off conflicts between governments over direct investment and the activities of multinational firms, the member nations of the Organization for Economic Cooperation and Development (OECD) have already begun to negotiate a ''Multilateral Agreement on Investment'' (MAI). In its current unfinished form, this agreement is flawed on at least two counts: it would be a stand-alone instrument (i.e., not explicitly linked to existing agreements of the WTO), and it would hardly be ''multilateral''; it is doubtful whether many non-OECD nations would join it, although in principle they could join if they wished. Indeed, not even all OECD nations would be required to sign it. (Thus, following accepted usage, this agreement should properly be termed ''plurilateral'' rather than ''multilateral.'')

This second flaw is of particular gravity: most of the potential benefit of a multilateral agreement on direct investment would result from reform by nations whose policies toward investment are not in conformity with the agreement. As is elaborated below, such nations by and large are not currently OECD members.

Somewhat offsetting these two flaws are two main arguments for the OECD instrument. First, the OECD member nations seem to be willing to obligate themselves to ''higher'' standards than would now be accepted by most non-OECD nations (exactly what is meant by ''higher standards'' is discussed in the next section). Second, the MAI, if completed on schedule, could be implemented much sooner than any future ADI within the WTO. There is some circularity in these arguments: by and large, the OECD nations already have in place relatively liberal policies toward FDI, and hence it is relatively easy for these nations to agree on ''high'' standards. But the benefits of achieving these standards within the OECD are limited because the OECD nations already largely meet the standards.

Thus, the main point made in this chapter is that, despite the likelihood of the MAI coming into being, an ADI is still desirable at the earliest possible date. The rationale behind this conclusion is further developed below, as are the ideal substantive provisions of such an agreement. The chapter then explores two options for developing such an agreement: to

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allow the OECD MAI to "migrate" to the WTO (that is, incorporate the MAI, modified as necessary, into the WTO framework at some future date) and to negotiate such an agreement in the WTO "from the ground up." The chapter ends with conclusions and recommendations.

A WTO Agreement on Direct Investment: Why Have One and What Should It Do?

To address the issue of why there should be an agreement on direct investment within the WTO, it is necessary to decompose the issue into two components: why should there be multilateral rules on FDI at all, and why should they be in the WTO?

With respect to the first component, it is often asked why it is worthwhile negotiating multilateral rules at all on FDI, when a large number of nations are already liberalizing their policy regimes. After all, won't the effect of such policy liberalization be the same as if nations had bound themselves to international rules?

There are two reasons such rules are nonetheless desirable at this time, and each is compelling. First, national policy reforms, even in nations in which there is a groundswell in the direction of liberalization, are likely to be more profound and enduring if these reforms are backed by international standards than if they are made in isolation. Thus, for example, the negotiation of the investment provisions (chapter 11, part A) of the North American Free Trade Agreement (NAFTA) actually helped Mexico to implement policy reforms that Mexican reformers were seeking anyway. (Indeed, after signing NAFTA, Mexico announced that it would multilateralize its obligations under chapter 11, part A to investors from all nations.)

Second, international rules (or standards) would serve to lock nations into agreed-upon standards and thus might help to check or prevent any future policy "backsliding." It is more difficult for a nation to adopt "deliberalizing" policies if such backsliding would contravene an international obligation than if no such obligation existed.

An ADI is desirable within the WTO to offset the two flaws of the MAI already noted. First, an ADI could (and should) be fully integrated into the existing framework of international commercial law, as embodied in the various WTO agreements, rather than as a stand-alone agreement because many existing provisions already complement a future ADI. Such provisions are part of agreements such as those on trade-related investment measures (TRIMs), on subsidies and countervailing measures, and on trade in services (GATS).[6]

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6. If the ADI could be concluded as a multilateral agreement—one in which all WTO member nations participated—the investment provisions of the GATS would become redundant and could be jettisoned, leaving an agreement on trade in services only. If the ADI were to be concluded as a plurilateral agreement, its provisions and the investment provisions of the GATS would have to be brought into conformity.

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Desirable integration between the ADI and other agreements of the WTO would also include linking the ADI to the WTO dispute settlement mechanism. For reasons to be specified shortly, new dispute settlement procedures would nonetheless need to be adopted in the context of an ADI. In particular, the linkage would enable trade sanctions to be invoked against a nation found in violation of ADI obligations in accordance with WTO dispute settlement procedures. As with any other dispute, sanctions would be allowed only if the putative violations were not remedied in accordance with recommendations of a WTO panel. In contrast, one likely weakness of the MAI will be that violations of its obligations will not be subject to any form of international sanction. Simply put, an ADI would be more enforceable than an MAI.

Second, the number of nations that would likely subscribe to an ADI almost surely will be greater than the number that will sign on to the MAI. As already noted, one rationale for the current MAI negotiation is the OECD nations' belief that ''higher'' standards can be achieved in the OECD than in the WTO. There is an obvious element of speciousness to this rationale because, after all, the OECD nations could themselves choose to negotiate an agreement within the WTO on a plurilateral basis.[7] If then even a handful of non-OECD nations were willing to commit themselves to the ''high'' standards sought by the OECD group, the outcome would be more favorable than that of the MAI.

What are these ''high standards''? The MAI would obligate all signatories to the following key provisions, all of which should also be required ingredients for an ADI:[8]

- Signatories would accept a reasonably broad definition of what constitutes a direct investment, in order to cover the multitude of ways in which multinational firms establish themselves in host nations—for example, through the creation of subsidiaries, through joint ventures or other strategic alliances, or through service and turnkey operations.[9]

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7. Within the WTO, however, negotiations for the European Union nations would be conducted by the European Commission, whereas in the OECD the negotiators are from each of the individual national governments. It is not clear what difference this would make, although defenders of the OECD have argued that higher substantive standards can somehow be achieved by the OECD negotiators than by an equivalent group in which the European national representatives are replaced by negotiators from Brussels.

8. In what follows, a ''host'' nation is one that is recipient to direct investment while a ''home'' nation is the source of such an investment.

9. These typically are limited-liability corporations, established under host-nation law, in which the parent organization or investor has a controlling interest.

It should be noted that some nations in the OECD negotiations have been seeking a definition of investment that is arguably too broad. One European nation would, for example, have placed under the coverage of the MAI private residences of its nationals in other nations (in other words, the MAI would apply to vacation homes!). Whether the OECD, or

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- Host nations would be obliged to grant unencumbered right of establishment to foreign investors. Usually this right is considered ''good enough'' if it is granted on the same basis as that granted to domestic investors (if this is the case, it is said that ''preestablishment national treatment'' exists for foreign investors). But in practice, no nation grants full preestablishment national treatment to all foreign investors. Thus, in practical terms, unencumbered right of establishment implies a minimum of restrictions or conditions on entry by foreign investors, an absence of governmental screening except perhaps for national security reasons, and no preestablishment ''performance requirements'' imposed by the host government or any subnational governments.

  Much time is being spent in the MAI negotiations on what exceptions will be allowed to this general obligation to ensure right of establishment. Even within the ''high standard'' OECD nations, sector-specific and other exceptions are rife, and one possible benefit of an MAI could be that it reduces the number of these exceptions. However, at this time it is unclear whether the MAI negotiations will significantly liberalize existing restrictions.
- Host nations would be obliged to grant national treatment to foreign-controlled firms and other covered investments. National treatment implies that such firms and investments are granted treatment that is no less favorable than that granted to similar domestically controlled firms and investments. Again, no OECD nation grants full national treatment to all foreign-controlled firms in all industries, and thus, again, the issue before the MAI negotiators is exactly what exceptions will be permitted. There is widespread agreement that some exceptions must be made in the name of national security. Beyond this, little consensus exists as to what exceptions should be allowed.[10]
- Host nations would be obliged to extend most-favored nation (MFN) treatment to investments from nations that participate in the MAI. This

the WTO, should be in the business of attempting to resolve disputes between owners of residences and local town or city governments strikes one as highly questionable. Likewise, it seems questionable whether the MAI should cover passive, rather than active, investments. The opinion of this author is that the agreement should cover direct investment by businesses (i.e., investments actually under the managerial control of the investor) and other arrangements that have a ''direct-investment-like'' characteristic (e.g., turnkey plants operated by a multinational firm under contract).

10. These two obligations—unencumbered right of establishment and national treatment—can impair governments' ability to pursue specific ''industrial policy'' goals, and many of the exceptions governments seek are in furtherance of such goals. No effort here is made to take sides in the industrial policy debate. However, efforts to implement specific industrial policies are more widespread in developing nations (including certain of the rapidly industrializing nations) than in most OECD nations, and thus negotiation of these two obligations likely would be more difficult in the context of an ADI with wide WTO participation than in the context of the OECD MAI. But by all accounts, the MAI itself is likely to be riddled with exceptions to both right of establishment and national treatment.

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implies that, when a host nation grants more favorable treatment to any investment from any nation than the MAI requires, that host nation must grant treatment at least as favorable to investments by MAI signatories. Again, the issue of exceptions is important. In particular, the specific issue has arisen in the MAI negotiations as to whether MFN exceptions should be granted in the case of ''regional economic integration organizations'' (REIOs) such as the European Union. For example, should one EU nation be allowed to grant preferential treatment to investments of investors from other EU nations without extending this treatment to all investments from MAI participating nations? The EU logic would say yes; the logic of the MAI would say no.

- Host and home nations would be obliged to allow unrestricted transfer of funds—both at the level of operating and capital funds—between investors and investments. Certain exceptions to this obligation would be routine (e.g., if the investor or the investment were under suspicion of criminal activity or some other infringement of the law); other exceptions might be allowed for balance of payments reasons.

- Host governments would be obliged to grant certain levels of investor protection. The most important of these obligations is that no host nation would be allowed to expropriate a direct investment except for a public purpose, on a nondiscriminatory basis, under due process of law, and with adequate and prompt compensation guaranteed to the investor.

One effect of adopting these obligations would be greater transparency: stated simply, investors would know with a high degree of certainty what rules apply to them in each country that adheres to these obligations.

With respect to these six sets of MAI obligations, there is widespread consensus on language pertaining to definition, funds transfer, and investor protection. Most of the differences center on the more difficult issues of exceptions to right of establishment, national treatment, and MFN. Undoubtedly, this same pattern would hold for ADI negotiations as well.

Though the stickiest area for both ADI and MAI will be allowable exceptions, WTO negotiations would face more demands for exceptions from developing nations than most OECD nations are seeking in MAI. One approach to handling these exceptions would be to allow developing countries to continue policies and practices deemed to be in violation of right of establishment and national-treatment obligations but to require that all such policies and practices be listed and for as many as possible to be phased out in accordance with published schedules. This approach was adopted with respect to Mexican policies and practices in the NAFTA negotiation, for example. Mexico is allowed far more exceptions in the NAFTA than are either Canada or the United States, but Mexico is simultaneously obligated to phase out many of these exceptions.

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Some countries have indicated that they would refuse to accept national treatment even as a principle (i.e., these countries would not obligate themselves to this principle even if they were allowed unlimited exceptions). However, the principle of national treatment is central to an agreement on investment, the purpose of which is to allow, to the greatest possible extent, unfettered flow of direct investment across national boundaries. Thus, nations holding this view could not participate in an ADI; for this reason, an ADI very likely would have to begin as a plurilateral agreement.

As already noted, one benefit of the ADI would be linkage to the WTO dispute resolution mechanism. However, the dispute settlement procedures would have to be supplemented considerably. This is because many investment-related disputes involve a multinational enterprise and a national or subnational government. However, in the WTO, only national governments (''states'') have ''standing''; no other party (such as a firm) can bring a dispute before the WTO.[11] The need for some sort of ''enterprise-to-state'' dispute settlement procedure, in addition to a ''state-to-state'' procedure such as in the WTO, has been recognized in the NAFTA (chapter 11, part B) and is contemplated within the MAI. However, neither of these integrates enterprise-to-state dispute settlement procedures into the existing WTO procedures, something that would be desirable and possible to achieve.

One alternative means to do this would be to create a two-stage procedure whereby, after lodging a dispute, a firm would first have to show it had standing. Standing would be granted if the firm could show probable cause that its interests had been damaged as the result of the failure of a government to honor obligations under the ADI. This determination would be made by a panel of jurists trained to hear such cases. The second stage would be consideration of the case by a WTO panel, which would examine the merits of the dispute and issue a recommendation.[12]

A reasonable question is, what would happen if the panel found against the defendant country and recommended a change in law or policy but the country did not implement the recommendations? In a state-to-state dispute, the plaintiff country would then be authorized to apply sanctions against the defendant country. This would be awkward in the case of an enterprise-to-state dispute; it is difficult at best to imagine a firm, even a

11. Governments could, of course, act as agents for firms in existing WTO procedures. The obvious flaw with this is that a government's interests (even the firm's home government, i.e., the government of the nation in which the firm has its headquarters) and the firm's may not coincide. Hence the government agent might not in good faith be able to represent the firm. Indeed, as business continues to ''globalize,'' it is increasingly likely that government and global-firm interests will diverge.

12. As in all disputes before the WTO, the disputants would first attempt to work out a mutually satisfactory resolution via consultation; only failing this could the case be brought to the two-stage process.

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very large multinational firm, applying sanctions against a country. One option would be for the home nation of the firm to be allowed to apply sanctions against the defendant country. However, in some cases this might conjure up images of the ''gunboat diplomacy'' practiced earlier in this century, where the interests of large firms were imposed by powerful nations on weak ones. A second option might thus be for the panel to be allowed to award monetary damages to the firm, to be paid by the country, in an amount equal to the damages the firm suffered as the result of the breach of obligation.[13] The two options are not, of course, mutually exclusive. For investment disputes, both options might be allowable.

Although it would be desirable to create enterprise-to-state dispute settlement procedures in order to implement an ADI within the WTO, these procedures would supplement rather than displace the existing state-to-state procedures for investment-related disputes. It remains entirely possible that a nation's interests could be affected by the investment policies of another nation and that this could result in a dispute. For example, a nation might believe that its exports were displaced (or threatened with displacement) by another nation's policies to induce international investors to locate production facilities in its territories. If these policies violated ADI obligations, a dispute could be lodged before the WTO that would be resolved using existing procedures.

Indeed, this example points up a major lacuna in the MAI. According to reports that have ''leaked'' from the MAI negotiations, MAI will not place any limitations on the use by national or subnational governments of ''investment incentives.'' By offering these subsidies or subsidy-like incentives to firms, governments do mean to induce firms to locate production facilities on their territories. Such subsidies can have distortive effects, for example, causing firms to relocate production from a relatively economic to a relatively uneconomic site, where subsidies are used to compensate differences in production costs to the firm. The net effect is to raise the cost to the world of producing the relevant goods or services. Despite the extra costs (and the deadweight losses imposed on society), governments often are eager to offer investment incentives to increase local employment opportunities. Indeed, government competition to attract investment often leads to agencies bidding against each other and upping the stakes.[14] The case is thus strong that there should be international agreements to put caps on such incentives or, better, to

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13. Such a procedure is in fact applied in enterprise-to-state dispute resolution in the NAFTA, where an arbitral tribunal can award monetary damages to a firm that suffers losses as the result of a nation's failure to honor NAFTA obligations. Indeed, under NAFTA procedures the tribunal can only award damages; it cannot recommend changes in law or policy.

14. In such a situation, the granting of incentives can take on the character of a classical ''prisoner's dilemma'' game: collectively, the authorities might be best off if no one offered any incentives at all. However, if just one authority does offer an incentive, every other

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eliminate most such incentives entirely.[15] For political reasons, however, the MAI negotiators have been reluctant to deal with this issue.

For this issue, the WTO is likely to be a better venue for achieving ''high standards'' than is the OECD. This is true for two reasons. First, rich nations (and rich subnational governments) can afford to offer more generous incentives than poor ones, for obvious reasons. Thus, limitations or elimination of investment incentives will benefit poorer countries more than richer ones, and hence the developing nations might as a group emerge as a stronger constituency for such limitation or elimination than the OECD nations. Second, WTO law already deals with export subsidies under the Agreement on Subsidies and Countervailing Measures, and a natural extension would be for this agreement to be enlarged to cover investment incentives.[16]

An issue often linked to investment is incentives that are granted in exchange for meeting certain performance requirements. Performance requirements are often a condition for entry as well. It has already been noted that unencumbered right of establishment implies that no performance requirements should be placed on international firms as a condition for entry. However, it remains to be seen what, if any, restrictions on performance requirements are embodied in the MAI.

The WTO to a limited extent already deals with such requirements in the TRIMs agreement. This agreement bans two types of performance requirements: local-content and export requirements. The reasoning was that these requirements distort trade flows and are inconsistent with GATT Article III (national treatment on internal taxation and regulation, not to be confused with national treatment for investments). Other types of performance requirements can easily have trade-distortive effects: local-manufacturing requirements, trade-balancing requirements, and mandatory technology transfer, for example. Part of the work of the ADI should be to enlarge the range of measures covered by TRIMs.

Two Routes to an ADI

As noted at the outset, there are two routes to reaching an investment agreement: use the MAI as the basis for an ADI, or start from scratch and

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authority's ''best response'' is also to offer incentives. Because at least one authority is almost sure to calculate that it can gain advantage unilaterally from offering an incentive, the result is that it does so and causes all other authorities to play this ''best response.''

15. There may be valid reasons for granting subsidies, however, and hence any discipline on investment incentives would have to attempt to distinguish between ''good'' and ''bad'' incentives. Generally, the distinction rests on whether the subsidized activity generates some tangible positive externality in excess of the cost of the subsidy. However, determining whether a subsidy in fact generates such an externality is problematic.

16. The Agreement on Subsidies and Countervailing Measures could already reach most investment incentives and that all that would be needed in an ADI would be a provision

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negotiate an entirely new instrument. With the MAI still incomplete and information on its content sketchy, it is difficult to evaluate these two alternatives. However, it seems a safe bet that the MAI will contain all six of the obligations listed in the previous section: a broad definition of investment, right of establishment, national treatment, MFN, unencumbered transfer of funds, investor protection. Were the MAI to be adopted (in an adapted version) by the WTO, the task would center on negotiation, nation by nation and sector by sector, of the exceptions to the main obligations. Thus, in practical terms, it might make little difference which route is taken. The yeoman's work in creating such an agreement will not rest in drafting the language of the obligations, but rather in the negotiation on what exceptions will be allowed.

The main problem with the WTO adopting the MAI is summarized in the expression ''NIH'' (not invented here). Those WTO member nations that have been excluded from the MAI negotiations already distrust this instrument simply because they had no role in its creation.[17]

Given the ''NIH'' factor and the fact that 80 percent of the work to negotiate an ADI would consist in hammering out exceptions, it is likely that the WTO will have to ''start from the ground up.'' The MAI will be a useful reference point, but it seems unlikely that the WTO will adopt it and adapt it to the WTO framework.

Conclusions

The principal reason negotiations on a Multilateral Agreement on Investment are proceeding at the OECD rather than at the WTO is that the OECD member nations collectively have felt that few if any nonmember nations were prepared to enter into such negotiations at a serious level. In the end, whether an agreement on investment will be reached at the WTO depends upon at least some of these nations deciding that such an agreement is, after all, in their best interests.

But is it? The case can be advanced that the answer is an unequivocal yes. The benefits of direct investment, as noted earlier in this chapter, are virtually without question. These benefits exist for all nations, but they are especially important to developing nations seeking to catch up technologically with the advanced nations. Subscription to a strong multilateral agreement on direct investment would help the subscribing country attract such investment and capture these benefits.

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indicating that no investment incentive would be granted that was actionable under this agreement.

17. This has come out in a number of meetings, in particular one held by the OECD in Hong Kong in March 1996, where representatives of about 20 Asian and Latin American non-OECD nations attended. All but two of these nations spoke against the MAI.

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Why, then, are many developing countries apparently unwilling to subscribe to an ADI? There are several reasons.

One is largely tactical. Developing countries seek action on a number of agenda items, including accelerated liberalization of textile and apparel trade and trade in agricultural goods, and hence negotiators from these countries might hold back on investment rules, hoping to use these as a bargaining chip. But also, on the substantive side, residual 1970s thinking remains about direct investment and multinational enterprises. Although this sentiment is receding worldwide, enough of it remains in certain nations to block their participation in an effective ADI.

A second reason for developing-nation reluctance is a persistent belief on the part of some national investment development agencies that performance requirements can benefit local economies, including by making them conditions for entry; thus the relevant authorities are unwilling to subscribe either to limitations on performance requirements or to an obligation to allow unencumbered right of establishment. This can and often does lead to policies that are shortsighted even from a national point of view: firms tend to demand privileged access to markets in exchange for accepting performance requirements (which can impose additional costs on the firm), and thus the nation loses potential benefits of competition as part of the deal. And, as already noted, the global effect of the performance requirement is distortive: overall, the world loses benefits.

One aspect of an ADI that most developing nations would readily endorse would be an obligation on international firms to obey the laws and policies of the nations in which they do business. Such an obligation would also be in the firms' own interests. In particular, under such an obligation, a subsidiary of a firm in nation A would be obligated to follow that nation's law and policy, even if this were to conflict with the law and policy of some other nation. In a word, the obligation would help to resolve the dilemmas a firm faces when a nation tries to apply local law and policy extraterritorially. Such an obligation in turn might dissuade certain governments from such attempts.[18]

Indeed, much of the benefit of an ADI would be to constrain governments from taking actions that are both shortsighted from a national point of view and distortive from a global perspective. However, as long as national leaders believe that selective intervention can serve national interests, the benefits of such constraints will be lost to view.

How lost to view are these benefits? The assumption behind the MAI is that, outside the OECD, the fog is very thick. Given the policy shifts that are occurring in many nations, this seems overly pessimistic. Surely

18. The implicit restriction on extraterritorial application of law and policy should, however, itself be subject to certain exceptions—for example, nations with nuclear weapons would be allowed to prevent transfer of relevant technology between overseas subsidiaries of firms based within their sovereign jurisdiction.

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a plurilateral agreement within the WTO is possible, where at least one non-OECD nation would be willing to join in the fray. And who knows: once the ship sets sail, the fog might lift.

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