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Dissecting the MAI

This chapter provides a brief but comprehensive examination of the MAI itself, based on the negotiating text dated 24 April 1998. This was the last draft completed before the negotiations collapsed in the autumn of 1998, and, in fact, no further negotiations took place following publication of this draft. Thus one is faced at the outset with the problem of evaluating a draft that was neither agreed to by all parties nor even completely finished. And although most of the main provisions of the agreement were in place, much of the language was bracketed, meaning that consensus had not been reached on that language. Some of the bracketed language represents major unresolved conflicts, but most of it reflects minor differences over wording. The upshot is that the April text is sufficiently complete to provide a fair idea of where the MAI was headed, even if some of its main provisions and a number of its details might later have changed, some substantially.

This chapter also identifies some deficiencies in the MAI as it stood at the time of the talks' collapse. The main ones in the core text were failures to address investment incentives and taxation. (Chapters 1 and 2 have already discussed some reasons why these were omitted.) This chapter also argues why some discipline on investment incentives would have been appropriate and examines why the negotiating parties failed to achieve this objective.

A third major deficiency was that the MAI failed to achieve significant liberalization of current policy toward direct investment in the OECD countries. This is largely the result of the large number of exceptions that would have been registered in annexes to the main text. Thus, although the MAI draft was close to 200 pages in length and contained many provisions covering a wide range of issues, at the end of the day it would have changed little in the investment policies of the signatory countries. Any evaluation of the MAI's potential effectiveness must, of course, be based on a simple criterion: would these provisions have served to remove or significantly reduce distortions created by governments that diminish the total value of goods and services that international investment makes possible (see chapter 1)? Granted, it is very difficult to quantify this lost value of goods and services, or the extent to which an international agreement such as the MAI might have been able to prevent this loss. Nonetheless, it is clear that the MAI, as it was drafted and had all extant national exceptions to core principles been allowed, would have been inadequate to reduce these distortions and losses to any significant degree.

The main reason this was so was, again, simply that the MAI would have achieved virtually no change in current government policy or practice on the part of any of the signatory countries. However, this statement must be qualified. Although the MAI itself would not have forced significant, immediate changes in national policy, such changes might have resulted from decisions handed down under the application of the agreement's investor-to-state dispute settlement procedures. Unfortunately, as we saw in chapter 2, experience to date with similar provisions in NAFTA has not been wholly reassuring. The dispute settlement provisions have so far been used in many cases to attack regulatory takings, including those created under regulations designed to protect health and the environment.

Although some such regulations might produce economic distortions, it can be argued that such distortions are the price one pays for a cleaner and healthier environment (see chapter 5). And as argued in chapter 2, the Ethyl Corporation's complaint against Canada—the NAFTA case to date with the clearest environmental implications—was settled without resort to a tribunal finding and did not establish an antienvironmental precedent. Another case with environmental implications, Metalclad's complaint against Mexico, also described in chapter 2, was decided in Mexico's (and the environmentalist movement's) favor. Nonetheless, the investor-to-state dispute settlement procedures represent the one element that the MAI would have created having the potential to force changes in countries' law and policy. What outcomes would have resulted from application of these procedures remains unknown.

But this in itself poses a problem. One of the worst fears of the MAI's opponents was that countries that signed the MAI might be yielding elements of their sovereignty to some unknown tribunal unaccountable to anyone. This fear might have been overblown, but it did bolster opposition to the agreement.

Also figuring importantly in the MAI's failure to achieve real liberalization was the fact that it would have been a stand-alone instrument. That is, it would not have been linked (in a formal legalistic sense) to existing agreements in the WTO or elsewhere. This creates the problem in the services sectors already alluded to in chapter 1: any concessions granted in the MAI in sectors covered by the WTO's General Agreement on Trade in Services (GATS) would, under GATS obligations, have to be granted on a most-favored-nation basis to all WTO members. Thus, liberalizing measures to which the OECD countries might have been able to agree among themselves could not be realized unless these countries were willing, in effect, to extend them almost universally.

The draft MAI did incorporate certain core provisions on which, for the most part, the negotiating parties had achieved consensus. These would have established clear principles acting in the direction of investment liberalization, by removing laws and policies that discriminate against foreign investors. These included provisions pertaining to national treatment, most-favored-nation status, and investor protection, which are discussed in detail below. Most of these provisions were, in fact, borrowed from existing legal instruments, such as NAFTA and various bilateral investment treaties.[1] Even so, some of the language in these provisions was bracketed, again indicating that no consensus existed.

Had the draft MAI's core principles been applied without exception, they would have served to eliminate most remaining barriers to investment within the OECD, and hence would have generated some benefits. Their value would have been enhanced had they been extended to developing countries, where barriers and discriminatory policies are more widespread. Thus, even though the MAI, by virtue of the exceptions, would have done little to liberalize current policy, it nonetheless might have contributed to future liberalization by establishing a set of strong principles on which certain countries had agreed and on which future negotiations to liberalize further would be based. In other words, the MAI arguably set the stage for future policy changes, even if it did not immediately lead to such changes.[2] Also, had countries not party to the MAI negotiations subsequently joined the agreement, they might have been required, as a condition of accession, to change their policies that did not conform to MAI obligations. Whether any of this would have actually happened is, of course, a matter of conjecture. Nonetheless, the case can be made that, even if the MAI had achieved little in the way of "up-front" liberalization, it would have created a long-run dynamic process by which substantial liberalization could have been achieved over time.

However, whether such a dynamic would have come about is speculative and the fact remains that the MAI was largely status quo preserving. Given this, it is perhaps surprising that the MAI became such a lightning

1. On this matter see Dymond (1999).

2. However, as is stressed in both chapter 1 and chapter 7, significant investment liberalization has taken place worldwide over the past decade or so even without the MAI. At most, the MAI would have helped this process along.

rod for interest groups opposed to economic globalization. As we saw in chapter 2, these groups mounted their intensive campaign to defeat the MAI only after the release of the April 1998 draft. This campaign was never effectively countered by any pro-MAI constituency, presumably because no such constituency could identify any tangible benefit to itself from the MAI as drafted that was worth fighting for.

The objective of this chapter's examination of the April 1998 draft is to describe in some detail what purpose each provision was meant to accomplish and to evaluate whether it would have achieved that purpose. Where appropriate, this evaluation itself is embedded in a discussion of whether the purpose addressed a desirable end. Again, however, the draft MAI was a very lengthy document, and perforce the evaluation presented here is rather lengthy as well. The reader who is not interested in the details of the MAI provisions might therefore wish to skip the remainder of this chapter and proceed to chapter 4.

The Structure of the MAI

The MAI as drafted is what international economic policymakers call a top-down, free-standing agreement.[3] "Top-down" means that its obligations are binding on all signatory countries in all sectors, except where explicitly stated otherwise. By contrast, a "bottom-up" agreement would be one whose provisions apply only to certain specifically enumerated sectors and activities.[4] Exceptions in the draft MAI are of two types: "general exceptions," which would apply to all countries (and, in some instances, to all sectors) and country-specific "reservations." In the draft, the general exceptions are included in the main text with the core provisions. Separate from these are the country-specific reservations, which themselves come in two varieties, list A (those that may be negotiated away) and list B (those that are nonnegotiable). At the time that negotiations were suspended, not all countries had submitted detailed lists, but all had submitted indicative lists outlining the sort of exceptions that would be sought.

The entire MAI thus consists of the core provisions and the list of separate, country-specific and sector-specific reservations. Although, unlike the core provisions, this list has not been published, persons involved with

3. For expositional convenience, the rest of this chapter describes the draft MAI's provisions in the present tense rather than the conditional, having duly noted that the agreement never actually came into force.

4. Thus, for example, the WTO General Agreement on Trade in Services (GATS) is a bottom-up agreement, whereas the General Agreement on Trade and Tariffs (GATT) is top-down. In terminology also sometimes used in diplomatic contexts, a top-down agreement adopts a negative-list approach, that is, the agreement covers all but a list of sanctioned exceptions. A "bottom-up" agreement, conversely, takes a positive-list approach, with obligations applying only to what is explicitly listed.

the negotiations have indicated that, when complete, it would have codified essentially without modification all existing provisions of the OECD countries' laws that were not in conformity with the core provisions.[5]

The term "free-standing" means that the MAI would not have been part of the WTO framework but rather would have operated outside this framework. As noted earlier, this aspect of the MAI could have caused problems of consistency between countries' MAI obligations and their WTO obligations. If an MAI signatory wished to avoid this problem in a given sector, it might have registered that sector as an exception to the MAI. This would have been risky, however. If the exception were later challenged under the WTO's dispute settlement mechanism, the panel empowered to resolve the dispute might not have recognized the exception. This problem of potential inconsistencies between MAI and WTO obligations was one that had not been addressed at the time the MAI negotiations ended.

Goals, Scope, and Application

The draft MAI is organized into 12 articles:

I. General Provisions
II. Scope and Application
III. Treatment of Investors and Investments
IV. Investment Protection
V. Dispute Settlement
VI. Exceptions and Safeguards
VII. Financial Services
VIII. Taxation
IX. Reservations
X. Relationship to Other International Agreements
XI. Implementation and Operation
XII. Final Provisions

This text discusses only the eight articles that would have created new substantive rules. Four articles (VII, VIII, X, and XI) tied the MAI to other international agreements without adding new provisions.

Article I consists mostly of a preamble outlining the basic goals of the agreement. These goals include "to strengthen ties of friendship and to promote greater economic co-operation" among the participating countries, to further recognition that "international investment has assumed great importance in the world economy and has considerably contributed to the development of their countries," to seek "agreement upon the treat-

5. See Dymond (1999); see also Henderson (1999).

ment to be accorded to investors and their investments [that] will contribute to the efficient utilization of economic resources, the creation of employment opportunities, and the improvement of living standards," and to ensure that "fair, transparent, and predictable investment regimes complement and benefit the world trading system." The article further affirms that the signatories (which the draft refers to as the contracting parties) wish "to establish a broad multilateral framework for international investment with high standards for the liberalization of investment regimes and investment protection and with effective dispute settlement procedures." Also mentioned among the goals is a renewal of the signatories' commitment to the Copenhagen Declaration of the World Summit on Social Development and to observance of internationally recognized core labor standards.

Even this preamble contains bracketed language, however. Examples include references to environmental protection and conservation, to a reaffirmation of the 1992 Rio Declaration on Environment, and to the "development of world-wide rules on foreign direct investment in the framework of the world trading system as embodied in the World Trade Organization."

The preamble's provisions pertaining to the environment and labor, incidentally, constitute the only language in the draft MAI on these issues apart from Article III. (As discussed below, provisions in that article bind governments to not lower standards on labor or the environment as a means of attracting investment). Nothing in the preamble, however, represents a binding obligation on any signatory—the preamble is simply a statement of goals. One issue that remained unresolved when the MAI negotiations were terminated was whether or not to add language to create binding obligations pertaining to these goals. As chapter 2 noted, any such obligations would have reduced the likelihood of non-OECD countries signing the MAI; they would also have generated opposition within the business communities of the OECD countries themselves. Indeed, the OECD Business-Industry Advisory Committee (BIAC), the official liaison between the OECD and the business community, had advised against inclusion of such obligations. But at the same time, certain negotiating parties, including most fervently the United States, favored their inclusion.

Finally, the preamble also indicates that the MAI shall be free-standing (as defined above) and open to accession by all countries, not just OECD members.

Article II, on the scope and application of the agreement, defines the terms "investor" and "investment" for purposes of the agreement and lays out its geographic scope. At the outset of the negotiations, in response to pressure from the business community, the goal was established to define very broadly the types of investors and investments that would be covered. Thus, "investor" includes both natural persons having "the nationality of, or . . . permanently residing in, a Contracting Party in accordance with its applicable law" and "legal person[s] or any other entity constituted or organized under the applicable law of a Contracting Party." The first category covers investors who are living human beings, whereas the second includes all types of business enterprises, whether for profit or not, and whether privately owned or state owned. An "investment" includes "every kind of asset owned or controlled, directly or indirectly, by an investor." Thus the scope of the MAI would have extended quite broadly, to portfolio investment as well as to direct investment. Intangible investments such as intellectual property would also have fallen under the scope of the agreement. This provision was sought by the business community as a means to create additional ammunition over and above that already created in the WTO Agreement on Trade-Related Intellectual Property Rights (TRIPs) against unauthorized use of intellectual property. Also covered are "nonequity" alternatives to direct investment such as long-term management contracts, under which a firm holds managerial control over, but not equity in, another business firm outside its home country. In all, the article defines eight categories of assets to be covered by the agreement.

Whether the agreement should have been so wide in scope is open to question. Without a doubt, the principal intent of the participating countries (and of their business communities) was for the agreement to apply primarily to direct investment: business operations in one country owned by and under the direct managerial control of investors in another. Most of the MAI's core provisions are indeed written primarily to apply to this type of investment, and their application to other forms of investment can pose certain problems. Some of the most important of these are illustrated later in this chapter and in chapter 6. Chapter 7 presents a case for narrowing this scope in any future multilateral investment agreement.

The geographic scope of the agreement essentially extends to all territory under the sovereign control of the signatory countries, including maritime areas beyond the "territorial sea" as defined in the 1982 United Nations Convention on the Law of the Sea. Elsewhere in the agreement (and discussed later in this chapter) are provisions for resolving disputes between signatories, as well as those between private investors and signatories, arising under the agreement. The draft MAI implicitly discourages application of one country's law and policy into territory under the sovereign control of another (so-called extraterritoriality), in favor of recourse to these dispute settlement procedures. Issues of extraterritoriality, especially those arising from the US Helms-Burton legislation, led to much difficulty in the negotiations, as narrated in chapter 2.

Obligations of Host Countries

Article III of the draft MAI, titled "Treatment of Investors and Investments," covers the obligations of signatory governments toward investors and their investments. Not all of these obligations are of equal importance, of course. However, these and the provisions on dispute settlement are, collectively, the most important parts of the whole agreement, and the parts most worth salvaging in any future investment negotiations, because they establish two key principles. The first is that governments should not, within their territories, discriminate in favor of domestically controlled enterprises against enterprises controlled by investors in a signatory country. And the second is that governments should not favor enterprises controlled by investors from one foreign country over enterprises controlled by investors from a signatory country. These principles of nondiscrimination are a critical tool for removing the government-imposed distortions that limit the efficient worldwide allocation of investment. Without these principles in place, the world economy will fail to achieve the maximum output from the limited investment resources available.

Binding international obligations of this kind can in effect "save governments from themselves," by giving them reasons to deny preferential treatment of investments controlled by politically powerful domestic constituencies (or by foreign investors with ties to local politicians). These preferences often have the effect of creating local monopolies or oligopolies and stifling the benefits that accrue from open competition among rival sellers of comparable goods and services. Such preferences might be very good for the domestic group that receives them. They might even be good for a politically well-connected foreign multinational that seeks to preserve a local monopoly against incursion by other multinationals. But rarely are they good for a country or its citizens as a whole.

The list of obligations in Article III is lengthy, but five of them appear essential to achieve the agreement's overall objectives. These five core obligations pertain to national treatment, most-favored-nation treatment, transparency, performance requirements, and investment incentives (on which there was no agreement at the time the negotiations were terminated). The rest of this section first examines each of these core obligations in detail, and then turns to an examination of other, arguably less important obligations.

National Treatment and Most-Favored-Nation Treatment

Two obligations of the MAI—the national treatment obligation and the most-favored-nation obligation—constitute the agreement's main provisions against discriminatory treatment of foreign investors and their investments. The national treatment clause reads as follows:

> Each Contracting Party shall accord to investors of another Contracting Party and to their investments, treatment no less favorable than the treatment it accords [in like circumstances] to its own investors and their investments with respect to the establishment, acquisition, expansion, operation, management, maintenance, use, enjoyment, and sale or other disposition of investments.

This clause is meant to ensure that neither foreign investors nor their investments are subject to discriminatory treatment from governments, in the sense that the foreign investors or investments are treated less favorably than domestic investors or investments.

One element of the draft MAI that distinguishes it from most other efforts to codify rules for investment is that the national treatment clause applies on a preestablishment as well as a postestablishment basis. Most bilateral investment treaties call only for the latter. Thus the MAI, in principle, rules out laws and policies designed to discourage new entry by foreign investors if these laws and policies do not apply equally to new entry by domestic investors. Had this principle been implemented without exception, it alone would have been a major liberalization. Even among OECD countries, national governments do have in place laws and policies that discriminate against foreign entry. However, these almost surely would have been preserved in the form of reservations had the MAI come into force.

The clause establishing most-favored-nation treatment reads as follows:

> Each Contracting Party shall accord to investors of another Contracting Party and to their investments, treatment no less favorable than the treatment it accords [in like circumstances] to investors of any other Contracting Party or of a non-Contracting Party, with respect to the establishment, acquisition, expansion, operation, management, maintenance, use, enjoyment, and sale or other disposition of investments.

This clause is meant to ensure that investors of one country (whether an MAI signatory or not) and their investments do not receive more favorable treatment than that granted to any MAI signatory. A third clause requires that signatory countries grant investors and investments of all MAI signatories the more favorable of national treatment or most-favored-nation treatment.

One issue not fully resolved when the negotiations broke down was whether or not there should be an exception to the most-favored-nation clause for regional economic integration organizations (REIOs). The issue was whether or not preferences granted within the European Union could be continued without the EU members having to extend these to nonmember MAI signatories on a most-favored-nation basis. The United States, on behalf of itself and most of the other non-EU countries in the OECD, argued that such preferences should, as a matter of principle, not be allowed. The United States stuck to this position in spite of the fact that certain preferences created by NAFTA might have been covered under the REIO exception, to the benefit of investors of the United States and their investments. Apparently, the United States was prepared to give these benefits up. The United States seems to have been mainly concerned not over preferences currently in effect in the European Union, but rather over new preferences that might be created in the future, especially regarding investment in countries that are candidates for future EU accession. Of major concern was that the European Union might conclude agreements with former Soviet bloc countries that would give EU investors preferential claims on assets being privatized in these countries. Separate provisions of the MAI, discussed below, pertain to privatizations that attempt to provide nonpreferential and nondiscriminatory treatment for foreign investors as potential acquirers of privatized assets. Thus a major US concern was that a REIO clause would create special exemptions from these provisions.

Transparency

The basic requirement of the draft MAI's transparency clause is that all signatory countries publish "or otherwise make publicly available" all laws, regulations, and other policies applicable to foreign investors. Also, each signatory is required to "promptly respond to specific questions and provide, upon request, information" to other signatory governments with respect to such laws, regulations, and policies. However, neither these requirements nor any other provision of the MAI prevent a signatory government from requiring foreign investors or their investments to provide "routine information concerning that investment solely for information or statistical purposes." Governments can protect the confidentiality of information thus given. That is, information that must be provided to other signatory governments would not include information provided by foreign investors and their investments that is protected by assurances of confidentiality.

The transparency requirement is very important for the simple reason that, without it, governments might pursue unannounced or unpublicized policies that are highly discriminatory. This would clearly undermine the benefits that would ensue from the pursuit of those nondiscriminatory policies that are announced.

Performance Requirements

The draft MAI's provisions on performance requirements are among its most important elements, and it is important to understand what the agreement would and would not do in this matter. Performance requirements are obligations placed on foreign investors or (more commonly) their investments to do certain things in pursuit of national objectives. Often these objectives pertain to industrial policy. The objectives can be economic in nature, but may be social or political. Analysts, especially economists, have long objected to such requirements, largely on grounds that they can distort economic decisions and render the outcomes suboptimal. For example, a government might require that a local subsidiary of a multinational firm export some minimum percentage of its output. Such a requirement might help that government meet a national goal of export expansion, but it might also cause the exports of some other country to be displaced. The net result would be an overall reduction of economic efficiency, under the presumption that the second country can produce and export those goods or services at lower cost than the first country. Thus, it is argued, such a performance requirement can have effects not unlike those of a trade restriction or export subsidy, and hence should be subject to the same level of international discipline.

A recent study (Moran 1998) stresses that the effects of most performance requirements imposed on multinationals by developing countries are so perverse as to actually retard development in the country imposing them. Thus, whereas most analysis of performance requirements highlights the adverse effects on countries other than the one imposing the requirement, the latter is not immune. Those performance requirements especially likely to have negative effects on host countries include local content requirements, requirements for joint ventures or other forms of local equity participation, and requirements that would force technology transfer. Moran does note, however, that export performance requirements have in some cases benefited the country imposing them. (Mexico's export requirements placed on local subsidiaries of major automobile firms are an example.)

The negative aspects of performance requirements were explicitly recognized during the Uruguay Round of multilateral trade negotiations. One of the products of those negotiations was a new Agreement on Trade-Related Investment Measures (TRIMs), which has been administered by the World Trade Organization since 1995. The TRIMs agreement, however, covers only two types of performance requirements: local content requirements and trade balancing requirements (these are defined below). Local content requirements had already been declared inconsistent with Article III of the General Agreement on Tariffs and Trade (GATT) by a GATT disputes settlement panel during the 1980s. Certain of the parties that had negotiated the TRIMs agreement (including the European Union, Japan, and the United States) had sought a wider coverage than was actually agreed to, and the clause on performance requirements in the draft MAI reflects their earlier position.

The draft MAI bans signatory governments from imposing a number of types of performance requirements as conditions of entry or of continued presence of a foreign investor or investment. This list significantly expands the TRIMs obligations. However, the qualification "as conditions of entry or of continued presence" is important. As is discussed below, the same performance requirements in other circumstances, such as when linked to investment incentives, would not necessarily be banned. Indeed, performance requirements are most commonly used in OECD countries under just such circumstances.

The requirements to be banned as conditions of entry (or expansion, operation, maintenance, use, enjoyment, sale, or other disposition) of an investment were those that require a foreign investor:[6]

- to export a certain percentage or level of goods or services (export performance requirements);
- to achieve a certain percentage or level of domestic content in their output (local content requirements);
- to purchase, use, or accord a preference to goods or services produced or provided in the territory of a signatory country or from persons in its territory (a variant on local content requirements);
- "to relate in any way the volume or value of imports to the volume or value of exports or to the amount of foreign exchange inflows associated with such investment" (trade balancing requirements);
- "to restrict sales of goods or services in its territory that such investment produces or provides by relating such sales to the volume or value of its exports or foreign exchange earnings" (a variant on trade balancing requirements);
- "to transfer technology, a production process or other proprietary knowledge to a natural or a legal person in [the host country's][7] territory, except when the requirement is imposed or the commitment or undertaking is enforced by a court, administrative tribunal, or competition authority to remedy an alleged violation of competition laws [or to act in a manner not inconsistent with (relevant articles) of the TRIPs Agreement]" (technology transfer requirements);
- to "locate its headquarters for a specific region of the world or the world market in the territory of that Contracting Party";
- to "supply one or more of the goods that it produces or the services that it provides to a specific region or the world market exclusively from the territory of that Contracting Party";
- to "achieve a given level or value of production, investment, sales, employment, or research and development in its territory" (another variant on local content requirements);
- "to hire a given level of [local personnel] [nationals]";
- "to establish a joint venture" (presumably with local partners, although this is not specified); or
- "to achieve a minimum level of local equity participation."

6. "Foreign investor" includes subsidiaries under the investor's control.

7. The alternative bracketed phrases indicate that the choice of wording remained undecided in the draft.

All the items in the list except the first are types of performance requirements identified by Moran (1998) as potentially harmful to economic development. The apparent redundancy in the language banning local content requirements was considered necessary because, in implementing the TRIMs agreement, which also bans local content requirements, much confusion has arisen over what exactly constitutes such a requirement. Some of this confusion has resulted from the efforts of certain governments to preserve local content requirements by, in essence, disguising their true nature. The negotiators of the MAI thus felt it necessary to supplement the blanket ban on local content requirements by specifically banning those variants that have been subject to controversy in the TRIMs agreement.

Investment Incentives

At the time of the MAI negotiations, no OECD country generally imposed performance requirements on foreign direct investors as a condition of entry or continued presence. But some OECD countries have often made performance requirements conditions of receipt of investment incentives. Investment incentives are subsidies and subsidy-like measures granted to investors who agree to place their investments in the territory of the government granting the incentive. In addition to these OECD countries, many Asian countries, including some in Southeast Asia as well as China, have offered these incentives.

As already noted, the MAI draft did not effectively establish disciplines over investment incentives. But considerable theoretical analysis and empirical evidence indicates that such incentives can result in foreign investments going to locations where they are less efficient than they could have been. Investment incentives may, in addition, waste the resources of the governments that offer them, in the sense that any benefits derived locally therefrom may be fully offset (or more than offset) by the costs.

These propositions can be illustrated by the following example, which is based on an actual case as described by a senior government official of the country (an Asian nation) that offered the incentive. The official claimed that the incentive created benefits for this country. In fact, a dissection of the official's own arguments shows that the incentive reduced world welfare, and may have failed even to bring net local benefits.

What happened was as follows. A large multinational firm was considering investing in one of two countries in order to expand output of one of its products. In one of the countries (that of the official who is the source of the example, which we will call country A), the firm had no existing facilities for this product and would have had to build a new one from scratch. In the other country (country B), however, the firm already owned a production facility and could have simply expanded that facility. The product in question embodied a rather sophisticated technology, and officials of country A believed that, if the firm could be enticed to locate the new facility in their territory, the country would capture some external benefits in the form of technology transfer.

Management of the firm represented to officials of country A that to expand the facility in country B was in fact the more economic alternative. However, management also indicated that they would consider building a new facility in country A instead if given some sort of financial incentive to do so. In response, country A did offer a large package of incentives, and the production facility ended up being located there. Officials of this country therefore proclaimed its granting of investment incentives to be a major success.

But who were the real winners and losers in this episode? Let us first assume that the firm told the truth when it said that, incentives aside, it was more economical to locate facilities in country B than in country A. It follows that location of the investment in country B reduced world economic efficiency. It simply would have been less costly (that is, would have required fewer economic resources, and, hence, from a world perspective, efficiency-enhancing) had the firm located the investment in country B.

In the actual case, the firm did not disclose the reasons why it saw country B as the lower-cost location. However, a reasonable conjecture is that expansion of the existing facility would have enabled the realization of scale economies, or economies in logistics, that could not be realized by a new facility in country A. Thus the incentives represented, in effect, a transfer payment by the taxpayers of country A to subsidize the inefficient location of the facility in that country. One wonders whether the officials of country A would have won praise from their country's taxpayers if they had presented their "triumph" in this light.

But it gets worse for the hapless officials of country A. What if the firm in fact was bluffing about country A's locational disadvantage? What if country A had been the preferred choice all along, and the firm had claimed to prefer country B simply as a ruse, to induce country A's officials to offer an incentive package? This is not a far-fetched hypothesis. Country A was known to be rather profligate in its use of investment incentives, and executives of the firm were surely aware of this. If indeed the firm was bluffing, then the outcome of the story was that taxpayers in country A were suckered into paying the firm to do what it would have done without the incentives. In other words, all the benefits of the investment in country A might have been attained at no cost to the country. If this were true, rather than proclaiming success, the officials who granted the incentives should have hung their heads in shame.

In their defense, however, the officials might have pointed to the external benefits generated by the investment and noted that, given uncertainty about the firm's true situation, it was economically rational to grant incentives up to the amount of these externalities. If the officials had no way of differentiating bluff from truth, the granting of incentives served as a kind of insurance policy, ensuring that country A would realize at least some of the potential benefits. This possibility arguably exonerates these officials from wasting the taxpayers' money. But it does not exonerate them from the charge that their actions contributed to lost welfare globally. Indeed, even if the firm was not bluffing, the net result of the offering of incentives was that potential external benefits were created in country A at the expense of country B. In other words, the incentive created a "beggar-thy-neighbor" effect as well as a reduction in world economic welfare.

One argument for international rules to abolish or constrain the use of investment incentives is that, in cases like that just described, firms would have a reduced incentive, or none, to bluff about their locational preferences for new investments when dealing with host-country governments. An even stronger argument is that investment incentives necessarily result in either a loss of world welfare or an unnecessary transfer from taxpayers to foreign investors. If an investment would have gone to a particular location even without incentives, then incentives impose a cost on local taxpayers without creating any offsetting gain. But if the incentive results in placement of an investment in a nonoptimal location, it creates global welfare losses accompanied by beggar-thy-neighbor effects.

Why, then, does there seem to be so little willingness on the part of officials to end investment incentives? One reason is that, as we have seen, such incentives can create external benefits for the country offering them. The incentives may reduce global welfare, but the costs are felt elsewhere. And officials, after all, are accountable to their own citizens, not to those of foreign lands. The value of incentives as an insurance policy also accounts for countries' reluctance to give them up.

This propensity to offer incentives is magnified if governments believe that other governments are offering incentives for the same investment. Indeed, if multiple governments are seeking the same investment, the likely result is that they will bid against each other. The price paid by the winning government will then likely be significantly higher than if only one government were in the bidding. The reason is that each government believes, to a point, that if it can outbid other governments, the investment will generate net benefits even after accounting for all the costs of the bid. But without question, all governments would be better off if none of them bid for the investment and the "winner" were determined by its intrinsic locational advantage.

The situation just described is a familiar one in economics, where it is known as a "prisoner's dilemma." In a prisoner's dilemma, each party has an incentive to bid if it believes that other parties will also bid, but also, and perversely, each party has an incentive to bid if it knows that *no* other parties will bid. Yet if all parties bid, all are made worse off than if no one bids. Hence the best outcome for all is for all parties to agree that no one will bid. But this outcome is difficult to achieve, because each party believes that if it cheats on the agreement (and no one else does), it will come out ahead. Thus each party faces an incentive to cheat. Further, each party knows that all other parties face the same perverse incentive. Thus the likely outcome is that all parties will cheat. Indeed, because each party also knows that, if other parties cheat, it should cheat as well, each party's best move is to cheat from the outset. The consequence is that, even if all parties understand that their mutual interest lies in no one bidding, the actual outcome will be that all bid.

It is well established in the economic literature based on game theory that there is only one way to achieve the optimal solution in a prisoner's dilemma. That is for the parties both to agree among themselves not to bid *and* to devise a means to punish those that might cheat on the agreement (see, e.g., Friedman 1986, chapter 3). Indeed, it has been suggested in the theoretical literature that the whole WTO framework constitutes such an agreement, where sanctions applied through the dispute settlement process serve as punishment for any party that cheats on a WTO obligation. Similarly, it can be argued that multilateral rules like those of the WTO, together with an effective dispute resolution mechanism, are the only available and potentially effective means of limiting the efficiency- and welfare-reducing properties of investment incentives.

In the meantime, however, governments persist in granting such incentives. Indeed, there is evidence that their use rose substantially over the course of the 1990s.[8] Hence there would appear to be a strong prima facie case for some sort of ban or restriction on these incentives as part of a multilateral investment agreement.

This case is magnified greatly when such incentives are linked to performance requirements. In effect, this linkage serves to compensate investors for making suboptimal investment decisions. Thus, for example, a given site for the manufacture of a product might be uneconomic, in the sense that the delivered cost of the output is greater than could be achieved at another location. But a firm might be willing to locate production at the inferior site if it is offered enough of a subsidy to do so. In such a case, production at the inferior site imposes a cost on society at large: resources are used wastefully, and total output is less than what it could otherwise be. Of course, the main burden is borne by those whose taxes fund the subsidy.

Another problem with linking performance requirements to incentives is that these arrangements tend to be highly nontransparent: often they result from covert understandings between the agencies that grant the subsidies and the firms that do the investing. Thus, information about the

8. E.g., for Europe see European Union (1997). Among the major users of investment incentives are the US states, but information about the magnitudes and costs of these incentives are not published.

true extent of the practice is scant. However, it is clear that the investment subsidies granted by US states often do come with strings attached, as do investment incentives offered by national and regional investment promotion boards in Europe.[9]

Despite the clear distortions caused by linking investment incentives and performance requirements, the MAI negotiators were unable to agree on what to do about the problem. Bracketed language in the draft text would have committed the MAI signatories to future negotiations "to further avoid and minimize such distorting effects and to avoid undue competition between Contracting Parties in order to attract or retain investments." But it seems that certain OECD member governments preferred not to address the issue in the MAI at all. The main reason has to do with the federal structure of several of these governments, including those of Canada, Germany, and the United States. In all of these countries, investment incentives are handed out primarily by subnational governments: the state governments in the United States, the provincial governments in Canada, and the governments of the *länder* in Germany. In some (e.g., Canada), the problem is that, legally, the federal government might not be able to bind the subnational governments to a multilateral discipline on incentives, because it has no power over their spending policies. In others (e.g., the United States), the federal government clearly has this power but may be unwilling to use it for political reasons.[10]

The omission of investment incentives from the MAI is arguably the agreement's most blatant deficiency in terms of its ability to alter the practices of governments that might have adverse effects on the outcome of investment decisions. It probably is the most intractable as well, given that the problem has the nature of a prisoner's dilemma. (As one negotiator [who wishes to remain anonymous] put it, the failure of the MAI to create disciplines on investment incentives "was a triumph of realpolitik over economics.") As argued above, the only way to solve such a problem is for the parties to reach a consensus to bind themselves to mutually agreed upon disciplines, but for reasons just cited, no such consensus existed at the time the MAI negotiations were terminated.[11]

In addition to these four core obligations (or five, if one counts the empty obligation on investment incentives), Article III created other obligations that would apply to governments in their treatment of investors and investments. Many of the provisions establishing these obligations, however, were either not finished or not agreed upon when the negotiations broke down. Each of these is treated briefly in what follows.

9. Some of the best documentation of this practice is provided in reports prepared by governments of other countries. See, e.g., MITI (2000).

10. On the legal powers of the US federal government in this domain, see Enrich (1996).

11. Arriving at such a consensus would require a strong commitment to the desired outcome on the part of the top leadership of the negotiating countries. However, as chapter 2 revealed, such a commitment was almost totally lacking with respect to the MAI.

Temporary Entry, Stay, and Work of Investors and Key Personnel

The MAI negotiators originally intended to greatly simplify visa and other official requirements for nonnational personnel who might be assigned to work in an investment (usually a controlled subsidiary) of a foreign investor in an executive or technical capacity on a temporary basis. Provisions toward this goal would have qualified as promoting nondiscrimination in the sense that they would have ended preferences in employment for nationals of the country in which an investment is located. This goal was sought mostly by the business community.

The actual provisions in the draft MAI fell somewhat short of this goal. However, they did require that "Each Contracting Party shall grant temporary entry, stay, and authorization to work" to a natural person of another contracting party who is either an investor seeking to establish an investment or an employee of an enterprise covered by the agreement. The spouse and children of such a person must also be granted temporary entry and stay, and signatory governments are encouraged (but not required) to grant these spouses permission to work. Another provision allows investors to employ persons of any nationality to work in an investment, provided those persons have met national requirements.

According to some persons familiar with the negotiations, the negotiators' original intent was to make it easier than it typically is under existing law for foreign investors to employ in their subsidiaries persons who are not nationals of the host country. However, the existing text seems to do little more than ensure that signatory governments cannot require foreign investors to discriminate in their employment practices in favor of local nationals.

Nationality Requirements for Executives, Managers, and Directors

The draft MAI bans requirements relating to the nationality of executives, managers, and members of boards of directors of a foreign subsidiary whose parent firm is in an MAI signatory. Such requirements might include the stipulation that citizens of the host country be appointed to such positions in these subsidiaries.

Employment Requirements

The draft MAI requires signatory countries to allow investors of other signatories and their investments to employ any person of any nationality, providing that person holds a "valid permit of sejour and work" and the employment is compatible with that permit. It should be noted that this obligation and the one governing executives, managers, and directors are ones that all member countries of the OECD could meet with no change in existing law or policy. Members of the business community had sought a stronger provision that would have eased requirements for work permits. The extant, status quo-preserving language does not, of course, meet this goal. The language was retained in part at the behest of the business community in order that the issue might be revisited at some later time.

Privatization

The draft MAI imposes an obligation on signatories to accord both national treatment and most-favored-nation treatment to foreign investors seeking to purchase publicly owned assets being privatized. The same obligations would also apply to transactions after the initial sale. These obligations, however, do not disallow governments from executing voucher schemes that limit the purchase of such assets in an initial privatization to domestic residents, provided that this right is granted only to natural persons and that there are no restrictions on subsequent sales of the assets covered by the vouchers. Also, the MAI imposes no obligation on a signatory actually to privatize anything. The MAI negotiators sought to have the agreement cover special share arrangements (i.e., arrangements whereby managers, employees, or local residents are granted special treatment with respect to acquisition of shares in an enterprise to be privatized). However, four alternative drafts of such language were under consideration at the time the negotiations were terminated. These ranged from one draft that would ban most such arrangements to one that would permit them unless they were explicitly discriminatory or in violation of most-favored-nation provisions. (An example would be if the arrangement disallowed subsequent sale of the shares to a national of a signatory.)

Entities with Delegated Government Authority

Other provisions of the draft require that any entity to which a signatory government has granted regulatory, administrative, or other government authority act in a manner not inconsistent with MAI obligations. Among other things, the provision was a useful clarification that the obligation to provide national treatment extended to governmental and quasi-governmental regulatory agencies.

Monopolies, State Enterprises, and Concessions

The MAI draft contains the following bracketed provision: "Nothing in this Agreement shall be construed to prevent a Contracting Party from maintaining, designating, or eliminating a monopoly." An accompanying provision (not in brackets except as indicated) states that "Each Contracting Party shall [endeavor to] accord non-discriminatory treatment when designating a monopoly." The bracketed phrase would, of course, render this provision largely unenforceable. The MAI was meant to contain language precisely defining what constitutes a "monopoly" or a "designated monopoly," but as of the time that the negotiations were terminated, such language was not agreed upon, and several alternative definitions had been put forth.

A further provision requires that any designated privately or publicly owned monopoly:

1. not act in a manner inconsistent with MAI obligations with respect to any governmental, regulatory, or administrative authority delegated to it;
2. provide nondiscriminatory treatment to investors or investments of investors of another contracting party in the sale of monopoly goods or services;
3. provide nondiscriminatory treatment to these investors or investments in its purchases of monopoly goods or services (but this provision does not apply to procurement of goods or services by a government agency where these are for government purposes and are not for resale or for use in the production of a good or service for commercial sale);
4. not abuse its monopoly position;[12] and
5. act solely in accordance with commercial considerations in its sale or purchase of monopoly goods or services, except to comply with "terms of its designation that are not inconsistent with (the obligations just listed)."

Disputes arising over the application of these five obligations are not subject to the investor-to-state dispute settlement procedures but are subject to the state-to-state procedures.

If an activity is demonopolized, the relevant signatory is allowed to list a reservation regarding that activity at the time. Officially designated monopolies must also be notified to the MAI within 60 days of the agreement's entry into force, and any monopolies designated after the entry into force must be notified within 60 days, as must any elimination of designated monopolies and related new reservations.

State enterprises under the draft MAI would be subject to unfinished provisions for anticircumvention. "Anticircumvention" in this instance

12. Three alternative drafts to restrict such abuse are proposed, one of which is a "zero option" imposing no such obligation.

means that a government may not use a state enterprise to get around its MAI obligations. Rather, such enterprises would be bound by these obligations.

With respect to concessions (i.e., the transfer of any operation from public to private hands without transfer of ownership, for example, transfer of the right to mine on public land), two provisions would have applied. First, any such concessions must be transparent. "Transparent" here means that all relevant rules and procedures must be written in one of the two official languages of the OECD (French and English) and publicly available. It also means that publication must occur sufficiently in advance to enable candidates "to engage and, in so far as it remains compatible with an efficient operation of the mechanism of attribution of concessions, to accomplish the formalities required by qualifying evaluations." This latter (rather cumbersome) requirement was clearly intended to bolster nondiscrimination by disallowing procedures that de facto discriminate in favor of local persons over foreign investors. However, this requirement clearly would have been difficult to enforce. Second, the requirement for transparency does not apply to very small concessions (a threshold requirement was to have been established but was never decided) or to concessions associated with a designated monopoly.

Not Lowering Standards

Rather late in the negotiations, a provision was added to the draft MAI aimed at preventing other provisions from leading to an undesirable reduction in health, safety, labor, or environmental standards. This provision was inserted in response to pressure from nongovernmental organizations that believed that the MAI might have the effect of lowering such standards (see chapter 1). However, no specific language had been agreed to at the time that negotiations ceased. One version would obligate governments not to lower health, safety, and environmental standards and not to relax core domestic labor standards as a means to encourage investment. Another version would merely assert that it was "inappropriate" to lower or relax these standards.

As in other areas where language was not agreed upon, the main issue was whether or not the provision might be enforceable, in the sense that it could be the basis for bringing a dispute to the agreement's investor-to-state or state-to-state dispute settlement procedures. At the final negotiating sessions in the spring of 1998, certain negotiators, especially those of the United States, were leaning toward the obligatory language. Indeed, one of the US negotiators had made public statements suggesting that the United States might seek provisions pertaining to labor and the environment that went beyond this provision. But no action in this direction was actually taken.

Investment Protection Provisions

Article IV of the draft MAI deals with investment protection. One of the goals of the MAI, as articulated by the OECD Secretariat in a series of meetings held at the beginning of the negotiations, was to achieve very high levels of investment protection. Thus Article IV was accorded high priority during the negotiations, and this part of the draft agreement is largely devoid of bracketed or contested language. However, public reaction against the investment protection provisions as drafted was widespread and vocal. As detailed in chapter 2, critics of the MAI, especially the environmentally oriented NGOs, complained that these provisions, in conjunction with the MAI's investor-to-state dispute settlement procedures (and, arguably, an overly broad definition of what constitutes "investment") would have damaging repercussions. They could, the NGOs claimed, enable foreign firms to sue governments on an unprecedented scale for actions formerly considered within their sovereign rights but that might have adversely affected foreign investors' interests.

One issue that remains something of a mystery, especially in light of the opposition that the investment protection provisions created, is why the draft MAI should have contained the investment protection provisions it did. After all, the agreement was meant mostly to cover investment among the OECD countries, and these countries have a solid record of not expropriating each other's investments except in rare circumstances, and even then under due process of law and with compensation. In other words, there seemed to be little or no need for these provisions, at least unless and until the agreement was expanded to include developing countries, some of which have a history of expropriating foreign investments without due process or compensation.

These investment protection provisions of the draft MAI consist of six parts. The first part is on general treatment. This would have obligated MAI signatories to accord to investors of other signatories "fair and equitable treatment and full and constant protection and security . . . [no] less favorable than that required by international law."

The second part contained the article's core provision. It pertained to expropriation and compensation, the treatment of which is at the heart of the regulatory takings issue, discussed in the next chapter. This provision itself is in four subparts. The first is the one already quoted in chapter 2: "A Contracting Party shall not expropriate or nationalize directly or indirectly an investment in its territory of another Contracting Party or take any measure or measures having equivalent effect . . . except:

a. for a purpose which is in the public interest,
b. on a nondiscriminatory basis,
c. in accordance with due process of law, and

d. accompanied by payment of prompt, adequate, and effective compensation. . . ."

The remaining three subparts provide that such compensation is to be paid without delay, must be for the fair market value of the expropriated investment, and must be fully realizable and transferable. A further subprovision stipulates that "due process of law" includes the right of appeal for investors who feel that the compensation they receive for an expropriated property is less than the fair market value.

The third provision of the investor protection provisions deals with protection from strife. This provision essentially calls for national treatment in the event that investors suffer losses from war, civil disturbance, or similar disruptions. The negotiators meant this provision to be interpreted to mean that any such losses would be compensated only to the extent that the government chooses to compensate any party for losses due to strife. Because under most circumstances such loss is not subject to compensation, foreign investors would not normally be entitled to compensation. However, one subprovision explicitly states that if an investor of a signatory suffers loss as the result of requisition by another signatory's armed forces or destruction of assets by these armed forces, where this destruction is "not required by the necessity of the situation," the investor is entitled to have the loss treated as though it were an expropriation.

A fourth provision obliges signatories to allow investors of another signatory to transfer payments into and out of its territory freely and without delay. An illustrative list of payments that are allowed is provided, although it is noted that the list is not exhaustive. Thus, types of payments not on the list might nonetheless be subject to the same obligation. Signatories are obligated to ensure that such payments be made in a freely convertible currency at spot exchange rates. An important exception pertains to investors' freedom to transfer funds, however: signatories may restrict transfers in circumstances consistent with GATT provisions pertaining to balance of payments crises.

The remaining three provisions of the investor protection section are largely technical in nature. The first of these deals with information transfer and data processing. Signatories are not allowed to take measures to prevent the transfer outside their territory of information necessary for the conduct of business or related to the purchase or sale of an enterprise. They may, however, impose record-keeping and reporting requirements and take measures to protect privacy "including the protection of personal data, intellectual and industrial property, and the confidentiality of individual records and accounts."

The second of these provisions has to do with subrogation of claims. Here the basic obligation is that signatories must recognize claims that might arise out of assignment of a claim to a party other than the party originally holding the claim.

The third of these provisions is bracketed in the draft MAI. The basic obligation under this provision is that the investor protection provisions shall apply to investments existing at the time the MAI enters into force as well as to investments that might be established or acquired thereafter. What is left unresolved is whether the agreement would apply to "events which occurred, or to claims that had been settled, prior to its entry into force."

Dispute Settlement Procedures

Article V of the MAI establishes a set of dispute settlement procedures. Further, because the MAI was to have been a free-standing agreement and not part of the WTO, these dispute settlement procedures were to be independent and different from those of the WTO. Indeed, because the draft MAI imposes obligations on countries pertaining to international investors, which are not governments, and because only governments have standing (that is, the right to bring complaints) in the WTO's dispute settlement procedures, these procedures would not be adequate to the requirements of the MAI. The reason is that investors (e.g., large international firms) can have interests that diverge from those of their home-country governments. Indeed, disputes might arise between an investor and a host country in which the investor's home-country government would prefer an outcome entirely contrary to that sought by the investor. For example, the home-country government might not have wanted the investor to make the investment at all.

Thus the draft MAI provides for two distinct dispute settlement mechanisms. The first is a set of state-to-state procedures, intended to resolve disputes between governments. The second is a set of investor-to-state procedures, meant to resolve disputes between investors and governments. Both sets of procedures are modeled more closely on existing procedures of NAFTA than on those of the WTO.

In the MAI draft, the state-to-state dispute settlement procedures appear before the investor-to-state procedures. However, the negotiators envisaged that the former would normally be invoked only in the event of some failure in the execution of the latter. For example, the state-to-state procedures might be invoked if a signatory country should fail to abide by the outcome of proceedings under the investor-to-state procedures. For this reason it makes more sense to discuss the dispute settlement procedures in reverse order from that in which they appear in the text.

The draft MAI's investor-to-state dispute resolution procedures are similar but not identical to those of NAFTA. In both procedures, in the event of a dispute over interpretation or application of the agreement, investors are first urged to settle the dispute through consultation and negotiation with the appropriate authorities of the government against which the complaint is lodged. Failing this, under the MAI, an investor may submit the dispute to any of the following for resolution:[13]

- a competent court or administrative tribunal of the signatory country against which the dispute is brought;
- any procedure agreed to by both disputants; or
- arbitration in accordance with the MAI under the Convention on the Settlement of Investment Disputes between States and Nationals of other States (the ICSID convention), the Additional Facility Rules of the Centre for Settlement of Investment Disputes (the ICSID Additional Facility), the arbitration rules of the United Nations Commission on International Trade Law (UNCITRAL), or the arbitration rules of the International Chamber of Commerce (ICC).[14]

The ICSID Additional Facility is part of the World Bank Group, and UNCITRAL, as its name suggests, is part of the United Nations.

Under the draft MAI, each signatory would give its "unconditional consent to the submission of a dispute to international arbitration. . . ." However, a signatory could condition this consent on the investor (or investment) that is party to the dispute waiving its right "to initiate any other dispute settlement procedure with respect to the same dispute and withdraw from any such procedure in progress before its conclusion." (This condition is termed "limitation of consent.")

Under the arbitration procedures, a three-person tribunal would be formed to arbitrate the dispute. The parties to the dispute would each appoint one member of the tribunal, and the third, who would preside, would be appointed jointly by the disputants. A roster of persons qualified to be arbiters would be maintained by the MAI signatories, and under most circumstances arbiters would be drawn from this roster. However, if resolution of a dispute required special expertise not possessed by any person on the roster acceptable to the disputants, other persons possessing this expertise could be named to the tribunal.

If two or more disputes submitted for arbitration involving the same signatory have a question of law or fact in common, a tribunal may be established for "consolidated consideration" of all or part of these disputes. Because this tribunal might hear the complaint of more than one investor, the investors must decide jointly whom to appoint to the tribunal and under which set of rules the arbitration shall proceed. If no such agree-

13. In NAFTA, only a party that is strictly an investor of another signatory may institute arbitration procedures against a signatory. Under the MAI, an investment of such an investor (i.e., a subsidiary) may also initiate these procedures. In other words, the standing of enterprises with respect to the enterprise-to-state procedures extends further than in NAFTA.

14. Here the only difference between the MAI and NAFTA is the addition of the ICC option.

ment were reached within a specified time, the proceedings would be conducted under UNCITRAL rules. The tribunal would "assume jurisdiction over all or part of the disputes and the other arbitral proceedings shall be stayed or adjourned, as appropriate if, after considering the views of the parties, it decides that to do so would best serve the fair and efficient resolution of the disputes and that the disputes fall within the scope [of these provisions]." An investor could pull out of the procedure but, in doing so, would forfeit its rights to have the same dispute arbitrated later. The dispute could be resolved by other means, however.

In arbitrating a dispute, the tribunal could call upon expert advice. Third parties (signatories that are not disputants but have an interest in the case are entitled to make their positions known to the tribunal. All decisions of the tribunal must be decided in accordance with the MAI; that is, the MAI is the "applicable law." The tribunal "may recommend an interim measure of protection to preserve the rights of a disputing Contracting Party or to ensure that the tribunal's jurisdiction is made fully effective." A disputant may seek interim relief not involving monetary damages, and this is not deemed to be a submission of the dispute for resolution under which the signatory's limitation of consent (see above) could be invoked. The tribunal could determine that, if a signatory has failed to comply with its obligations under the MAI, a pecuniary award may be granted to the disputing investor. Members of a tribunal and parties to the dispute must protect the confidentiality of information revealed in the course of the proceedings, and this confidentiality must also be preserved in the draft of the final award.

The final award by an arbitral tribunal could consist of any combination of the following:

- a declaration that the signatory in a dispute has failed to comply with its obligations under the MAI;
- pecuniary compensation, including interest accruing from the time that the loss or damage was incurred;
- "restitution in kind in appropriate cases, providing that the Contracting Party may pay pecuniary compensation in lieu thereof where restitution is not practicable"; and
- "with the agreement of the parties to the dispute, any other form of relief."

The state-to-state dispute settlement procedures would be invoked in disputes between or among MAI signatories as to whether an action taken by one signatory is in conformance with its MAI obligations. This could include instances where a signatory has violated an obligation but claimed a national security or public order exception (see below). But as suggested above, if a signatory should fail to abide by the outcome of an arbitral award granted to an investor under the investor-to-state procedures, or if investor-to-state dispute settlement procedures are terminated without resolution by the tribunal arbitrating the investor's claim, state-to-state procedures might also be invoked. In such instances, presumably, the investor's home government would act on its behalf.

The state-to-state procedures laid out in the draft MAI mirror other dispute settlement procedures (including those of the WTO) in that a period of consultation is required prior to invoking the arbitration mechanism. Any MAI signatory may request that another signatory enter into consultations over a dispute regarding interpretation or application of the agreement. The request must be in writing and must "provide sufficient information to understand the basis for the request." The requested signatory must then actually enter into consultations within 30 days. If after 60 days from the date of the request the parties have failed to resolve the dispute, they may seek multilateral consultations with other signatories not involved in the dispute, which then must make a (nonbinding) recommendation within 60 days. Likewise, the disputing parties may, in the event of failure to resolve their dispute through consultations, "have recourse to good offices or to mediation or conciliation under such rules and procedures as they may agree."

However, the draft provides that, should all of these procedures fail to resolve the dispute, arbitration may be invoked. Under this procedure, a tribunal would be established that could then "decide disputes in accordance with this Agreement, interpreted and applied in accordance with the applicable rules of international law." The tribunal could, in the event that it decides that a signatory is indeed in contravention of its obligations, take remedial action, including recommending interim remedial action pending a final decision. The final remedial action might include:

- a declaration that an action of a signatory is in contravention of its MAI obligations;
- a recommendation that a signatory bring its actions into conformity with its MAI obligations;
- pecuniary compensation to the investor for any losses that might be incurred by the investor of the contracting party that requested the arbitration; or
- any other form of relief to which the signatory against whom the dispute is directed might agree.

Other provisions allow the decision of a tribunal to be nullified (e.g., if the tribunal has exceeded its powers or was not properly constituted). However, still other provisions are designed to encourage compliance with a remedial action (e.g., a signatory can be effectively suspended from participation in the agreement in the event of noncompliance, and other limited sanctions can be taken).

The investor-to-state dispute settlement procedures were, as chapter 2 described in some detail, an aspect of the draft agreement to which NGOs objected strenuously. The NGOs claimed that private companies might use the procedures to sue governments for losses claimed by the companies to result from application of environmental and other regulations. Whether this would actually have happened is, of course, an untested issue, but experience with similar provisions in NAFTA would seem to buttress the NGOs' case. Indeed, it could be argued that the dynamic created by these procedures would have been the major means by which the MAI would have had an impact. A series of cases in which panels found violations of core provisions of the MAI not covered by the exceptions might, for instance, have a significant impact on the investment policies of countries that practiced de facto discrimination against foreign investors in favor of incumbent domestic firms.

Exceptions, Safeguards, and Reservations

Article VI of the draft MAI allows a number of general exceptions to the agreement's obligations. In addition, certain temporary safeguards are allowed. The latter are exceptions that may be applied only on a temporary basis, whereas the former are subject to no time limit. And, of course, there would have existed lists of country-specific exceptions to obligations (reservations).

Reservations are covered under Article IX. This article requires that reservations be negotiated at the time of a country's accession to the MAI. In contrast, exceptions apply to all countries, and safeguards are available to all countries, automatically at the time of accession.

General exceptions are allowed for national security and for maintenance of the public order. These exceptions do not apply to the investor protection obligations, however. The national security exception essentially allows a signatory to take measures considered necessary for the "protection of its essential security interests . . . in time of war, or armed conflict, or other emergency in international relations" or "relating to non-proliferation of weapons of mass destruction, or relating to the production of arms and ammunition," even if these would otherwise violate MAI obligations. Also, a signatory is exempt from furnishing or providing access to information where such revelation would be considered contrary to its national security interests. Likewise, signatories may take actions in pursuance of obligations under the UN Charter without violating MAI obligations.

The general exception for public order states that, "subject to the requirement that such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between

Contracting Parties," signatories may take any measure necessary for the maintenance of public order without violating MAI obligations. The ambiguity of this exception is apparent: how, after all, does one define whether a measure ostensibly taken to protect public order is in fact a "means of arbitrary or unjustifiable discrimination"?

Actions or measures taken pursuant to these general exceptions are subject to a notification requirement. This requirement was instituted so that, if one signatory believed that another signatory had taken such actions or measures solely for economic reasons, or that the actions or measures were "not in proportion to the interest being protected," it could initiate state-to-state dispute settlement procedures.

Safeguards in the draft MAI are designed to allow signatories to apply measures inconsistent with MAI obligations regarding transfers, national treatment, or certain other obligations in the event of a balance of payments crisis or other monetary crisis. Such measures must be consistent with the Articles of Agreement of the International Monetary Fund and must "not exceed those necessary to deal with [the crisis]." They must also be reviewed no less frequently than every six months and terminated when circumstances allow. Provisions are also made for determining whether measures invoked by a signatory are in fact consistent with the allowed safeguard. A bracketed provision, however, would disallow the use of this safeguard to delay compensation in the event of an expropriation.

The most important exceptions in the MAI, as already noted, would have been the country-specific reservations. The lists of reservations as submitted were not made public, but reportedly they incorporated virtually all existing laws and policies of the negotiating countries that were inconsistent with obligations established in the draft MAI. However, acceptance of a country's proposed reservations would have been a matter of negotiation, and one reason completion of the MAI was repeatedly delayed was that negotiations over reservations were never really begun in earnest, let alone completed. Whether these negotiations would have resulted in actual liberalization of investment regimes among the negotiating parties is thus unknowable.

As noted earlier, accession to the MAI would have been open to any country (or regional economic integration organization or autonomous customs area) that "possesses full autonomy in the conduct of matters covered by (the MAI) [and] is willing and able to undertake its obligations on terms agreed between it and the Contracting Parties. . . ." The last phrase would include negotiations involving the proposed reservations that would be lodged by the acceding country. Of course, no such negotiations have ever been undertaken, since the MAI has never come into force. One can reasonably conjecture, however, that the main difficulty facing a non-OECD country seeking accession to the MAI would have been in the negotiation of reservations.

The Mouse That Might Have Roared?

If one were to try to characterize the MAI in a single phrase, it might well be "the mouse that might have roared." The agreement was a mouse in the sense that it did virtually nothing to liberalize the international investment policies of the countries that negotiated it, or to remove distortions that reduce the economic value of an investment. But it would have created a new dispute settlement procedure as well as a number of provisions that, applied without reservation, would doubtless have led to liberalization eventually. Given time, the possibility of future rollback of countries' reservations, and the likelihood of disputes being resolved in ways that would force liberalization, there is some probability that the mouse might indeed have roared.

But the draft agreement also contained some very zealous investor and investment protection provisions and established a very broad definition of investment. These might have opened the door to investors to use the agreement's dispute settlement procedures to sue governments for policies and practices that really had very little to do with international investment. Thus, if the MAI was the mouse that might have roared, its roar might not have been an altogether constructive one. In fact, certain interests saw the potential for an undesirable roar as so great that they combined to kill the MAI in its nest. But had the MAI survived, whether its roar might ever have been actually heard is another matter, on which one can only conjecture.