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A Proactive Investment Agenda for 2016

Introduction

An open international trade and investment climate is an essential prerequisite for economic growth worldwide. Despite ambitious work by many governments to foster investment, global foreign direct investment (FDI) has not thus far managed to fully recover since the crisis. Macroeconomic fragility, geopolitical uncertainty, fears of the Euro crisis and a slowdown of growth in major emerging market economies have all had their influence on investment decisions. At the same time, a number of Non-Governmental Organizations (NGOs) remain virulently opposed to discussions on investment agreements, and public misconceptions are widespread and insufficiently addressed. Furthermore, a number of countries in the world increasingly contest the merits of the open international trade and investment climate that was developed with great effort in recent decades.

While Global FDI flows seem to have picked up at the end of 2014, restrictions and opposition to FDI through various forms of investment protectionism still have significant adverse economic consequences for the global economic system overall. Hence, it is necessary to highlight the issue of investment protectionism both at national and international levels. BIAC is convinced that there is a renewed urgency for the OECD to explain and communicate the benefits of foreign investment and to expose and address protectionist actions. In this context, we would like to draw attention to the following areas of concern.

❖ Increasing criticisms towards outward investment

In times of economic uncertainty, there is a considerable risk of countries resorting to protectionist investment measures when addressing FDI. In light of high unemployment in a number of countries, concerns are increasingly being expressed that outward FDI can lead to job exports and a weakening of the domestic industrial base. However, these concerns reflect a fundamental misunderstanding of the benefits of both inward and outward investments as they contribute to companies' overall competitiveness and thus the economic well-being of a country's economy and its citizens. Inward and outward investments are inextricably and increasingly linked in global value chains.

Global investments enhance the competitiveness of multinational parent companies by allowing them to improve efficiency and better serve foreign markets. Further, they can complement important parent activities, such as exports. These findings suggest that the labor market impact of reduced export of goods and services produced domestically is more than offset by a positive scale effect due to improved competitiveness and better market access abroad. The ability of companies to make a positive contribution in their home economy is enhanced, not reduced, by companies' global engagement.

We encourage the OECD to contribute to a more balanced understanding, especially by politicians and other opinion leaders, of the effects of outward investment in home countries and to highlight the benefits at high political level.

❖ Global value chains

Trade and investment are inextricably linked, in particular in light of global value chains (GVC) where the different stages of the production process are located across different countries. Notwithstanding existing international commitments by governments, restrictions that affect trade and investment continue to be introduced in ways that are difficult to combat and reduce the potential of GVCs.

GVCs are essential to the growth of businesses and economies. They provide access to networks, global markets, capital, best practices, and technology. They enhance trade, productivity, and create jobs. In order for the private sector to thrive, reforms are needed that increase the competitiveness of domestic industries to engage in global value chains and liberalize markets for trade and investment. Good knowledge about the significance of global value chains is vital for informed policy decisions concerning trade and investment.

BIAC calls upon the OECD to continue work in this area to enable companies to participate in GVCs and identify opportunities for moving toward a new era of trade and investment liberalization.

❖ Forced localization requirements

Industry is increasingly concerned with forced localization requirements that companies are facing around the world. The issue of forced localization can take various forms as there are a variety of ways to force foreign companies to invest, procure, export from, or otherwise locate economic activity in those foreign jurisdictions. Such practice of forced localization has been exacerbated with the global economic downturn. Companies naturally source and invest for economic and societal reasons, but forcing companies to do so when there is no sound argumentation is distortive and anti-competitive, and thus ultimately limiting to economic growth and development. Furthermore, as is the case with other forms of protectionism, forced localization in one country encourages the spread of forced localization to other countries, to the detriment of global commerce and domestic economies alike.

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

❖ Investment and cloud computing

One concern for investors relates to data localization, servers and information requirements. Increasingly, global businesses are taking advantage of technology to localize data storage in an attempt to remain competitive in the market. At the same time, more and more governments are proposing new legislation and data localization requirements based on privacy or national security considerations that may have the potential to restrict investor's choice in data localization, thus raising costs and reducing agility, integration, responsiveness and competitiveness for global companies.

Work on the issue of cross-border data flows as well as monitoring of the Recommendation on Digital Security Risk Management for Economic Social Prosperity should be based on fact-based analysis of policy concerns expressed by governments and the legitimate interests of business.

❖ Investment screening and national security

Investment screening for the purpose of national security is legitimate and "essential security" provisions have long been found in many trade and investment agreements. However, broad and sweeping definitions of national security can provide governments with the possibility to block investment to serve protectionist measures. While protecting national security must be a top priority for governments, it is also important to keep in mind the negative impact of overly expansive or vague investment screening procedures on cross-border investment, growth and job creation. Rules should not be tightened for national security reasons without seriously exploring all possible alternative measures.

The legitimate concerns about protection of national security should not be used to introduce disguised protectionism. In times of economic uncertainty, there is a considerable risk of countries resorting to protectionist investment measures when addressing FDI and referring to "national security" in an increasingly politicized context. It is important to bear in mind that most foreign investments do not raise real national security concerns and that justified concerns often can be effectively addressed through measures that are not protectionist in nature.

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

❖ Bilateral Investment Treaties

The international investment landscape is constantly evolving. In the – regrettable – absence of a multilateral investment framework, it consists of a vast network of more than 3000 bilateral and regional investment agreements, as well as investment chapters included in free trade agreements (FTAs). The EU's exclusive competence on foreign direct investment, a recent development from the Lisbon Treaty, may lead to a streamlining of bilateral investment treaties (BITs) between EU countries and third countries. Mega-regional agreements that are currently being discussed are a key priority on the global trade and investment agenda and have increasingly attracted public attention.

As the volume of international investment flows rises and the variety of investment instruments expands, BITs continue to play a key role. Investors must be able to mitigate growing risks if potential FDI flows which are essential to economic growth, development, and jobs, are to be realized. BITs remain an important tool for attracting and protecting international investment and by guaranteeing equitable national treatment of foreign investors in accordance with international standards. They are therefore a crucial instrument and an important element in international investment decisions by companies.

Unfortunately, BITs have been subject to politically motivated criticism from some policy makers and NGOs, who allege without solid factual underpinning that they are mainly designed to protect foreign investors and do not sufficiently take into account obligations and standards to protect the environment, human rights, labor rights and social provision. However, such statements are to a large extent based on misconception without sufficient proof and without taking into account the real nature of BITs, which aim to extend the rule-of-law also to foreign investors and avoid discriminatory treatment of foreign investments. Recent developments, where countries such as South Africa and Indonesia have decided to put an end to a number of BITs are particularly worrying.

We encourage the OECD to carry out fact-based analysis of the role of BITs to create an open investment climate while providing protection for investments in uncertain environments, and to objectively analyze criticism that has been put forward.

❖ Investor-State Dispute Settlement

Open, transparent, and non-discriminatory investment policies and agreements, ensuring a predictable and fair treatment of investors and protecting investors against arbitrary behavior of host states are essential to stimulate investment. In this context, Investor-State Dispute Settlement (ISDS) provides a neutral and high-quality mechanism of legal dispute resolution in cases of breaches of investment treaties by host states, which makes effective the substantive protections offered by investment treaties between home and host states. It provides investors with a fair and unbiased instrument to invoke international public law commitments, which states have made to each other with a view to protecting investors. It is a fundamental part of the rule of law and all the more important in cases where the independence of local judiciary is not guaranteed.

In light of the current widespread and heated debate putting the ISDS system as such into question, BIAC believes that it is crucial that the discussion is put back in the right perspective and that common misrepresentations are effectively addressed. In 2015, BIAC issued a paper on ISDS, highlighting specific areas where the OECD can make an important contribution.

We encourage the OECD to provide objective analysis to inform national and international discussions on ISDS. Recognizing that there are different approaches in place, the OECD can also help spread best practices.

❖ Conflicting requirements and extraterritorial effects

OECD member countries adopted the *Declaration on International Investment and Multinational Enterprises* in 1976, with the aim of avoiding or minimizing the imposition of conflicting requirements on multinational enterprises by governments. The Declaration consists of four elements: (1) National Treatment, (2) Conflicting requirements, (3) International investment incentives and disincentives and (4) the Guidelines for Multinational Enterprises.

The recommendation on conflicting requirements is rarely given much visibility and often overlooked in practice. However, a significant rise in the use of extraterritorial jurisdiction as well as application of conflicting rules are burdensome to multinational activity and hence, pose a serious obstacle to international investment. It raises concerns for the international business community because the exercise of direct extraterritorial jurisdiction, in particular, may create a tilted playing field as well as increase the risk of litigation and transaction costs.

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

❖ Investment for Development

Private sector development is an essential source of financing strong, sustainable and inclusive development in developing countries, as flows of official development assistance (ODA) have been decreasing in absolute and relative terms in recent years. At the same time, it is important to explore how to increase the synergy between FDI and ODA, to make aid leverage private investment for development. This is also relevant for developing countries seeking to strengthen the resilience of their infrastructures to better manage the impact of possible natural disasters.

More broadly, private investment requires an enabling environment for businesses of all sizes to grow and compete. The OECD Policy Framework for Investment (PFI), which was updated in 2015 with the active participation of BIAC, is an international reference document for investment promotion agencies and donors. It provides a comprehensive and systematic approach for governments to implement policies for a robust and competitive environment for domestic and foreign investment and has been widely used since 2006 for country-specific investment policy reviews of emerging and developing economies.

In the context of the post-2015 development agenda, and building on the progress made at the International Conference on Financing for Development in Addis Ababa in July 2015, the focus now needs to be on implementation of the PFI in both developed and developing countries alike, in order to achieve the full potential of the Sustainable Development Goals.

BIAC encourages the OECD to make the implementation of the PFI for both member and non-member countries a cornerstone of its work on investment and development.

❖ Clear, stable and predictable tax frameworks for promoting investment

An important element of an investment environment is the framework for taxation. Clear, stable, transparent tax policies and tax administrations that do not impede investment are critical to support investment. OECD tax instruments such as the OECD Model Tax Convention and the OECD Transfer Pricing Guidelines are important underpinnings of global FDI. Tax policy is also a key factor in domestic resource mobilization supporting economic development. The OECD with its expertise in both taxation and investment should ensure that tax policies are not used for protectionist purposes, hampering cross-border trade and investment.

In response to legitimate public concerns, the BEPS project continues to change the international tax landscape. BIAC has always accepted the need for measured change, but great care is required if we are to radically change tax principles that have served to enhance global growth and jobs over the past 50 years. We must continue to look at the complete range of issues holistically, rather than focussing on just one small piece of the puzzle to ensure successful and coherent policy development. BIAC has been supportive of the BEPS project since its inception, and intends to continue to engage in a constructive, flexible and incremental way as the best way of achieving its success.

At the September 2015 B20 Conference in Ankara, the B20 policy proposals for the G20, among others, suggested the development of a common set of international investment principles and the promotion of greater transparency and harmony in taxation related to FDI, giving more attention to the discussions on BEPS and its impact on debt and interest deductibility on cross-border infrastructure investment.

BIAC recommends that OECD work on taxation be coordinated with OECD work on freedom for investment where relevant, and work to ensure that tax policies do not overtly or inadvertently lead to protectionism, but rather do support growth and development.

❖ Competitive neutrality and state-owned enterprises

Ensuring “competitive neutrality” is an increasingly important issue for the OECD business community. BIAC has therefore repeatedly expressed its strong support for an ambitious work program in this area, bringing together the expertise of different OECD committees. The 2014 OECD Council Meeting at Ministerial Level initiated a discussion on “Levelling the International Playing Field between Public and Private Business,” resulting in a multidisciplinary work program on State-Owned Enterprises in the Global Market Place.

As much of global growth is taking place in emerging markets, activities should not be limited to OECD countries. The OECD can make an important contribution by providing a deeper understanding of the challenges and opportunities, while fostering capacity building by sharing its analysis and engaging in a constructive dialogue with emerging economies. The fact that the SOE landscape is heterogeneous and the recent trend towards increased international investment by SOEs underline the importance of further OECD work in this area. This could include, for example, an inventory of state aid practices and an analysis of their effects on investment, detailing financial, non-financial advantages which accrue to SOEs. Due consideration should be given to the linkages between investment protection, liberalization and competitive neutrality.

BIAC encourages the Investment Committee to contribute to an evidence-based work program on competitive neutrality to complement work carried out by other parts of the Organization.

❖ Responsible business conduct and investment

Recent investment treaties regularly address responsible business conduct and sustainable development. Business recognizes that there is a link between investment and responsible business conduct. This link is also illustrated by the OECD Declaration on International Investment and Multinational Enterprises (MNEs), which consists of four pillars: national treatment, international investment incentives and disincentives, conflicting requirements, and the MNE Guidelines. On the one hand, the Declaration commits adhering countries to improve the investment climate. On the other hand, companies are encouraged to apply the standards of responsible business conduct as elaborated in the MNE Guidelines.

At the 2015 OECD Ministerial Council Meeting, Ministers reaffirmed the importance of the OECD Declaration on International Investment and of non-members adhering to it. They also encouraged efforts to widen adherence to the MNE Guidelines and invited OECD to study options in this regard. Based on a first discussion at the March 2015 Investment Committee, BIAC underlined a number of strategic issues that have to be taken into account in further discussions.

BIAC encourages the OECD to discuss the link between investment and responsible business conduct in a balanced manner and to closely involve business in discussions regarding implementation of the four parts of the 1976 OECD Declaration.

❖ Long Term Investment

Long-term investment, such as in infrastructure, energy, education, R&D, housing and business expansion, is a crucial driver to foster economic growth. However, the widespread economic uncertainty since the 2008-09 global economic crisis, coupled with bank deleveraging in response to new regulations, have reduced the ability of the financial system to efficiently secure the supply of long-term finance in order to meet countries' investment needs.

BIAC therefore appreciates the *G20/OECD High Level Principles of Long-term Investment Financing by Institutional Investors,* to which BIAC actively contributed in 2013. Recognizing the OECD's role in leading international policy analysis and standard-setting on the role of institutional investors in long-term investment, the 2013 G20/OECD Principles contribute to greater international policy consistency for institutional investors worldwide. Along the same line, BIAC is involved in the consultative review process of the new *Core Principles of Private Pensions Regulation* whose purpose also includes harmonizing private pension regulation with several long-term investment tools such as the *G20/OECD High Level Principles of Long-term Investment Financing by Institutional Investors* as well as several others.

BIAC encourages future OECD work to examine the potential impacts and cumulative effects of policy and regulatory approaches – both domestically and across borders – through the nexus of financial stability, economic growth, and return on investment. This future work should include clear cost benefit and impact assessments of any new international regulatory standards which potentially would negatively impact long term investment.

❖ OECD data and analysis

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

Further, we are witnessing a number of trends that are reshaping international investment patterns. For example, emerging markets have become increasingly important sources of international investment, and international investment by SOEs has been growing rapidly. There is a growing dialogue of cross-sectoral exchanges across national borders towards achieving sustainable economic development.

In the evolving global landscape for international investment, it remains inevitable to develop improved data and empirical analysis of emerging new trends to support policy discussions.

A clear role for the OECD

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

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

BIAC believes that it is a core element of the OECD's mission to play a leading role in the international debate on freedom of cross-border investment and to provide leadership to shape further understanding about the issues that are at stake. We urge the OECD to embark on an ambitious pro-active investment program and confirm the Organization's leading role in ensuring that markets are kept open for foreign investment, with a view to boost economic growth and foster job creation.

BIAC encourages the OECD's Investment Committee to continue its practice of including major non-member economies in its Freedom of Investment Roundtable and other appropriate discussions and subsidiary bodies. Foreign direct investment policy issues are not limited to OECD member economies. The OECD should continue to be a place where global FDI issues can be studied, discussed, and advanced.

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