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CONTENTS

BIOGRAPHICAL NOTE

David Henderson, who is British, was formerly Head of the Economics and Statistics Department of the Organisation for Economic Cooperation and Development (the OECD) in Paris. Before this, he had worked as an academic (first in Oxford University, and later in University College, London); as a British civil servant (first in HM Treasury, and later in the Ministry of Aviation); and as a staff member of the World Bank where at one time he was Director of the Economics Department. Since leaving the OECD he has been an independent author and consultant, and has acted as visiting fellow or professor at institutions in Britain, France, Belgium, Australia and New Zealand. In 1985 he gave the BBC Reith Lectures, which were published in book form under the title *Innocence and Design: The Influence of Economic Ideas on Policy*. Among his recent publications is *The Changing Fortunes of Economic Liberalism*, published in London by the Institute of Economic Affairs, and in Melbourne by the Institute of Public Affairs and the New Zealand Business Roundtable. He is an Honorary Fellow of Lincoln College, Oxford, and in 1992 he was made Commander of the Order of St Michael and St George.

AUTHOR'S PREFACE

The work for this paper was done successively in Paris, at the Groupe d'Economie Mondiale directed by Professor Patrick Messerlin at the Fondation Nationale des Sciences Politiques; in Melbourne, at the Centre for the Practice of International Trade directed by Professor David Robertson at the Melbourne Business School where Professor John Rose is Director; and in Wellington, at the New Zealand Business Roundtable where Roger Kerr is Executive Director. My thanks are due to all three institutions and the respective directors for the facilities, financial help and encouragement they provided. I am grateful also to Dr Brigitte Granville, Director of the International Economics Programme at the Royal Institute of International Affairs (Chatham House) in London, for publishing the study as part of her programme. I would like to acknowledge the helpful comments on my draft text of Dr Granville, Professors Messerlin and Robertson, Professor Jim Gillespie and Dr Bryce Wilkinson. Last, it is a pleasure to thank the various officials, both in the OECD Secretariat and in national administrations, who went out of their way to provide information, ideas and suggestions. The opinions that I express in the paper, and the responsibility for errors that may remain despite the commentators, are mine alone.

EXECUTIVE SUMMARY

Theme

The subject of this paper is a failed venture in international economic cooperation, the Multilateral Agreement on Investment (MAI). I consider the reasons for the failure and its wider implications.

Negotiations to draw up the MAI were launched within the Organisation for Economic Cooperation and Development (OECD) by its member governments in the early part of 1995. They came to an end, without result, towards the close of 1998. There is no prospect that they will be renewed.

The purpose of the MAI was to promote the further freeing of international flows of private foreign direct investment (FDI). To this end, it would have placed additional limits on the freedom of signatory governments to impose or maintain restrictions on such flows. It was to have been an instrument of liberalisation.

Background and context

As such, it would have codified and reinforced established policies. OECD member governments have a long record of progressively freeing cross-border capital flows. By the early 1990s, all of them had done away with exchange controls. In recent years, they have further reduced restrictions on inward FDI, chiefly through unilateral actions and within regional integration agreements such as the European Community's Single Market and the North American Free Trade Agreement.

Liberalisation of capital flows generally, and FDI in particular, has likewise been going ahead in non-OECD countries. Attitudes towards inward FDI have become much more positive in a growing number of developing countries, while since 1989 many of the former communist countries have likewise become open to such investment. For both groups, this is reflected in the large and still-growing number of bilateral investment treaties which are designed to clarify and secure the rights of foreign investors.

As a result of both policy changes and market-related developments, FDI flows have been growing in recent years considerably faster than world trade, which in turn has continued to increase in relation to world output. One contributory factor has been privatisation, which all over the world has opened up new possibilities for FDI.

Before the MAI was launched, external liberalisation across the world had in general been carried forward without arousing serious political opposition. Though it was not a popular cause, its results had been broadly accepted.

Ever since the creation of the OECD in 1961, its members had used it as a venue for promoting liberalisation of international capital flows, in particular through the Codes of Liberalisation and the National Treatment instrument. It was natural to think of the

Organisation as the venue for further negotiations in this area, the more so since there was no possibility, in the mid-1990s, that agreement could be reached to initiate such a process in the World Trade Organization (WTO).

The prospective signatories of the MAI were the OECD member governments, which have now reached 29 in number. However, the negotiations were opened up to non-member governments that wished to take part. Eight of these eventually participated, including Argentina, Brazil and Chile.

Contrary to what has been alleged, the possibility that such negotiations would take place in the OECD, as also the decision to launch them, were entirely public. Although it can now be seen that a wider process of publicity and consultation would have been advisable, neither the governments concerned nor the OECD engaged in concealment at any stage.

The MAI negotiations were entered into after full consideration by member governments, and apparently with good prospects of success.

Course of events

Two interrelated factors led to the abandonment of the MAI.

First, it gradually became clear that member governments would find it difficult to reach agreement: the range of topics for negotiation proved too wide, and the initial goals too ambitious. Governments were unready to allow their hands to be tied in the ways that had been originally sketched out, nor were they able to find a basis for compromises where disagreements emerged. Increasingly, negotiators thought and argued in defensive terms. In the latter stages of the negotiations, an issue which remained unresolved was whether and in what way to introduce into the MAI provisions designed to safeguard environmental and social standards.

Second, a wave of public opposition developed in a growing number of countries. This was led by non-governmental organisations (NGOs), linked through the Internet in what became an internationally orchestrated campaign. The NGOs comprised a wide range of interests and concerns, and despite some differences of view they were united in their hostility to the agreement. Their efforts made the MAI into a prominent and sensitive political issue. As such, it was taken up by commentators and parliamentarians, who in most cases were likewise hostile (and in some cases ill-informed). The agreement emerged as a potential vote-loser.

As negotiations went on, support for the MAI began to erode. On the one hand, it increasingly appeared to its original supporters, in both official and business circles, that agreement could only be reached on a watered down document that would bring no more than modest advances towards liberalisation. At the same time, the extent of opposition surprised and disconcerted political leaders. It led them to question a commitment, and a process, which in the earlier stages they had barely noticed.

At the OECD Ministerial Council meeting of May 1998, ministers decided on a six-month pause in the negotiations. During this period, following the report of a specially appointed commission of inquiry, the government of France announced that it would take no further part in the negotiations. From then on the MAI was doomed, though what were in effect the final obsequies were not pronounced until December 1998.

State of the debate

The MAI affair has reopened debates on the pros and cons of FDI, though with unimpressive results. On the OECD side, some weak or questionable arguments are now advanced in favour of liberalisation. From the side of the NGOs, the significance of the agreement was greatly overstated, while their opposition to FDI flows as such is often based on the delusion that the world today is increasingly run by multinational companies which represent a threat to national sovereignty and democratic freedoms. It was also maintained, by NGOs and some others, that the MAI would bestow new rights on multinationals without imposing the matching obligations that should go with them: this argument too is not well founded.

An obvious rationale for an agreement such as the MAI, and for the whole process of external liberalisation that has gone ahead across most of the world, is that it reduces the extent of discrimination between the residents of different countries. Here as elsewhere, the aim is to promote closer international economic integration, as a means of increasing both economic freedom and prosperity. From this standpoint, domestic and foreign investors are to be treated alike, with no special favours for the latter. The underlying philosophy is that of economic liberalism.

As against this approach, many critics have argued, both in relation to the MAI and more generally, that it is in the public interest for governments to retain a wide range of discretionary powers, including powers to discriminate between domestic and foreign investors and different investment projects or programmes. Here the NGOs are joined by many others – in governments, business circles, and a wider public. In some cases at least, the critics take too little account of the evidence against discretionary policies.

There is likewise a powerful coalition, official and non-official, in favour of defining and enforcing internationally agreed minimum standards relating to the environment and to terms and conditions of employment. From a liberal standpoint, however, it is not necessarily the case that 'higher' standards imposed by fiat are to be preferred to 'lower', while mandated uniformity is liable to be a force for disintegration. Hence the tendency to favour the further tightening and extension of environmental and 'social' regulation, which was taken still further in the MAI debate, is not a sign of progress.

A feature of the debate was that the opposition made virtually all the running. Despite their many weaknesses and exaggerations, the hostile arguments were not forcefully countered. Governments, businesses and independent commentators alike failed to present the liberal case effectively.

Significance of the failure

In itself, the MAI episode is not to be seen as a landmark event. It was an attempt to accelerate the process of liberalisation in one area of international transactions in one particular venue of negotiations. Within OECD governments, the factors that made agreement hard to achieve were not new: there has been no change of heart. For governments everywhere, the probability is that the recent trend towards enlarging the scope for inward FDI will be maintained, in part through other international agreements.

For the time being, multilateral negotiations relating to rules for investment are unlikely to go ahead, though it is possible that the subject will form part of the formal agreed agenda for the new 'Millennium Round' of trade negotiations, if this is launched at the WTO Ministerial Meeting in Seattle in November 1999. For the time being at any rate, it is likely that a continuing trend towards more liberal investment regimes will mainly take effect in other ways than through the WTO.

For this next stage in the evolution of policies towards FDI, a clear responsibility falls on the OECD member countries, including especially the European Community and the United States. They need to make progress with some of the leading issues that remained unresolved in the MAI process.

This is not only a matter of further negotiations. There is a place also for reviews, discussions, studies and inquiries outside the context of negotiations, and for these in particular the OECD remains well suited. Its activities in relation to FDI issues should be further developed; and here as more generally, the continuing aim should to be to involve non-member countries in the work of the Organisation. These countries, if they so wish, should now be admitted to membership of the OECD Codes of Liberalisation.

On investment and other issues, the OECD should work more closely with the WTO. At the same time, and as the MAI affair itself suggests, the internal working of the Organisation needs to be made more coherent and effective, in ways that involve both national delegates and the Secretariat.

The conduct of business in international economic relations

The MAI episode has raised in an acute form the question of how international discussions, consultations and negotiations are best conducted, and what should be the role within them of the NGOs, as also of organisations representing businesses and trade unions. The present tendency of many governments is to endorse the case for wider public participation. In some official quarters, the argument has even been made that representatives of 'civil society' should have the right to take part in international negotiations.

This latter notion is misguided. Contrary to what is sometimes assumed, the NGOs are not authentic representatives of 'civil society' as a whole. In any case, the notion that 'civil society' has claims of its own to speak for the people of a country has no basis when that country has a democratically elected and responsible government. Persons who are neither elected nor politically accountable can have no such status.

In considering the claims to participation by non-governmental organisations generally, including those representing business or unions, a dividing line has to be drawn. On one side of the line, these organisations, when their credentials and representative status hold good, have valid claims to being kept well informed, and to being consulted and brought into discussions. On the other side, no such organisation has a valid claim in its own right to participate actively in proceedings where the responsibility for decisions and outcomes rests with the governments of national sovereign states. The conduct of substantive discussions, and still more of negotiations, should remain with elected political leaders, and with those who are appointed to serve and act for them in national and international agencies.

It is in this sphere of procedures and demands for recognition that the MAI episode, when otherwise long forgotten, may prove to have had lasting and unfortunate consequences. Just as anti-liberal arguments have gone largely unanswered, so the excessive claims made on behalf of 'civil society' have in many cases been met by agencies and governments with a surprising degree of acquiescence or even support.

Moral of the story

The MAI initiative came to nothing because it became politically unviable. The circumstances of the failure mean that new moves towards freer international trade and investment are likely to meet with more opposition than in the past. Hence the ground has to be prepared better, politically as well as technically, than it was in this instance. Political leaders have to be well briefed in advance, and persuaded of the case. Governments need to be more explicit, and more visibly open, both to make themselves better informed and to avoid damaging charges of secrecy. Effective procedures for consultation and discussion need to be developed, while at the same time the integrity of the negotiating process has to be maintained. Both within and outside government, the case for a liberal approach has to be made more effectively. All these could be useful lessons, and eventual outcomes, of a venture that failed.

1

INTRODUCTION

My subject here is a failed venture in international economic cooperation. The venture in question is the recent unsuccessful attempt by the member countries of the Organisation for Economic Cooperation and Development (OECD) to establish a new instrument of cooperation – the MAI, or Multilateral Agreement on Investment. My object is to place this episode in perspective, looking at the future as well as the past.

The MAI began as a little-noticed initiative, to all appearance limited in scope and unlikely to stir up controversy. Its unexpected misfortunes, and eventual failure, are of interest not only in themselves: they also raise fundamental questions concerning the basis, direction and conduct of international economic policies.

The episode outlined

The main story opens in Paris in the early part of 1995. Every year, the Council of the OECD meets at ministerial level and, among other things, the ministers concerned then take decisions on the future agenda for the Organisation and give directions accordingly. Among the documents prepared for the 1995 meeting was a joint report from two of the many OECD committees, the Committee on International Investment and Multinational Enterprises (CIME) and the Committee on Capital Movements and Invisible Transactions (CMIT). The report was entitled *A Multilateral Agreement on Investment*. It opened with an assertion that the time was ripe for arriving at an agreement of this kind in the OECD, adding that the two committees

> are convinced that the foundations have now been laid for the successful negotiation of such an agreement building on OECD's existing instruments and expertise.[1]

In the light of subsequent events, these confident opening sentences now read ironically.

As expected, the Ministerial Council accepted this view of the situation, and in the communiqué issued at the end of the meeting the Negotiating Group, already constituted by the two committees, were given the mandate which they had asked for. They were instructed to proceed with the negotiation of an agreement which would:

> provide a broad multilateral framework for international investment with high standards for the liberalisation of investment régimes and investment protection and with effective dispute settlement procedures;

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1 OECD, *A Multilateral Agreement on Investment: Report by the Committee on International Investment and Multinational Enterprises (CIME) and the Committee on Capital Movements and Invisible Transactions (CMIT)*, Paris, 1995.

> be a free-standing international treaty open to all OECD Members and the European Communities, and to accession by non-OECD Member countries.[2]

It was specified in the communiqué, again in conformity with the recommendations of the two committees, that the objective should be to reach an agreement by the time of the OECD ministerial meeting of 1997. Hence a period of two years was envisaged, from the opening of the negotiations to their expected fruitful outcome in the form of a new international treaty.

In the event, these official hopes were dashed. In December 1998, more than three-and-one-half years later, the negotiating process, already stalled, was brought to an inglorious end. An OECD press release of 3 December, following what was described as 'an informal consultation among senior officials responsible for investment policy', conveyed the stark news: 'Negotiations on the MAI are no longer taking place'. Although officials will now have submitted a report to member governments in the context of this year's OECD ministerial meeting, and such a report is likely to have included proposals for some kind of further cooperative action, the MAI project, while not as yet officially terminated, appears beyond revival. A brief well-defined chapter in the history of international affairs, and of intergovernmental economic cooperation, has now been closed.

Sequence and approach

Here I offer a summary account and interpretation of the negotiations themselves, in which, however, they are set in context. The MAI affair is not just a self-contained episode. Both its origins and its possible lessons and implications are best seen in relation to the larger continuing story of the evolution, recent and prospective, of the external economic policies of national states across the world. On this larger canvas, non-OECD governments appear, as well the Organisation's member countries; all cross-border transactions are included, and not just the flows of foreign direct investment (FDI) which formed the subject-matter of the MAI negotiations; and a much longer time-perspective is involved.

As to the origins of the MAI, the notion of taking further 'the liberalisation of investment régimes', along the lines approved by ministers in 1995, was not at all new or surprising, and it had been thoroughly examined within the two committees before the decision was taken to go ahead. An international agreement of this kind could be seen, and was seen, as a natural extension of the OECD's work and role; and it appeared as timely and appropriate in view of the continuing rapid increase across the world in FDI flows and the proliferation of smaller agreements relating to them. More broadly, as an exercise in the further liberalisation of cross-border transactions in general, the MAI proposal gave expression to beliefs and trends which were dominant in the OECD countries and increasingly prevalent in the rest of the world: in this wider perspective also, its logic seemed evident. Within an even more extended time-frame these beliefs and trends themselves, as well as the MAI episode, can be seen as forming part of a world-wide and long-continuing story which goes back some two-and-one-half centuries – the story

2 OECD, Ministerial Communiqué, May 1995.

of the changing fortunes of economic liberalism. From roughly the end of the 1970s, in a growing number of countries across the world, these fortunes substantially improved.[3]

This background to the MAI is relevant, not just for an understanding of the episode itself and its significance, but also in weighing future possibilities. Although the MAI as such is dead, the circumstances which gave rise to it, and which made it appear to governments as a promising venture, have not gone away. As will be seen, they continue to bear on the prospects for further liberalisation of cross-border transactions, including flows of FDI; on the influences at work in this connection, both in the OECD countries and more generally; and on the scope for, and the mechanisms of, international economic cooperation. But these prospects now have to be viewed in the light of the MAI episode itself, which forms a point of departure for the next stage in the evolution of external economic policies.

My treatment here is broadly chronological. It comprises four main sections, of which two look back and two look forward. Section 2 sketches out the world-wide historical sequence, of events and ideas alike, from which the launching of the MAI negotiations was perceived, within the small circle of those who were directly involved, to be a natural and clearly achievable next step. In Section 3 I summarise the course of the actual negotiations, and outline what I see as the reasons for their failure and ultimate abandonment. Section 4 revisits, in the light of the MAI debates, the arguments for and against the freeing of cross-border investment flows. Here I question the way in which the OECD case is currently presented, offer an alternative 'liberal' rationale for policies, and give reasons for rejecting or doubting views that many critics of the MAI have advanced. I also touch on the question of international norms and standards relating to the environment and labour. Section 5 looks at the post-MAI future. I consider the significance of the MAI episode; the likely direction of policies with respect to FDI flows; and the scope for further international cooperation in this area, not just through negotiations but more generally, and hence the roles of the OECD and the World Trade Organization (WTO). In connection with the OECD, I offer my own suggested draft text for the relevant (MAI-related) paragraphs of the official communiqué to be issued after the meeting of the OECD Ministerial Council, on 26–27 May 1999. I then consider issues relating to the conduct of discussions and negotiations, in the light of experience with the MAI and the claims now made on behalf of 'civil society': here also, a draft communiqué paragraph is offered. I end with a few reflections on the political lessons of the MAI. The Annex gives background information about two aspects of the role of the OECD in relation to the subject-matter of the paper.

Although the issues are world-wide and my treatment is general, I have commented in particular on the evolution of policy with respect to FDI flows in Australia and France. This is partly because the paper is being published in both countries; but in any case, developments there are worth noting both as illustrations and for their own sake. Those

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[3] This latest chapter of the story, comprising the evolution of economic policies over the past two decades, forms the subject of my recently published study: David Henderson, *The Changing Fortunes of Economic Liberalism: Yesterday, Today and Tomorrow*, London, Institute of Economic Affairs, 1998. Now and then, I have drawn on this study below without specific attribution.

in France are of special interest, because of the strong opposition to the MAI that was evinced by the present government of Lionel Jospin. The French withdrawal from the MAI negotiations was the main precipitating factor in bringing them to an unexpectedly early end.

Despite its mainly historical content, the paper is oriented towards the future. This accounts for its format and timing. My aim is to explore and throw light on the main MAI-related issues, and to place them in today's context, rather than attempting an investigation in depth. Clearly, it is too soon to write an informed account of the negotiations: the full evidence is not yet available, and at this stage an outsider, with no scope for conducting a wide range of interviews, cannot hope to do justice to the facts. But it is not too soon, even for outsiders, to attempt an interim assessment of these events and their possible wider implications. In making such an attempt, this paper is designed as input for a continuing debate which, following the demise of the MAI, has now entered a new phase.

2

BACKGROUND AND CONTEXT

The decision to launch the negotiations in 1995, and the expectation of those directly involved that they would succeed, have to be seen in the context of four tendencies, four related sets of circumstances, which seemed to provide a clear basis for going ahead. These were:

- The strikingly rapid growth and spread of FDI flows
- The long-established OECD role in relation to (i) the liberalisation by member countries of trade in services and international capital flows and (ii) the conduct of governments in relation to foreign-owned firms established within their borders
- The trend towards more liberal external economic policies, which extended to capital flows (including FDI) as well as trade, and which gathered momentum across the world from about the end of the 1970s
- The widespread public acceptance of this trend, and hence of more liberal trade and investment régimes.

The growth of foreign direct investment

Over the past half-century, as in the century or so leading up to the First World War, the volume of world trade has grown faster than world output: in this sense, 'globalisation' is a long-established phenomenon, still to be seen today. In recent years, however, it is not so much the growth of trade as that of FDI flows that has been especially notable. Over the decade 1986-96, for example, world output increased in round terms by 40 per cent, while the volume of world trade approximately doubled; but the corresponding estimate for FDI, which relates to inflows in real terms, suggests that they rose over the same period by a factor of more than four and one-half.[4]

Two mutually reinforcing influences have been at work here. A strong impulse to cross-border links and operations on the part of businesses has come from developments – in products, markets and (especially) communications and management systems – which have increased the advantages of operating globally. The second and probably dominant factor has been the evolution of official policies, which is summarised below.

As a result of this remarkable growth in FDI flows, there has been an increasing focus on the national policies that bear on them, the ways in which policy régimes interact, and the scope for international cooperation and agreements on investment-related issues.

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4 Figures for the growth of world output and trade are derived from International Monetary Fund (IMF) sources, while for FDI flows the estimate comes from the United Nations Conference on Trade and Development (UNCTAD) *World Investment Report for 1997*, p 269.

In this, it was natural to consider the possibility of fashioning a multilateral system of rules and disciplines relating to cross-border investment flows, which would complement the system that had been developed for international trade flows within the General Agreement on Tariffs and Trade (GATT) and the WTO which succeeded it. Hence the notion of a multilateral agreement on investment was in the air.

The OECD's role in liberalisation

In large part, the MAI project was based on the positive experience of intergovernmental cooperation in this general area, over a period of almost four decades, within the OECD. From its earliest days, member governments have used the Organisation as a mechanism for systematically reducing the extent of their restrictions on international capital flows of all kinds, as also on trade in services.[5] For this purpose, they agreed on, and put into effect, a set of rules and disciplines together with procedures for reviewing, interpreting, and extending these. Hence the proposed new Agreement was seen, with good reason, as a continuation and extension of a process already well established.

A central feature of this process has been, and remains, the two OECD Codes – the Code of Liberalisation of Capital Movements and the Code of Liberalisation of Invisible Transactions. These are legally binding instruments, the oversight and further development of which is the responsibility of one of the already mentioned committees, the CMIT. All member governments are subject to the obligations of the Codes, and adherence to them has been made a condition of accession for the new members that have been admitted to the Organisation over the past five years.[6]

Flanking the Codes, and dealing more specifically with the status and rights of foreign-owned enterprises that are established within member countries, is the 1976 Declaration on International Investment and Multinational Enterprises. In this, a leading element is the National Treatment instrument, by which member governments bind themselves – though unlike the Codes, no legal obligation is involved – to accord to foreign enterprises already established within their borders terms no less favourable than those accorded in like situations to domestic enterprises. Here the responsibility for oversight lies with the sister committee, the CIME.

Had it come to pass, the MAI would have superseded the Codes and the Declaration. Its demise leaves them still in operation. Hence they are of interest, not just for historical reasons, as the starting point for an unsuccessful venture, but also as a possible basis for cooperative action in the future. For this reason, I have summarised their provisions and history in the Annex. Here four general points are worth making.

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5 This aspect of the Organisation is reviewed, in the context of its activities as a whole, in David Henderson, 'The Role of the OECD in Liberalising International Trade and Capital Flows', published in *The World Economy: Global Trade Policy 1996*, Sven Arndt and Chris Milner (eds).

6 For some 20 years following the early 1970s, the membership of the OECD comprised 24 countries, and the question of enlargement was not an active one. These 'core' members comprised 19 European countries – the 15 which are currently members of the European Community, plus Iceland, Norway, Switzerland and Turkey – together with the United States, Canada, Japan, Australia and New Zealand. Since 1994 five more countries – Mexico, the Czech Republic, Poland, Hungary and the Republic of Korea – have been admitted to membership.

First, the OECD member governments have consistently accepted, and reaffirmed, the principle that their restrictions on international transactions in these areas should be progressively reduced. They have explicitly accepted the limitations that this entails for their freedom of action.

Second, they have accepted, and extended over time, the system of rules and disciplines referred to above. Within it, their restrictions must be transparent, formally notifed, and made subject to review and surveillance in committee; and their powers to claim exceptions or exemptions, and to impose new restrictions or reimpose old ones, are defined and limited in various ways.

Third, within this evolving framework the actual choice of measures, as also the venue in which they are decided and put into effect, is for governments alone to determine. The Codes do not lay down programmes of action, nor are specific decisions to liberalise normally taken within the OECD.

Fourth, over time obligations within the Codes have been extended to cover virtually all international capital flows, short-term and long-term, as well as the cross-border provision of financial services.

Of course, these OECD-related events and procedures are only one element in a more extended picture. The main record of liberalisation in relation to international capital flows is to be found in the actual measures taken by national governments, both individually and in concert, not just in the OECD group but more generally. These too make up the background to the MAI initiative; and they form part of the wider story of still-continuing closer economic integration across the world. I consider first the core OECD area, and then other groupings of countries.

The Liberalisation of Capital Flows in the OECD Countries

From the end of the Second World War, the external economic policies of what became the core OECD member countries, and the ways in which these policies have evolved, have conformed to a broadly similar pattern – more so than for the developing countries, where there was and is much greater diversity. Broadly, these OECD governments have adhered throughout to what I have termed *heavily qualified liberalism*. This approach has been followed in relation to all the main classes of transactions – merchandise trade, trade in services, and capital flows including FDI – though not to international migration, which has remained closely controlled. As one would expect, the degree of commitment to liberalisation has varied – over time, across countries, and between international transactions of different kinds. Policies have been subject, as always, to diverse and often conflicting influences and pressures; and actual outcomes have included interventionist phases, episodes and tendencies. Nevertheless, the prevailing long-term trend in all these countries is clear. Over the half-century as a whole, the external economic policies of the core OECD countries have become considerably, in some ways dramatically, more liberal.

In relation to the MAI, the main elements of this liberalisation process are fairly recent. Over the decade or more that preceded serious thinking about a possible agreement, there were notable advances towards the derestriction of capital flows in general and

FDI in particular. The main advances took place in the countries that were significantly less liberal, so that there was a marked convergence across the OECD area on a broadly liberal régime which earlier had characterised only a limited number of member countries. The two main areas of change, which overlap to some extent, were those of exchange controls and restrictions on inward FDI.

As to the former, long-established and extensive exchange control régimes still existed in the majority of OECD members at the end of the 1970s: the main exceptions were the United States, Canada, Germany, Switzerland, and the Netherlands. However, in October 1979 the entire British system of controls was suspended overnight, and similar action was taken in the following year in Japan. At the end of 1983, Australia likewise abolished exchange controls, and New Zealand followed suit a year later. These radical reforms left, as the main areas of restriction, two groups of countries in continental Europe: France, Italy and the southern European countries, and the Scandinavian countries apart from Denmark. In relation to these, a big step forward was taken with the adoption by the European Community member countries of the Single Market programme, within which, in 1988, the Capital Movements Directive provided the basis for the complete abolition from 1990 of restrictions on capital flows within the Community. All the EC member countries which had continued to maintain exchange controls had brought them to an end by the early 1990s, and they had been joined in this by what were then the three non-EC Scandinavian countries.

Two features of these changes bear in particular on the FDI régimes of the OECD countries. First, the removal of exchange controls went together in almost all cases – including Australia and New Zealand – with far-reaching liberalisation of domestic financial markets; and among other aspects, this typically provided freer access for foreign businesses offering banking and financial services. Second, getting rid of controls likewise entailed removing all restrictions on capital *outflows* including those associated with outward FDI. From then on, it has been only inward flows that have remained subject, in varying degrees, to official restrictions.

Even in relation to inward flows, and for the most part independently of the moves away from exchange controls, considerable strides were taken by the OECD member countries towards greater freedom. For many of them, in Europe and North America, this was the outcome of regional integration agreements. As a result of the Single Market programme and its sequel, flows of inward FDI were very largely freed, not only between the members of the European Community, but also more broadly within the European Economic Area (EEA). Similar though less far-reaching liberalisation measures formed part of the Free Trade Agreement of 1988 between the United States and Canada; and this freeing of inward FDI flows was extended, both geographically and in other ways, within its successor treaty, the North American Free Trade Agreement (NAFTA) of 1993, in which Mexico, not long before its admission to the OECD, became a third participant.

Aside from these regional initiatives, most of the OECD countries also took unilateral measures of various kinds with the intention and effect of making inward FDI flows freer. This can be seen in the widely separated but equally instructive cases of Australia and France.

Two instances of investment liberalisation: Australia and France

From its earliest days, *Australia* had been a country open to capital inflows including direct investment of all kinds; and aside from some cordoned-off sectors, where FDI was heavily restricted or ruled out – chiefly banking, broadcasting, and domestic aviation – this continued to be the case over the first two decades or so after World War II. From the latter half of the 1960s, however, the situation changed. As a result of the growing influence of nationalist ways of thinking, Australian governments, of different political complexions, turned against the long-established 'open-door' régime, and over the period from 1969 to 1975 they imposed a range of successively tighter restrictions on inward FDI. Though some of these proved short-lived, the policy régime as a whole became clearly and explicitly more restrictive, especially in relation to the screening and approval of takeovers and acquisitions of Australian-owned businesses and proposals for foreign ownership of minerals and natural resources. This more nationalist orientation of policy was reflected in the main single item of relevant legislation during these years, the Foreign Takeovers Act of 1975, which was passed under the then Labor government with Gough Whitlam as prime minister.

As noted in a recent analysis, the change of government which soon followed brought no significant rethinking in this area:

> The Fraser government moderated the Whitlam government's rhetoric ... but its actions were not markedly different in kind … in April 1976 surveillance machinery was rationalised with establishment of the Foreign Investment Review Board (FIRB) … .[7]

During the ensuing seven years or so, the nationalist emphasis, and with it the balance between liberalism and interventionism, was broadly maintained; and in the Closer Economic Relations Trade Agreement between Australia and New Zealand (CER), arrived at in 1982 and ratified in the following year, there was no provision for the freeing of direct investment flows between the two countries. One indication of the state of public opinion in the early 1980s is that

> … the national conference of the Labor party in July 1982 announced a policy to reverse the trend toward more foreign domination of the country's economy by increasing Australian ownership and control of resources and enterprises and by closer regulation of foreign investment.[8]

This was still the official party line when the Labor Party came to power after the election of April 1983.

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7 Richard H Snape, Lisa Gropp and Tas Luttrell, *Australian Trade Policy, 1965–97: A Documentary History*, Sydney, Allen and Unwin, 1998, pp 667–8. This volume gives a good short account of the evolution of policy, together with a selection of relevant contemporary documents. Also informative, for the period from 1945 to 1975, is the chapter by Heinz Arndt, entitled 'Foreign Investment', in *Australian Economic Policy*, edited by JP Nieuwenhuysen and PJ Drake, Melbourne, Melbourne University Press, 1977.

8 Lawrence B Krause, 'Australia's Comparative Advantage in International Trade', a chapter in Richard E Caves and Lawrence B Krause (eds), *The Australian Economy: A View from the North*, Sydney, Allen and Unwin, 1984, p 304.

Since then, however, the orientation of policy, and the official thinking that underlies it, have been substantially recast. It is true that the Act of 1975 survives in amended form, while the FIRB still continues to operate. But as from early 1984, the trend was reversed, and a whole series of liberalising measures has been brought in.[9] Although there have also been one or two moves in a restrictive direction, the net result of a succession of legislative and administrative changes over these 15 years has been to restore in Australia something close to the pre-1968 'open door' régime – which itself, as seen above, provided for exceptions. The present stance of policy is officially summarised in terms more positive than would have been used at any stage between the late 1960s and the mid-1980s:

> The Government's foreign investment policy is framed and administered with a view to encouraging foreign investment in Australia and ensuring that such investment is consistent with the interests of Australia.
>
> The Government recognises the substantial contribution foreign investment makes to the development of Australia's industries and resources.[10]

Among the numerous changes made, possibly the most significant have related to the conditions imposed for approving foreign takeovers and new businesses. In 1986 the requirement that 'net economic benefits' should be demonstrated in each case was suspended in relation to proposed investments in manufacturing, tourism and non-bank finance services: from then on, 'proposals were to be automatically approved unless contrary to the national interest'.[11] In the following year, this same relaxation was extended to 'other sectors namely resource processing, services, insurance, sharebroking and rural properties'. Although liberalisation from 1984 onward began and was pushed ahead under successive Labor governments, the orientation of policy was not changed after the Coalition government came into office in 1996.

The way in which policies have evolved in Australia, over this past 30 years or more, has much in common with parallel developments in Canada and New Zealand, where likewise what had become a strongly nationalist and restrictive orientation of policies was reshaped from 1984 onwards.

In *France*, even more than in Australia, from the mid-1980s there has likewise been an increasingly liberal attitude towards FDI. The main changes are summarised in the following excerpts from an OECD report of 1996:

> The rules governing FDI in France have changed considerably since the latter half of the 1980s. Freedom of investment has been instituted for virtually all investment originating in Europe … which accounts for the majority of foreign investment in France. The liberalisation of transport, telecommunications and air transport is under way. The regulations governing

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9 Foreign Investment Review Board (1998), *Report 1996–97*, pp 49–56. A useful chronological list of the main policy measures is in Appendix D and a list of 'legislation, policy statements and publications' is in Appendix B.

10 FIRB Report for 1996–97, *op cit*, p 35.

11 FIRB Report, *op cit*, p 53. This is also the source for the related quotation that directly follows.

> direct investment by countries outside the EEA have been considerably relaxed and simplified. Enterprise creation has been liberalised and acquisitions by non-EEA investors were authorised relatively quickly. A number of reciprocity measures have been allowed to lapse.
>
> Finally, in February 1996, a law repealed the requirement for prior authorisation for the acquisition of French enterprises by non-EEA investors … . Excluding exceptional cases, this authorisation will be deemed granted one month after the application has been filed.
>
> This far-reaching liberalisation was not simply the result of the lifting of exchange controls and the free circulation of capital movements introduced in 1990. Rather, it was prompted by the aim of integrating the French economy more closely into the world economy, the recognition of the beneficial effects of FDI, the need to bring regulations into line with increasingly liberal practice and the desire to attract at least the share of FDI commensurate with France's economic importance.[12]

It is worth noting that in two important respects the French treatment of inward FDI is now more liberal than that of Australia. First, simply as a result of France's membership of the European Community and the way that Community policies have evolved, investment flows of almost all kinds from the rest of the EEA – that is, from countries which make up perhaps one-fifth of world GDP – are close to becoming completely free. Among other aspects, this extends to investments in real estate, which in Australia remain subject to close and detailed screening. Second, the recent change with respect to prior authorisation has probably made the screening process in France for investment proposals from firms in non-EEA countries less restrictive than that which is currently applied to the whole of the outside world, including even New Zealand, by the government of Australia.

Liberalisation in the non-OECD countries

Alongside these developments and for the most part quite independently of them, the climate of opinion with respect to foreign trade, capital controls and inward FDI also changed in a steadily widening range of countries outside the core OECD members. In most cases this was a more radical departure than in the OECD group, since the countries concerned had up to then explicitly rejected the idea of liberal external economic policies, rather than giving it formal approval and effective though heavily qualified expression. An early example of the change was Chile, where far-reaching liberalisation was carried out from the mid-1970s onwards. In China,

> [t]he new political leadership which emerged after the mid-1970s decided to move away from the previous policies of autarchic self-reliance and open the economy to the benefits several other Asian countries had derived from an expanding world economy.[13]

From the early-to-mid 1980s, a growing number of countries, chiefly in Latin America and East Asia, took steps to relax or abolish restrictions on trade and capital flows; and

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12 OECD, *Reviews of Foreign Direct Investment: France*, Paris, OECD, 1996, p 57.

13 Angus Maddison, *Chinese Economic Performance in the Long Run*, Paris, OECD, 1998, p 86.

following the shift in policies that was made in 1991, India joined the ranks of these reformers, though up to now with more reservations.

From 1989 onwards, the same tendencies appeared, following the breakdown of communist economic systems, in many of the former communist countries of Central and Eastern Europe and what had been the Soviet Union. In an article on the transition process in these economies, published in 1996, Peter Murrell noted that:

> Within just a few years, three-quarters of [these] countries abandoned centrally managed trade, removed most quantitative restrictions, reduced tariffs to fairly low levels and adopted essentially full convertibility on current account.[14]

In both groups of countries, a leading element in this reorientation of policies has been the liberalisation of inward FDI. Here as in the core OECD countries, attitudes evolved, and policies became less nationalist, less defensive, and less restrictive. Increasingly, governments have come to take a positive view of the effects of inward direct investment, and have adapted their régimes accordingly. There has been a general tendency to remove barriers and restrictions, to open up sectors that were previously cordoned off, to relax performance requirements, to give recognition and expression to the national treatment principle, to offer positive investment incentives, and to provide more effective guarantees and protection for foreign investors.[15]

Evidence of this change is to be found, not just in the lists of specific measures taken, but also in the spread of *bilateral investment treaties* (BITs), otherwise known as investment promotion and protection agreements. As the alternative title suggests, the object of these treaties is to clarify and secure the rights that can be claimed by foreign investors. Their core elements are the principle of non-discrimination for established investors, protection against expropriation and protection from strife, the freedom of capital transfer, and dispute settlement provisions. Hence the readiness of a growing number of non-OECD countries to enter into them – between OECD members, there are virtually no such agreements, since they are viewed as unnecessary – is a clear sign of the times. At the end of 1997, as noted in the most recent of the annual surveys of international investment, published by the United Nations Conference on Trade and Development (UNCTAD), over 1,500 BITs were in operation, of which approximately three-quarters had been signed during the 1990s.[16] While most of these treaties are between OECD member governments and non-members, a growing number and proportion involve governments from the latter group only.

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[14] Peter Murrell, 'How Far has the Transition Progressed?', *Journal of Economic Literature*, Vol 10, No 2, Spring 1996, p 31.

[15] It should be added that these more favourable attitudes towards FDI have often been reflected in the granting of investment incentives of various kinds; and these typically come under the heading of 'encouragement' as opposed to 'liberalisation'. This point is taken up later, in Section 4.

[16] United Nations Conference on Trade and Development, *World Investment Report 1998*, Geneva, 1998, Chapter IV. A good summary treatment of BITs, as also of other investment instruments including those mentioned in the following paragraph, is to be found both here and in Chapter IV of World Trade Organization, *Annual Report 1996*, Geneva, 1996.

In addition to these bilateral arrangements, an increasing number of non-OECD countries, both in East Asia and Latin America, have entered into, or are discussing the formation of, regional integration agreements in which rules for direct investment flows have, or would have, a place. Two leading examples are the Mercosur agreement between Argentina, Brazil, Paraguay and Uruguay, and the Association of South-East Asian Nations within which new forthcoming investment liberalisation measures have just been announced. Within the looser framework of the Asia Pacific Economic Cooperation (APEC) forum, in which both OECD and non-OECD economies are participants, the liberalisation of trade and investment flows has been officially specified as 'the cornerstone of APEC's identity and activity'; and in 1994 members endorsed a set of APEC Non-Binding Investment Principles.[17] In Europe, the Association Agreements between the European Community and a number of countries in Central and Eastern Europe incorporate rules for the treatment of foreign investment; and a striking instance of cooperation between members and non-members of the OECD is the 1994 Energy Charter, which has now been ratified by 38 countries and is chiefly concerned with investment promotion and protection.

These developments in the non-OECD countries made it possible, for the first time, to think of the process of liberalising capital movements in general, and FDI flows in particular, as one in which both sets of governments, OECD and non-OECD, could now work together towards common objectives – as increasingly they had begun to do, in the context of trade issues, within what was the General Agreement on Tariffs and Trade (GATT) and is now the WTO. This brought a possible extra dimension to the idea of a new MAI-style initiative within the OECD: it now appeared reasonable to think in terms of a procedure, and an end-product for the negotiations, in which non-member countries would also be involved.

The WTO: a wider role

By the time the MAI was launched, the Uruguay Round negotiations had resulted in new agreements, folded into the newly-established WTO, which marked 'the evolution of the multilateral trading system from a set of rules primarily aimed at regulating policies affecting cross-border trade in goods to a set of rules also covering host country treatment of foreign companies'.[18] This too forms part of the story of liberalisation. In two of these agreements, the General Agreement on Trade in Services (GATS), and the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS), there are provisions relating to foreign investment. In the third, the Agreement on Trade-Related Investment Measures (TRIMS), the main aim is to specify, and to rule out, those types of government-imposed performance requirements, chiefly local content regulations or

[17] At present APEC extends to 21 countries, seven of which (Australia, Canada, Japan, the Republic of Korea, Mexico, New Zealand and the United States) are OECD members. The other 14 countries comprise Brunei Darussalam, Chile, China, Hong Kong China, Indonesia, Malaysia, Papua New Guinea, Peru, the Philippines, Russia, Singapore, Chinese Taipei, Thailand, and Vietnam. The quotation is from the record of the 1993 APEC summit meeting.

[18] World Trade Organization (1996), *op cit*, p 71.

trade-balancing conditions, that are incompatible with the rules of the GATT. It is thus an agreement specifically concerned with rules for the treatment of direct investment – the first of its kind since the GATT was established in 1947.[19]

Since in consequence of these agreements the treatment of foreign investors had been formally brought within the scope of the newly-created WTO, it could be asked in the mid-1990s – and was asked – whether the WTO, rather than the OECD, might be the appropriate venue for negotiating a new investment agreement which, if successfully concluded there, would then have a much wider membership and a better claim to be described as 'multilateral'. This would have been the preference of the European Commission, in part because within the WTO the Commission speaks for all its member countries, since trade policies are a Community responsibility, whereas in the OECD each member country speaks for itself and the Commission, though a participant in all meetings, is not a full member. At the 1996 OECD ministerial meeting, ministers in fact 'affirmed their interest in beginning an examination of trade and investment in the WTO and working towards a consensus, perhaps including the possibility of negotiations'.[20] But as is shown by the cautious wording here, and by the fact that these same ministers had already initiated the MAI process, a quite different time-scale would have been involved. In the mid-1990s, there would have been only limited backing among non-OECD members of the WTO for new wide-ranging negotiations on investment; and indeed the TRIMS Agreement, which was and is the closest to being a precedent and point of departure within the WTO structure, is restricted in scope and even so was arrived at only with difficulty: it has been described as 'a useful if somewhat meagre result of five years of tough negotiation'.[21] Given the kind of agreement that the OECD governments had in mind, it would have been impossible, at that stage, for negotiations to be set in train within the WTO. Indeed, the idea was tested at the WTO Ministerial Meeting in Singapore at the end of 1996, and resisted by a group of developing countries including in particular India, Egypt, Malaysia and Uganda.

Since then, four years have passed, the MAI initiative has failed, external economic policies have evolved further, and the possibility of another WTO trade round (the 'Millennium Round') has been opened up. In this new situation, there may well be greater scope for investment issues to be brought more effectively within the WTO, and this possibility is mentioned in Section 5 below.

The impact of privatisation

One reason for the growing involvement of FDI in economies all over the world, and the readiness of governments to tolerate or encourage it, has been the spread of *privatisation*. Where public enterprises had been monopolies, as was generally the case,

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19 The WTO agreement on subsidies is also relevant to investment, since it restricts the use of incentives. It has not so far been tested in this respect through actual cases brought.

20 William H Witherell, 'An Agreement on Investment', *OECD Observer*, No 202, October-November 1996, p 6.

21 John Croome, *Reshaping the World Trading System: A History of the Uruguay Round*, Geneva, World Trade Organization, 1995, p 309. The Agreement covers goods only, not services.

participation of foreign businesses was ruled out. When the enterprises were sold, governments had the option, which was widely and increasingly exercised, of allowing overseas bids and purchases. In some countries, such as New Zealand aside from the case of telecommunications, virtually no restrictions have been placed on the extent of foreign ownership of the assets being sold. More typically, as in both Australia and France, barriers and limitations of various kinds have been imposed, in particular cases, on the extent of foreign participation in sales and ownership of the assets.[22] However, the general tendency across the world has been for restrictions of this kind to become less significant over time; and despite them, it remains the case that, over the whole range of countries affected, decisions to privatise have opened the way for FDI flows that would otherwise have been precluded.

Public attitudes and political calculation

For the most part, though with some exceptions to be noted, the trend towards more liberal external economic policies, and the measures that gave expression to it, did not meet with strong opposition. In the OECD member countries many of the changes were accepted, or at any rate acquiesced in, by the leading political parties and by public opinion. As to the OECD Codes of Liberalisation, the extensions made over the years were of interest only to a restricted circle of experts: most politicians, as well as most voters, had no knowledge even that such instruments existed. As to specific measures of liberalisation, the abolition of exchange controls aroused little public comment and virtually no opposition. Again, within the European Community with its growing membership, the Single Market programme, and the wider freeing of restrictions on capital flows that went with it, was likewise broadly supported or accepted. In relation to cross-border capital movements, therefore, far-reaching steps towards greater freedom were decided on, and put into effect by the many governments concerned, with no serious differences as between the political parties that counted and little public opposition. Outside the European Community, these were not especially popular moves, nor were they seen as means to attract votes. But governments did not lose by them, nor did they expect to.

Admittedly, the freeing of inward investment flows in particular was often more controversial (as also, in many cases, were the reductions in trade barriers that governments made); and alongside this, there was also widespread suspicion of, and hostility towards, proposed schemes of privatisation. But the actual measures taken in these areas were sponsored by governments of different political complexions, and have not since been reversed. In cases where parties took an anti-liberalisation stance while in opposition, it proved normal for them when in office to accept what had already been done, and often to take it further. While governments did not think of either privatisation or the further derestriction of inward investment as ways of gaining popularity, they were not deterred from going ahead, when the time seemed ripe, by

[22] In the Australian case, generally speaking, such restrictions have been imposed in the case of privatisations undertaken by the Commonwealth government, but not when the initiative has come from State governments.

fears that it would bring political disaster. Only in the case of the Canada-US Free Trade Agreement, and its successor the NAFTA, was opposition widespread and intense; and here the main grounds for protest related to trade rather than to FDI.

Because the liberalisation of FDI and other capital flows which took place from the early-to-mid-1980s onward in all the core OECD members, and in a growing number of other countries, had met with a relatively smooth passage, there was reason to think, in the early part of 1995, that this would also be the case with the MAI and the negotiations leading up to it. This expectation was soon to be disappointed.

The question of openness

In the course of the MAI negotiations, charges of concealment and secrecy were made against the governments and officials concerned, and these will be referred to in the section that follows. At this stage, it is worth noting that the OECD Codes were and are public documents, that changes in them were and are invariably published in full, that the existence and terms of reference of the two committees and the nature of their work had long been public matters, and that the OECD had published periodic accounts of these aspects of the liberalisation process and the role of the Organisation within it. Again, the earlier decisions by ministers to inquire into the advisability of going ahead with the negotiations, as also the instruction in 1995 to launch them, were announced in public documents, while the already-quoted report from the two committees, which formed the basis of the instruction, was likewise published. There was no element of concealment here.

Of course, this is not all. In the light of what happened later, it would have been wise for the OECD itself, and for member governments within their own borders, to give greater publicity to the proposal for a wider investment instrument, and to convene or support seminars or conferences at which it could be explained, reviewed and debated. In particular, a broader-than-normal process of consultation could have been initiated. In accordance with standard procedure, consultations were duly held at the OECD, at various stages, with the two committees that are formally attached to the Organisation as representing the 'social partners' – namely, the Business and Industry Advisory Committee (BIAC) and the Trade Union Advisory Committee (TUAC). However, broader consultations involving non-governmental organisations (NGOs),[23] like those held once the extent of public opposition expressed by these groups had revealed itself, could have been organised from the outset. This would have helped to shield the Organisation and member governments from the later damaging (though unwarranted) charges of secrecy and concealment. It might also have done something to dispel misunderstandings on both sides,[24] to give early warning of a number of issues that

23 There is a question of definition here – what to include under the heading of 'non-governmental organisations'. Agencies representing businesses and trade unions, such as the OECD's twin committees, would appear *prima facie* to qualify for inclusion. However, the term 'NGOs' is normally used in a more restricted sense, and this is the convention I have followed.

24 The 'Lalumière Report', to be referred to later, notes that, because of the consultations that had been held with the TUAC, the French trade unions linked to it were less hostile to the MAI than were the French NGOs.

were later to emerge as unexpectedly contentious, and to alert governments to the possibility that this next stage of freeing inward investment could prove more controversial and politically vulnerable than similar exercises in the past.

The launching of the MAI initiative

Such was the background, the sequence of events, against which the idea of the MAI took shape. As to the likely content of the agreement, the liberalisation that it was expected to bring was seen as a continuation of the trend in policies with respect to FDI, and international transactions more generally, which was well established in OECD member countries and increasingly evident in the rest of the world. As to modalities, such an agreement was likewise perceived as a straightforward extension of the roles and activities of the two OECD committees concerned, which had well-functioning procedures approved by member governments and a long record of accomplishment virtually free from unwanted political fall-out. Conducting negotiations within the Organisation, as contrasted for example with the WTO, carried with it the advantages that the Codes provided a firm and agreed basis for further advances, that all the countries involved could be expected to be in favour of an agreement, and that the officials taking part would be experts who were accustomed to working closely together. It seemed evident that an agreement could best be fashioned by (to quote again the 1995 report from the two committees) 'building on OECD's existing instruments and expertise'.

For all these reasons, the path ahead seemed clear. Even so, the decision to proceed was taken only after a lengthy process of consideration. Instructions to the two OECD committees to examine the idea of a 'wider investment instrument' were given by ministers as early as 1991. By the time that the launching officially took place, therefore, the project had been the subject of systematic and increasingly detailed review by officials from member governments for a period of four years. Whatever the reasons for the subsequent failure of the MAI, lack of technical preparation cannot be held among them.

Given all these favourable trends, signs and endorsements, and the long and apparently thorough preparatory work, why did the MAI negotiations break down?

3

THE NEGOTIATIONS: FROM LOSS OF MOMENTUM TO BREAKDOWN

Participants and process

Following the decision to go ahead, the two committees of officials joined forces in their Negotiating Group, which had been charged with the task of drafting a treaty. At all the meetings of the Group, a WTO representative attended as an observer, while the International Monetary Fund and the World Bank were likewise represented when the agenda concerned them. (No such invitation, however, was extended to UNCTAD, which in 1996 was given a mandate by its member governments to work on a 'possible multilateral framework on investment'). From September 1997 on, a number of non-member countries became participants with observer status: the full list of these eventually comprised Argentina, Brazil, Chile, Hong Kong China, Estonia, Latvia, Lithuania and Slovakia.

The MAI was envisaged from the start as an instrument which the OECD countries would design but others could accede to. This procedure has been condemned, on the grounds that countries which had had no part in drawing up the agreement could not be reasonably be expected to wish to join it. This however is a mistaken argument: recent history provides many instances where countries have been ready to act in such a way. For example, the GATT was concluded by the then Contracting Parties as far back as 1947, but this did not deter Mexico from joining some 40 years later, when the conception of national interests had changed. Again, no would-be new entrant to the European Community has yet been deterred from applying by the European Community's insistence that in every case the already established *acquis communautaire* must be accepted in full. Within the MAI negotiations, in the event, the participation of non-members proved to be a positive feature.

The Negotiating Group emerged as a rather mixed body, in that the departments represented on it varied from country to country. In Australia, the negotiating authority rested with the Treasury, while in France, similarly, it was lodged in the Direction du Trésor of the Ministry of Finance, the Economy and Industry. In the United States, representation was shared by the State Department, the Office of the US Special Trade Representative and the Treasury, with the first two of these playing the most active roles. In Japan also, the responsibility was shared, between the Ministry of Foreign Affairs and the Ministry of International Trade and Industry. In New Zealand, the responsible department was the Ministry of Foreign Affairs and Trade, while in Britain it was the Department of Trade and Industry and in Germany the Ministry of Economics. This mixed allegiance is unusual for an intergovernmental committee, and it may be that the difficulty of reaching agreement was somewhat increased by it. However, it is clear that the main problems of the MAI arose from other causes than the choice of principal negotiators.

As was to be expected – since it was standard procedure, not peculiar to the OECD – the Group's discussions were closed to outsiders, nor were the formal records of them made public by the Organisation (though the official summaries were released to non-member governments with country attributions removed). From time to time, however, the OECD held conferences on the subject-matter and progress of the negotiations, normally involving official participants from non-member countries, and most of the associated conference papers were published.[25] In addition, articles were published on the MAI, talks given, and press conferences held, by Secretariat members. To this extent the issues involved, and the ways in which they were being dealt with, were made public by the Organisation right from the start, though admittedly not in ways that gave prospect of a large audience. While initially there was no systematic attempt to enlist the interest, still less the participation, of a wider public, there was equally no veil of secrecy; and as from June 1996, the Organisation set up a page for the MAI on the OECD Internet site, which provided 'information on the history of the negotiations, the status of current negotiations, and the issues under discussion'.[26] It is therefore surprising that the European Parliament, in the course of a Resolution concerning the MAI which it forwarded in 1998 to the European Commission, should have expressed itself as 'regretting the fact that the negotiations have hitherto been conducted in the utmost secrecy'.[27] As will be seen later, this is not the only respect in which the Resolution is misleading to the point of total irresponsibility.

A strong though less sweeping condemnation of the process has been made in the Lalumière Report, where it is argued that leading issues 'were not brought by the Secretariat to the attention of ministers, still less made the subject of debate'.[28] This is unfair to the OECD Secretariat, since it is not at all their role to raise issues with ministers, nor indeed to have any direct contact with them: it was and is the task of the national civil servants concerned – in this case, the members of the Negotiating Group – to keep their own ministers informed, and to warn them of risks that could lie ahead. However, it is true (i) that both Group members and the Secretariat failed to anticipate the extent of the political problems that were to arise in the negotiations, and (ii) that a wider and more timely consultative process, of the kind already referred to, might have alerted both them and their governments to developments which, in the event, came as an unpleasant surprise.

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25 For example, *Multilateral Agreement on Investment: State of Play in July 1996*, Paris, 1996, which contained a first selection of the papers given at a conference in Rio de Janeiro. Further instalments of this 'State of Play' series were issued later.

26 OECD, *Policy Brief No 2, 1997: The MAI*, p 8.

27 European Parliament, 'Resolution containing Parliament's recommendations to the Commission on negotiations in the framework of the OECD on a multilateral agreement on investment (MAI)', Brussels, 1998.

28 *Rapport sur l'Accord Multilatéral sur l'Investissement (AMI)*: Interim Report, Paris, September 1998, p 3. This document, which will be further referred to below, is generally described as the Lalumière Report, since the inquiry was led by Catherine Lalumière, a French Member of the European Parliament.

Two problem areas

Two main interrelated sources of concerns about, or active opposition to, the MAI, emerged successively. As each grew stronger and the two became mutually reinforcing, they led eventually to a suspension and then a termination of negotiations.

The first source of trouble was internal, as problems emerged within the Negotiating Group. Various issues proved more difficult and more contentious than had been expected, in large part because of the rather far-reaching character of what was attempted. Hence it appeared increasingly, as time went on, that the conception of the MAI might be too complex and too ambitious to bring off, and that in any case the negotiations would outrun the time initially assigned to them. This was duly reported to the OECD Ministerial Council meeting of 1997, where the communiqué said that ministers 'welcome the major progress made' and 'express their determination … to conclude the Agreement in time for the 1998 Ministerial Meeting'.

It was only several months later that a second factor, still less foreseen at the start, began to make its full impact. As the negotiations went ahead, from the latter part of 1995, a growing number of NGOs had begun to take an interest in them, and to express their concerns about the aims and content of the agreement. In December 1996 there was an informal meeting with some of them at the OECD, and in October 1997 this was followed by a fuller and more carefully prepared meeting at which the members of the Negotiating Group and Secretariat officials engaged in discussion with representatives of over 40 NGOs, who afterwards apparently felt that for them it was not a productive session since their objections had not been heeded. Meanwhile, the opposition had acquired a new dimension. In August 1997 the then Consolidated Negotiating Text of the MAI, which had been circulated to members of the Negotiating Group by their Chairman, and which had the status of a restricted internal document, was leaked by posting on the Internet. This gave rise to a wave of attacks, likewise posted on the Internet. The whole conception of the MAI became the subject of a hostile international campaign by NGOs in immediate communication with one another. Hence the agreement emerged as a live political issue, with the potential for losing votes and support. This cast further doubt on the practicability of the original concept. Well before the 1998 OECD Ministerial Council meeting was due to be held, it was clear that the project was in trouble.

Before turning to the sequel and the final outcome, some further words are due on both the two problem areas, the internal and the external.

The OECD members: several bridges too far

The MAI was thought of from the start as a big step forward. This followed from the decision to create a new and free-standing instrument. For such an instrument to have an identity of its own, a rationale, it would have to go well beyond what was already to hand within the OECD, in the Codes and Declaration: as compared with these, it was described by the Secretary-General of the Organisation as being 'a quantum leap to something much more ambitious'.[29] In any case, as has been seen, the previous 10 years

[29] Donald Johnston, in a speech delivered at the University of Toronto, 10 November 1997.

had brought on to the world scene a whole series of new intergovernmental agreements – bilateral, regional, multilateral and sectoral – designed to make investment flows freer and more assured. To justify its creation and separate existence, the MAI would have to offer also new elements or dimensions which these did not collectively provide: it would have to bring 'value added'. From the outset, the negotiations were viewed in this light.

As a result, the proposed draft agreement was conceived in broad and far-reaching terms. It was to be 'comprehensive and fully binding', and incorporate 'high standards in every respect'.[30] In the event, governments in the Negotiating Group settled for a good deal less than total comprehensiveness, since they decided – to the relief of the experts in that field – not to cover the central and highly complex issues of *taxation*. But the problems arising from the issues that remained ensured that, even before its original completion date, the MAI was revealed as being more than one bridge too far.

This can best be shown by setting out what were intended to be the main new elements in the agreement – those which were initially seen as establishing the identity of the MAI as a true leap forward. Arguably, the list comprises some 15 main items:

- Unlike the Codes, the MAI was to be a fully-fledged international treaty, to be ratified by national legislatures.
- As to application, interpretation and enforcement, and again unlike the Codes, it was to incorporate formal dispute settlement mechanisms. These would provide for investor-state as well as state-to-state actions.
- The definition of 'investment' was to be comprehensive and open-ended, so that it would include '[not only] direct investments (the creation, expansion or participation in an enterprise), but also portfolio investments (whether debt or equity), real estate, intellectual property rights, rights under contract and rights conferred by authorisations or permits'.[31]
- All official actions would be included – legislative, regulatory and administrative.
- All phases of the investment process would be covered, and hence made subject to national treatment and most-favoured-nation obligations. These obligations would therefore be extended to include applications to invest, as well as the operations of firms that were already established. Subject to reservations or exceptions being agreed, all screening processes would therefore be put in question.
- Reservations – 'country specific exceptions', as distinct from what was designed to be a narrow range of 'general exceptions' – would be subject to 'standstill', in that the lists could not be added to; 'rollback', in that there would be a clear obligation to move in due course towards paring them down; and 'ratchet', in that once removed an exception could not be restored.

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30 Witherell, *op cit*, p 7.

31 Robert Ley, 'The Scope of the MAI', in OECD, *Multilateral Agreement on Investment: State of Play in April 1997*, p 41.

- The 'topdown' principle would apply, so that all general and specific exceptions would have to be listed and all non-listed investment actions would be automatically subject to the disciplines.
- New measures of liberalisation would be introduced by governments in the course of the negotiations, and would be incorporated in the final treaty ('upfront liberalisation').
- Privatisation measures would be made subject to national treatment and MFN obligations.
- There would be provisions governing the conduct of public monopolies and state enterprises, to ensure that foreign investments were not discriminated against.
- Higher standards of investment protection (relating to general treatment, expropriation, protection from strife, and free transfer of funds) would be incorporated.
- Performance requirements would be made subject to prohibitions or specified limits, going well beyond, in both coverage and content, those to be found in the TRIMS agreement within the WTO.
- Rules and disciplines would be brought to bear on investment incentives.
- Rights of access and residence would be established, in relation to all stages of the investment process, for key foreign personnel.
- The various disciplines would now be applied to lower levels of government, as well as to measures applied by national authorities.

This was not all. The above list comprises only those new elements which – with the arguable exception of limits for investment incentives – were generally agreed to be desirable. But in addition, there were from the outset major issues on which there was already open disagreement, which could not be excluded from the agenda in the way that taxation was soon to be, and where failure to make progress could well be damaging to the negotiations as a whole. This additional list covered:

- The question of extra-territoriality – ie, whether and in what circumstances a state can extend the application of its investment-related national laws beyond its own territory.
- Special provision for 'regional economic integration organisations' (REIOs), by which the member countries would be able to extend preferential treatment to each other without this becoming subject to the disciplines governing exceptions.
- The treatment of 'cultural' industries.

Later, as the negotiations went on, their scope was extended still further. There emerged as an additional major item, on which again there was no prior consensus, the proposed inclusion within the agreement of provisions relating to environmental standards and labour standards. From early 1997 onwards, these latter issues took up a lot of time. Although eventually a formula was worked out which was acceptable to a large majority of countries, no consensus was arrived at: here as elsewhere, there remained unsettled questions even at the end of 1998, when the negotiating process came to a halt.

All this proved too much for negotiators to handle and – more important – too much for governments to swallow. Within the list, it is perhaps not profitable to identify particular items which became (so to speak) the critical bridges too far: it was the ensemble, the package as a whole, that was revealed as unmanageable. As time went on, three interacting elements began to weaken the momentum of negotiations, and to put in doubt their final success.

Differences, disappointments and growing concerns

First and not surprisingly, problems and differences arose over most if not all of the new aspects – for example, the wording of the broad definition of investment, the design of dispute settlement mechanisms, and the treatment of investment incentives. The area of disagreement was later extended, at least for a time, when it came to considering different proposals for the treatment of international norms and standards. Over a range of issues, the task of arriving at agreed texts proved harder, more contentious and more time-consuming than had been expected.

Second, it became clear that it would be difficult, if not impossible, to bring about a situation in which mutually acceptable concessions would be made on subjects where open disagreements already existed. This particularly affected the largest trading and investment entities involved, the United States and the European Community. For its part, the United States, which had pressed strongly for the launching of the MAI, wished in particular to make progress in relation to (i) the screening of investments (prior authorisation), (ii) an effective dispute settlement mechanism, and (iii) the imposition of transparency obligations and effective disciplines on exceptions for cultural industries and REIOs. By contrast, the European Community and its members were concerned to limit extraterritoriality, as claimed by the United States in the context of the Helms-Burton Act and the Iran-Libya Sanctions Act, and to ensure that disciplines were extended to lower levels of government, which meant pre-eminently the constituent States of the United States. When it became clear to both sides that achieving the results each hoped for under these headings would be difficult, this naturally led to a feeling that the negotiations might in the end have little of substance to offer to the leading participants. It may be that, as in other contexts – the current dispute over bananas being a notable and depressing example – both sides could have acted in a more constructive and responsible way.

Both disagreements and disappointments, as also difficulties in maintaining momentum, arose from a fundamental problem which confronted, though in varying degrees, all the countries involved. Everywhere, the pace and content of liberalisation had up to then been fairly closely controlled by national governments, whether acting individually or together, and the political risks at each stage had been reasonably calculable and on the whole well contained. It was not clear that this would be true of the MAI, with its well-advertised combination of 'high standards' all round, 'upfront liberalisation', a formal treaty, and new mechanisms for enforcement. Governments became increasingly concerned over the possibility that they would lose control, or be seen as having lost it, over the pace of liberalisation, and over sensitive areas of policy where they had hitherto maintained, and wished to continue to maintain, their freedom of action. Hence defensive attitudes set in, and the list of proposed national exceptions grew to an extent which made this on its own a source of difficulty within the negotiations and of scepticism as to their final results. This concern of governments with the eventual acceptability of the agreement was naturally heightened as the opposition to the MAI became widespread and vocal.

The impact of the NGOs

From the time when the MAI negotiating text appeared on the Internet, the opposition grew and spread in a remarkable way. It brought together, over a growing range of countries within and beyond the OECD members, a broad coalition which included conservation and environmental groups, consumer associations, societies concerned with development in poor countries, human rights groups, local governments, movements for social justice, organisations representing indigenous peoples, church groups, and trade union and professional organisations. An increasingly concerted international protest movement gathered momentum, and a set of negotiations which up to then had aroused little public attention now became a focus for world-wide controversy. 'At the time of its defeat, internationally co-ordinated anti-MAI campaigns were known to be active in more than half of all OECD countries and numerous developing countries'.[32] A storm had burst over the hitherto calm and secluded proceedings of OECD committees.

As to individual OECD member countries, Australia provides one instance among many of swiftly gathering opposition. In March 1998 both the minister for foreign affairs and the Senate referred the MAI for inquiry to the Joint Standing Committee on Treaties of the Commonwealth Parliament. The inquiry was advertised in mid-March, and submissions were called for by 30 April. In response, as noted in the Committee's interim report:

> [S]ome 792 submissions were lodged … . We believe that many other organisations and individuals intend to put submissions before the Committee … . The overwhelming number of submissions oppose or express concerns about particular aspects of the MAI. [33]

The long list of organisations which responded so promptly to the Committee's call includes 'Citizens Against MAI', 'Australia Stop MAI Coalition', and 'Coalition Against the Multilateral Agreement on Investment'.

In many countries, the opponents of the MAI who now emerged viewed it as a highly significant, even momentous, development: it was described in such terms as 'this historic agreement', and 'what might have been the most far-reaching international

32 Oxfam GB, 'Update on the MAI', Oxford, December 1998, p 1.

33 Parliament of the Commonwealth of Australia, Joint Standing Committee on Treaties, *Multilateral Agreement on Investment: Interim Report*, Canberra, May 1998.

agreement of the century'. Moreover, as the campaign gathered strength, it became clear that more was at stake than the MAI itself. As the Lalumière Report (p 3) noted: 'The agreement has become a symbol. It crystallises the demands and frustrations of civil society with respect to globalisation'. This largely accounts for the vehemence of the opposition.

The impact of the NGOs on the negotiations was both direct and indirect. As to the former, they influenced the content of official discussions and the way in which successive drafts of the treaty evolved, particularly in relation to the treatment of social and environmental standards. It was partly in response to NGO criticisms, although pressures from within national governments were also involved, that these issues became so much more prominent as the negotiations went on. In later drafts the language was designed to ensure (i) that social and environmental standards would not be lowered in order to attract foreign investments, (ii) that obligations under the treaty would not hinder or prevent governments from maintaining such standards, and raising them as they saw fit, and (iii) that under the provisions relating to expropriation, foreign investors would not be able to claim compensation for losses arising from the non-discriminatory exercise by governments of their regulatory powers. This reflected to a large extent the arguments and pressures that the NGOs had brought to bear.

However, the decisive impact of the NGOs was indirect rather than direct. Their campaign had made the MAI into a prominent and sensitive political issue; and as such it was also taken up by commentators, many if not most of whom were sceptical or hostile, and by parliamentarians who felt that they had been insufficiently informed and consulted. Despite the fact that, as will be seen, some leading arguments brought against the agreement were worthless or highly debatable, while the often-repeated charge of secrecy was unfounded, there was little attempt by governments or the OECD to fight back. The extent of the opposition surprised and disconcerted political leaders, and led them to question a commitment, and a process, which in the earlier stages they had barely noticed.

The ebbing away of support

From the latter part of 1997 onward, the situation of the MAI grew worse. Partly because of the growing outside opposition, but also (and probably still more) as a result of the continuing internal difficulties which remained unresolved, it became increasingly apparent that, if any agreement was eventually reached, it would have to be on a watered-down version of the treaty as originally conceived. This weakened the case, and contributed to a loss of momentum. On the one hand, it did nothing to disarm opponents, since their objections were wide-ranging and in many cases fundamental. On the other hand, it undermined the whole rationale of the agreement, since dilution meant a significant reduction in 'value added'. Hence for many of those who favoured liberalisation, and had therefore supported the original conception, the fate of the MAI now began to seem a matter of indifference. This reaction is illustrated in an article published in April 1998 by an Australian academic, who concluded that:

> ... the negotiations at the OECD, which set out to produce a mountain of reform, have so far yielded a molehill ... . If the present draft were jettisoned, not much would be lost.[34]

Such a view became increasingly prevalent in the business community. Generally speaking, the main concern of business groups lay in securing greater openness and consistency in the FDI régimes of the non-OECD countries, rather than in tightening up the OECD Codes; and for this reason some of them had favoured the WTO, rather than the OECD, as a venue for negotiations. Once it became clear that only a limited number of non-OECD governments were likely to become signatories of the MAI, its potential value was reduced. A second factor affecting business sentiment was the differences that arose in the negotiations with respect to (i) pre-establishment screening processes, (ii) performance requirements, and (iii) dispute settlement mechanisms, including especially provision for investor-state actions. As time went on, it appeared doubtful whether what the MAI would provide in relation to these would go even as far as what was already to be found in the leading regional integration agreements and a number of BITs. Further, business organisations became concerned about the inclusion within the MAI of provisions relating to social and environmental aspects, which (it was argued) would obscure and interfere with the primary purpose of the treaty. For all these reasons, the feeling spread that whatever was eventually signed would not be worth a great deal.

Within OECD governments, the prospective balance of gains and costs from the MAI became notably less favourable, as a result of changes on both sides of the scales. This is illustrated by the cases of Australia and France.

In Australia, the main political parties are agreed that it is in the national interest for Australia to be a seen as an open economy, where inward foreign investment is generally welcomed, and assured always of treatment which accords with public laws that are consistently applied and in conformity with internationally accepted norms and practice.[35] But as the MAI negotiations proceeded, it became clear that the country's standing and reputation in this respect, already well established, did not at all depend on their successful conclusion – the less so, as the prospective outcome was watered down, and the argument that the MAI would represent a notable advance for the participants collectively became harder to uphold. Hence while the political risks of signing even a diluted agreement had greatly increased as the negotiations went on, the prospective countervailing economic gains, which in any case had been seen as modest rather than spectacular, now appeared smaller. As a result, official support, which throughout had been qualified and conditional, was further weakened.

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34 Wolfgang Kasper, 'Open for Business?: Australia's Interests and the OECD's Multilateral Agreement on Investment', *Issue Analysis No 1*, Sydney, Centre for Independent Studies, p 19.

35 This is not true of the smaller parties, all of which are more nationalist and highly critical of foreign ownership of Australia-based assets and resources. Not surprisingly, the same strand of thinking is to be found in the major parties also, though there it is in opposition to the official line. This strong continuing nationalist element in political life, which of course is not peculiar to Australia, helps to account for the remaining official restrictions on inward FDI and the hesitancy of governments about relaxing these further.

In France, the same tendency, in this case stronger and more emphatic, made its appearance in early 1998. As late as October 1997, a French delegate to the negotiations, in the course of a meeting, had described the MAI as 'a reasonable agreement'[36] but following demonstrations that took place in Paris in February, largely focusing on the threat which the MAI might represent to the freedom of French governments to safeguard national cultural interests, the government became alerted to what it now saw as defects and dangers in the draft agreement, and a strong cautionary statement was made by the responsible minister. As will be seen, this was soon to be followed by more drastic action.

While each case is different, much the same tendency appeared in other OECD countries: both Canada and New Zealand are clear examples, while as noted above both the United States and the European Community had reason to view the prospective outcome as disappointing. Everywhere, the combined effect of 'inside' reservations and disagreements and the 'outside' upsurge of opposition was to deprive OECD governments of their initial readiness to back the project, and to bring many if not most of them to view it as at best an unrewarding venture and at worst a political liability.

The end of the line

The new and less favourable atmosphere was reflected in the 1998 OECD ministerial meeting. Contrary to all past experience with the handling of such issues, and in a development which few would have predicted even as recently as one year earlier, the MAI became the main single focus of discussion in the meeting, and some sharp exchanges took place. In the communiqué, a special section was devoted to the subject, the wording of which gives evidence of differences patched up rather than resolved. Ministers reaffirmed 'the importance they attach to achieving a comprehensive multilateral framework for investment with high standards of liberalisation' but they went on to announce 'a period of assessment and further consultation between the negotiating parties and with interested parts of their societies', in preparation for the next meeting of the Negotiating Group in October 1998. The communiqué referred to 'the need to complete work on MAI disciplines and exceptions', while at the same time mentioning specifically a number of the headings under which doubts and reservations had been expressed.

In France, a special commission was then appointed, in May 1998, to inquire into the MAI and make recommendations concerning the next steps to be taken: its interim report (the 'Lalumière Report', already referred to above) was issued in October, following extensive consultations with business organisations, trade unions, NGOs and other interested parties. The report concluded that while it was clearly in the interests of France 'to work actively for a framework of rules governing international investment', the negotiations could not be continued within the OECD unless a 'fundamental reorientation' was made: without this, France should withdraw from the proceedings. Reorientation was needed in particular because (it was argued) the MAI as proposed was subject to the 'fundamental objection' that it presented a new and serious threat to national

36 OECD, *Multilateral Agreement on Investment: State of Play in October 1997*, p 36.

sovereignty. France should support the idea of further negotiations, which could be either in the OECD or (in due course) in the WTO, but only subject to 'at least' seven conditions designed to meet this objection. Briefly, this list of seven, which in its total effect was notably restrictive, comprised:

- A restricted definition of FDI, to exclude portfolio investment and financial market operations
- Dispute settlement procedures to be confined to actions between states alone
- Deletion of the reference to 'full and constant protection and security', under the heading of 'general treatment' of investments
- Deletion of the reference to 'measures having equivalent effect', in relation to the draft clause on expropriation
- Action ruling out performance requirements to be limited to an extension of the TRIMS provisions in order to cover services as well as goods
- Abandonment of the 'ratchet' provision, so that reservations withdrawn could be later brought back, subject to compensation for trade partners as in the WTO
- A requirement that the final agreement be conditional on the adhesion of a sufficient number of non-OECD countries.

The receipt and publication of the Lalumière Report was followed by an official statement in the Chamber of Deputies by the prime minister, M Jospin, on 14 October – a week before the Negotiating Group was due to meet, following the six-month pause. Like the Report, he emphasised in particular that the MAI posed 'fundamental problems with respect to the sovereignty of states'; and after describing the agreement in its present shape as 'unreformable', he announced that France would take no further part in negotiations at the forthcoming meeting in the OECD. As to the future, he said that France wished and would propose a resumption of negotiations, but on 'an entirely new basis', and with full involvement of non-OECD countries so that the venue, 'naturally', would be the WTO.[37]

This effectively brought the negotiating process to an end. The other participants duly came together in the following week, at what could now only be an informal meeting. Immediately following this, the subject was considered by the Executive Committee in Special Session, an OECD committee of senior officials from ministries of foreign affairs. The Chairman of this Committee – Mr Stuart Eizenstat, US Under-Secretary of State – afterwards issued a statement that ended as follows:

> There was a consensus among delegates on the need for and value of a multilateral framework for investment. The goal should still be sought. At the same time, delegates noted that significant concerns had been raised during consultations on the MAI. They include issues of sovereignty, protection of labour rights and environment, culture and other important matters.

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37 Statement by the prime minister in response to a question in the National Assembly on the Multilateral Agreement on Investment, 14 October 1998.

> Delegates agreed on the importance of devoting additional time to take stock of these concerns and to assess how to accomplish the goal we all share of developing a multilateral framework of rules for investment. In further consultations, it will be important to broaden the participation of non-OECD member countries and to engage in further discussions with representatives of civil society (business, labour, non-governmental organisations, consumer and other groups). These consultations should proceed with a view to deciding how best to reach the shared goal … and to deal effectively with the concerns that have been expressed.

These were small results indeed to announce after more than three years of intensive work in the negotiations; and the only sequel was the further informal OECD meeting in early December, already referred to above, at which the curtain was finally brought down.

4

LIBERALISATION: THE ARGUMENTS REVISITED

Within the MAI debate, the arguments that bear on the further freeing of international investment flows have been given a new airing. Here the current position of the OECD is in some ways open to question. On the other side, a number of mistaken or dubious arguments brought forward by opponents of the agreement, and by advocates of watering down, have gone surprisingly uncontested.

The OECD case: muddying the waters

With a view to topicality, recent OECD statements have argued the case for an agreement such as the MAI on the grounds that it would make for greater stability in international financial markets. Thus the Secretary-General of the Organisation, in his opening statement at the October 1998 consultations referred to above, asserted that:

> "Patient capital" as opposed to short term "hot money" is what the world needs. A good international investment agreement would make an important contribution to a new architecture for the international financial system.

In the same vein, a few days later, the Chairman of the Executive Committee in Special Session, Stuart Eizenstat, made the point that:

> It is particularly important to encourage foreign investment at a time of concern about the effects of short-term capital flows.

While there is something in this idea, the case for freeing FDI flows does not at all depend on it. More important, the argument is from an OECD point of view two-edged. In so far as short term capital flows constitute a problem, an obvious remedy, more direct than promoting FDI, would be to place restrictions on them. Yet as noted in Section 2 above, and described more fully in the Annex, the OECD member governments, through the Codes of Liberalisation, chose some 10 years ago to move in the opposite direction: the obligation to liberalise was then extended to cover virtually all short-term flows, with no reservations for so-called 'hot money'. The logic of the Secretary-General and Mr Eizenstat might suggest that this extension should now be reconsidered. For good reason, this is not at all in question. No OECD member government – and this now includes Korea, which was one of the countries most seriously affected in the Asian financial crises of 1997 – has acted to reimpose restrictions on capital flows, nor has it been suggested that recent financial market instability has put in question this aspect of the Codes.

A second argument, traditional rather than topical, and directed to the freeing of *inward* FDI flows, is likewise double-edged. It can be found in the 1996–97 report of the Australian Foreign Investment Review Board. Here it is maintained (p 35) that in the Australian case:

> Capital from other countries supplements domestic savings and provides scope for higher rates of economic activity and employment.

While the general point is valid – subject to a qualification about to be made – it likewise carries an unintended implication. For if it is an object of policy to raise aggregate domestic investment, however financed, why not promote this end, not only by encouraging inward FDI, but also by discouraging outward flows? Like the previous argument, the reasoning here could point towards a reimposition of exchange restrictions.

A third argument, to be found, alas! in some recent OECD Secretariat documents, is that *outward* FDI flows will benefit the source countries by increasing exports and 'improving' the trade balance. But such increases and 'improvements' are not ends in themselves; and if they were, one would have to take account also of the counterpart changes, by the same token presumed to be adverse, that would necessarily occur in other countries. This line of thinking should be laid to rest.

A better though still not watertight OECD argument, again prompted by the wish to be topical, is that *inward* FDI (to quote again Mr Eizenstat) 'creates good jobs'. Here there are two main qualifying points. First, if the argument is put in the context of high unemployment rates, it is obvious that present-day cross-country differences in these rates, which are wide, cannot be accounted for by reference to the character of the foreign investment régimes concerned: their respective treatment of FDI flows does not at all explain why the recorded 1997 unemployment rate for the United States was 4.9 per cent, while that for Spain was 20.8 per cent. Freeing FDI flows is no more than a minor element in a programme to bring down unemployment.

The second point is more general. It is argued, and rightly, that inward FDI flows, often if not characteristically, bring with them not only 'good jobs', as claimed here, and higher aggregate rates of saving and investment, as suggested by the Australian FIRB, but also skills, expertise, contacts, access to new markets, the transfer of better methods and new technologies, and a reinforcement of domestic competition, all of which should contribute to better economic performance in host countries. Hence foreign investment is often viewed as an 'engine of growth'. But while all this is broadly true, and important, it does not establish a case for particular investments. The net benefits that FDI projects will bring to the host country – the 'social rate of return', as distinct from the profitability of an investment to the investing firm itself – are affected by the associated terms and conditions which may vary greatly from case to case. Suppose, for example, an investment is made in a line of production which is highly protected in the host country, or that the project is heavily subsidised in one way or another. Such a venture may be profitable to the investing firm, and furthermore have all the positive effects just cited above, yet it may nevertheless represent a poor bargain because of the costs of the incentives attached to it or the low value at international prices of the output that it produces. Hence a general argument for freedom of international capital flows which covers specific cases has to be put in other terms than those just summarised.

A liberal rationale

A more secure basis for freedom of FDI flows, inward and outward alike, is to be found in an earlier OECD publication already quoted. This restates as follows a prosaic rationale which goes a long way back in history:

> The ultimate objective is that residents of different Member countries should be as free to transact business with each other as are residents of the same country.[38]

The principle asserted here is that of *non-discrimination*. It is a general principle, and in applying it to international economic relations investment is only one dimension. The argument for freedom of cross-border capital flows, inward and outward, is part of a broader case, which extends also to trade in goods and services and to the movement of persons, for closer economic integration across political boundaries. The case applies within as well as across national states, wherever the existence of separate political jurisdictions gives rise to discrimination.

As stated above, the rationale is incomplete. That residents and non-residents should be treated alike is not an end in itself. At a deeper level, reducing the extent of discrimination as between them is a means to enlarging the domain of economic freedom – both for its own sake, as a leading dimension of personal freedom more generally, and as a means to greater prosperity. The case for closer cross-border economic integration forms part of the wider case for economic liberalism.

Pushed to the limit, this guiding principle points to full economic integration across the world as a final goal. In this situation political boundaries would lose most of their economic significance.[39] Of course, no government today is committed to full integration of its national economy with the whole of the rest of the world. Especially but not only with respect to international migration, there are strong reservations virtually everywhere. Indeed, most governments permit, and even encourage, elements of disintegration within their own borders; and the same is true of member governments collectively within the European Community. But a large and growing number of governments have accepted the idea of closer integration in specified areas and classes of transactions, and have taken steps accordingly: the main story here has been summarised above in Section 2.

This is the context in which the role of the OECD is to be seen. What its member governments have instructed the Organisation to work towards, through the Codes and

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38 OECD, *The Liberalisation of Capital Movements and Financial Services in the OECD Area*, Paris, 1990, p 13.

39 Some significance would remain even with full integration, if only because tastes and customs vary and buyers' choices may be affected by the local, regional or national associations of different products. But political boundaries would lose much if not all of the economic significance they now derive from the discriminatory policies of governments.

Declaration (and had it come off, through the MAI), is progressively closer economic integration with respect to capital flows and related transactions, within as well as across member states, and *with no defined limit to the process*. Non-discrimination is a guiding principle in this, even though the thinking and practice of member governments are far from being fully liberal.

Despite what is often asserted, a liberal investment régime is not designed either to favour inward FDI or to offer special opportunities to multinational firms. On the contrary, non-discrimination implies strict neutrality. In so far as foreign investors are now discriminated against – for example, where screening processes operate, or rights of access and residence are closely limited – liberalisation would indeed improve their relative (at present more restricted) status. On the other hand, special deals involving investment incentives for inward FDI, which as noted above are a common feature of the world scene today, would for the most part be inadmissible. The whole array of tailored subsidies, tariffs or quotas, tax holidays, low-cost infrastructure, monopoly rights, and preferences with respect to government procurement, as also the detailed performance requirements with which such special concessions are often linked, would be ruled out of order. The aim of a liberal foreign investment régime is to open the way for FDI flows, outward as well as inward, and not to encourage or promote them either in general or in the case of specific projects. Liberalisation does not mean dispensing favours to foreign investors, and a liberal régime would in fact preclude governments from doing this.

The MAI initiative, then, can be seen as a cooperative attempt to tie the hands of participating governments, in order to bring their investment régimes closer to a non-discriminatory liberal norm. By the same token, the opposition to the MAI was largely based on an anti-liberal rationale, a rejection of economic liberalism in this context as in others. Here three main strands of thinking are to be found, often though not always linked together. They relate to (i) the role of multinational companies, (ii) the freedom of national states to choose and operate their own industrial policies and development strategies, and (iii) the observance of internationally agreed environmental and social standards.

Anti-liberalism: the multinationals as a menace to humanity

Among the charges brought against the MAI, one of the most insistent has been that it would have transferred power from national governments to multinational companies, with unfortunate or disastrous results for the host countries or even the world as a whole. In Australia, for instance, the Joint Standing Committee on Treaties, in its interim report referred to above, noted in relation to the large number of immediate submissions made to it that:

> Many … express broad views that the MAI will reduce Australia's sovereignty and allow multinational corporations to plunder Australian assets with no corresponding obligations on them (p 17).

In the same vein but with a much wider, even apocalyptic, perspective, a report prepared in mid-1998 for a Canadian NGO, the Council of Canadians, goes beyond the possible dangers to host countries, asserting that

> … this global investment treaty constitutes a power grab for transnational corporations that would end up hijacking the fundamental democratic rights and freedoms of peoples all over the world.[40]

As they stand, such views are hard to take seriously, because they greatly overstate the significance of the MAI – even as it was originally conceived, before dilution set in. Independently of the MAI, however, there could be a question as to whether, in part because of the trend in policies across the world towards making economies more open to inward FDI, multinational companies have now become dangerously powerful. This is the main theme of a recent volume produced by a leading American NGO, the Sierra Club, from which the two following assertions are taken:

> … transnational corporations (TNCs) have consolidated their power and control over the world … . In effect, what has taken place is a massive shift of power, out of the hands of nation-states and democratic government and into the hands of TNCs and banks. It is now the TNCs that effectively govern the world.
>
> Enormous economic power is now being concentrated in the hands of a very few global corporations relieved of constraints to their own growth.[41]

Such views, though widely held, are without foundation. The idea that multinationals could be the main threat to democracy and personal freedom appears strange, if not ridiculous, in the light of past history and current evidence. At present, multinationals are scarcely to be found, and are entirely without influence, in such countries as Afghanistan, Cuba, Iran, Iraq, Libya, Myanmar, North Korea, and the Sudan; and these are precisely the countries where intolerance, repression and authoritarian rule are most evident. Equally, and going further back, multinationals were not to be found in the former Soviet Union in the days of Stalin and Brezhnev, in the satellite communist countries of Central and Eastern Europe over the period from 1945 to 1989, nor in the China of Chairman Mao. On the other hand, in a number of countries where outstanding progress has been made in recent years towards greater democracy and wider personal freedom, this has gone together with both privatisation and new opportunities for foreign investors: the list here includes Argentina, Poland, Hungary and the Czech Republic.

As for the economic power that multinational firms may have – for instance, to set prices or restrict entry – the most effective curb on its exercise is competition. This is exactly what a liberal foreign investment régime promotes, since it gives opportunities – though without conferring special favours – not only to particular foreign investors but also to

40 Towards a Citizens' MAI: An Alternative Approach to Developing a Global Investment Treaty Based on Citizens' Rights and Democratic Control', a report prepared for the Council of Canadians by the Polaris Institute (Canada), p 3.

41 Jerry Mander and Edward Goldsmith (eds), *The Case Against the Global Economy*, San Francisco, Sierra Club Books, 1996. The first quotation is from a chapter by Tony Clarke (p 298), and the second from a chapter by David Korten (p 26).

their actual or potential competitors. More broadly, it is because of the pervasiveness of competition in a market economy and an open international economic system that the statement just quoted from the Sierra Club volume, that multinational firms are 'relieved of constraints to their own growth', is false.

In this perspective, competition appears as a positive element. This is of course the official view taken within the European Community, where the creation of the Single Market, with freedom for capital flows as a central feature of it, was explicitly designed to promote greater dynamism across the Community through opening up national markets, and where a Directorate-General of the Commission is specifically charged with the task of maintaining and promoting competition in the Community as a whole. It is therefore bewildering that, in its Resolution on the MAI already referred to, the European Parliament should take the view that:

> … the aim of an MAI should be to prevent ruinous [*sic*] competition between investors which would be harmful to the populations concerned.

In point of fact, no investment agreement ever signed or contemplated, including the many where EC member countries were involved, has subscribed to such an aim.

For some, a more direct threat which the multinationals pose is to national sovereignty. A recent example is an Australian commentator on the MAI, who argues that these firms

> … make no secret of the fact that they view national sovereignty as an outdated nineteenth century concept. What they seek is a borderless world, and this, to a large extent, is incompatible with the continued existence of both parliamentary democracy and national sovereignty.[42]

No evidence is cited, and no source quoted, to support these wild assertions about the views and aims of multinationals. Since a borderless world neither exists nor is in prospect, concerns about its impact on sovereignty may be premature. My own view, for which history provides some support, is that full freedom of both trade and capital flows would present no threat whatever to parliamentary democracy. Furthermore, it might well leave unaffected the central political role of national states: these states, if they chose, could continue to run their own affairs in such matters as defence, foreign policy, constitutional arrangements, legal systems, cultural concerns, education, residence, citizenship, electoral systems and voting rights, and the status of the national language.[43]

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42 Colin Richardson, 'The Multilateral Agreement on Investment', *Dialogue*, Vol 17, No 4, 1998.

43 The argument that power is passing from national states to multinational firms is to be found in the late Susan Strange's book, *The Retreat of the State: The Diffusion of Power in the World Economy,* Cambridge, Cambridge University Press, 1998. But her case rests on a highly questionable conception of power in which it is 'gauged by influence over outcomes' (p 53). So broad a definition blurs the critical distinction between the exercise of coercion, whether by states or other agencies, and those influences on events which do not directly constrain freedom of choice. In any case, now as in the past, serious political and economic outcomes are rarely decided through the influence of business firms alone.

Anti-liberalism: the multinationals as unduly favoured

Two milder variants of the criticism that the MAI would have conceded too much to the multinationals are to be found. One is the argument that such a treaty would have conferred new rights on foreign investors without providing for corresponding obligations. Here again, by way of illustration, is the European Parliament Resolution, which expresses concern that the draft MAI

> … reflects an imbalance between the rights and obligations of investors, guaranteeing the latter full rights and protection while the signatory states are taking on burdensome obligations which might leave their populations unprotected.

Although often voiced, this idea has no basis. Generally speaking, what foreign investors would have gained from the MAI would have been not much more than an enlarged freedom to enter new markets, and to operate there on the same basis as national firms, through the fuller extension of the national treatment principle. The end-result of such a process is no different from that already largely realised within the European Community. Just as the completion of the Single Market has not simply imposed 'new burdensome obligations ' on EC member countries – if this were the case, what made them sign up to it? – so the MAI held no such dangers for the participants. As for the 'full rights and protection' guaranteed by it, these for the most part were no different from what was available, as a matter of policy, to domestic firms: both sets of businesses, domestic and foreign-controlled, would be subject, as now, to the same (national) laws and regulations.[44]

Surprisingly, one of the critics here is Professor Jagdish Bhagwati, who has argued that the MAI

> … is conceived as a set of rights for corporations, instead of systematically including also their obligations. The latter would also require that notions such as the 'stakeholder' obligations of corporations to the communities they operate in should also be laid down in the agreement.[45]

What this might mean is unclear. If 'stakeholder obligations' should be 'systematically' included, presumably in writing, in investment agreements affecting foreign-based enterprises, why should they not apply equally to domestic firms? Why should they not then form part of the legal and regulatory framework which governs the conduct of both sets of companies? Just what are the obligations, if any, that should be enforced, distinctively and exclusively, and – for the first time in history – through an international agreement, on newly-entering foreign-based corporations?

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44 The qualifications ('generally' and 'for the most part') need to be made, because the possibility emerged that under the MAI foreign investors might be able in certain situations to bring actions and claims for compensation which would not be open to their domestic counterparts. This, however, was no part of the negotiators' intentions.

45 Letter to the *Financial Times*, 22 October, 1998.

A second variation on the theme of undue favouritism, equally misleading, is to be found in the submission made to the Joint Standing Committee on Treaties by the Australian Council of Social Service (ACOSS). The Council quoted with approval the observation of a Canadian professor, Marjorie Griffith Cohen, who had written that:

> Canada could show leadership internationally by not simply supporting the needs of only international business, but the needs of the people of the world as well.

The ACOSS witness described this as 'a central idea of great importance'; but in fact, 'innocence' would have been a more fitting term to have applied. From her remarks, it would seem that the possibility had not crossed Professor Cohen's mind that the interests of people and businesses might coincide – that in a competitive market economy businesses, whether national or international, make profits, and can only continue to make profits, by providing goods and services that people wish to buy of their own choice, and that 'the needs of the people of the world' may be better served through the wider choice and lower prices which are made possible by removing barriers to free entry.

The anti-liberal views so far cited are characteristic in particular of the NGOs and of hostile parliamentarians and commentators. When it comes to the two remaining headings, however, the case for departing from liberal precepts has wider support, in official and business circles as well.

Anti-liberalism: the arguments for discretionary policies

As noted already, the main aim of the MAI, as with other investment agreements, was to bind governments – to limit their freedom of action in ways that are designed to make their economies more open and their treatment of businesses less discriminatory. As against such an aim, it can of course be argued that it is in the public interest for governments, each in its own way, to retain discretionary powers, including the power, in appropriate and defined circumstances, to discriminate against foreign investors, to control cross-border capital flows, to offer tailor-made packages of investment incentives and performance requirements, and more broadly, to influence directly the pattern of output and investment in conformity with national objectives. While such a position may be combined with hostility to multinationals, as is the case with many NGOs, there need be no such link. As has been seen, the present French government, while against the MAI because of what it saw as an unacceptable intrusion on sovereignty, itself maintains a generally open investment régime and has explicitly endorsed the idea of a wider multilateral investment agreement within the WTO. Other OECD governments likewise accepted the role of multinationals and the general case for investment liberalisation; at the same time, however, while not coming out against the MAI, they insisted, like the French government, on keeping residual discretion through the lists of reservations that they submitted.

Much the same general case for discretion and the retaining of sovereignty was made in stronger terms by NGOs, chiefly on behalf of the developing countries. To quote one of the NGOs in question:

> … the task of building new industries cannot be left to the free interplay of global market forces. Accession to the MAI would preclude the poorest countries from adopting policies that have been used extensively by those countries that have previously attained higher living standards. Without the ability to use discretionary policies to diversify their economies, the poorest countries risk being locked into a marginalised position in the world economy as suppliers of cheap raw materials and low cost labour.[46]

Some NGOs also argued for greater autonomy in these areas for lower levels of government, with countries like their own in mind: their objections to closer economic integration applied within as well as across national boundaries.

Issues of industrial policy form a vast and highly contentious subject, which falls outside the scope of this paper. However, it is worth noting three related reasons for scepticism about the benefits of discretionary measures.

1. Lessons of history It is true that many of the core OECD countries in the past pursued, more strongly than today, industrial policies which would have been ruled out, or open to question, under MAI-style rules. But it is not evident, though often taken for granted, that these policies served their interests well. In Britain for example, activism of this kind had damaging results, in particular (though not only) when it took the form of 'building new industries' (to use the NGO phrase just quoted): examples are aircraft, nuclear reactors, aluminium smelting, and computers. For Japan, it is not clear that the outstanding economic performance of the post-World War II decades owes much if anything to official interventionist policies: arguably, the impact of these on the economy as a whole was slight, and on balance negative rather than positive.[47] Going beyond the core OECD group, the same may be true of other East Asian countries where discretionary policies have been followed. As Ian Little has noted, those who refer to the success of these policies

> … give no evidence of high social returns. They seem to think that it is enough to show (a) that there was a good deal of specific intervention in Korea and Taiwan in favour of particular industries, and (b) that some of the promoted industries survive and export.[48]

More broadly, there is no good reason to think that discretionary industrial policies are either necessary or especially appropriate for countries in the early stages of economic development. On the other hand, it may well be that the costs of such policies are higher in the world of today, in which the scope for cross-border trade and investment, and the potential benefits from freeing them, are greater than they used to be.

2. Illusions and reality of protection Those who advocate discretionary policies are apt to take it for granted that the activities thus favoured are of special value or merit. Often, however, a closer look casts doubt on this assumption. A case in point is the

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[46] Barry Coates, *The Developmental Implications of the MAI: WDM Critique of the Fitzgerald Report*, World Development Movement, July 1998.

[47] This is the view taken in Ramesh Ponnuru, *The Mystery of Japanese Growth*, London, Centre for Policy Studies, 1995.

[48] Ian Little, *Picking Winners: The East Asian Experience*, London, Social Market Foundation, 1996.

protection for cultural industries which many OECD countries offer, and which, in the context of the MAI, was a leading issue for Canada and France. In announcing his government's withdrawal from the MAI negotiations, M Jospin repeated the well known formula that cultural activities are not to be viewed and judged in commercial terms: '*Les biens culturels ne sont pas des marchandises*'. Here as elsewhere, cultural protection is seen as giving judicious and effective expression to higher ideals than those of the market-place.

Reality may be different, and a recent article on European film policy by Professor Patrick Messerlin takes as its sub-title the title of the Jean Renoir film, *La Grande Illusion*.[49] The following illustrative quotations from the article relate to the situation in France.

> When is a film French? The answer is astonishing: a film is French when it has received French subsidies (p 11).
>
> Roughly 80 major types of subsidies are available for film production – indeed, the film industry seems to be the only French industry to have a book entirely devoted to explaining and describing all of the subsidies available to it (p 15).
>
> When supporters of the quotas and subsidies say that these instruments work, they simply mean that quotas have been enforced and subsidies have been spent … [but] these instruments, even when zealously enforced, as in France, have not produced the effects desired by their supporters (p 18).
>
> Being protected from American films, French film-makers have tried to direct and produce quasi-American films … . French film policy has led to an accelerated 'Americanisation' of French film production – from soap operas to sitcoms for teenagers and hard thrillers (p 20).

While the case of the French film industry may be more absurd than most, it is entirely normal for discretionary policies to involve complex bureaucratic processes, unintended side-effects, and single-minded rent-seeking on the part of economic agents. This reinforces the case for rules, even though they impinge on sovereignty if that term is to be identified with the exercise of discretion. Another element in the case is that discretionary policies carry with them risks of bias, favouritism and corruption. The sovereign right of governments to give way to sectional pressures, or to continue to engage in cronyism, is not a principle worth defending.

3. The power of do-it-yourself economics Even where governments are well-intentioned and disinterested, they may be drawn to unwise interventionist policies by strongly held but mistaken intuitive economic ideas and beliefs.[50] As it happens, issues relating to FDI flows and the impact of multinationals provide a conspicuous and long-running example of this widespread phenomenon, and there is a moral here which is relevant to MAI-style investment agreements.

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49 Patrick Messerlin, 'European Film Policy: *La Grande Illusion*', *Trade Policy Review 1996/97*, London, Centre for Policy Studies.

50 This phenomenon, much underrated by economists, is the theme of David Henderson, *Innocence and Design: The Influence of Economic Ideas on Policy*, Oxford, Blackwell, 1986, and is further discussed in *The Changing Fortunes of Economic Liberalism*, *op cit*, pp 59–63.

In 1967 the French author and journalist, Jean-Jacques Servan-Schreiber, published a book called *Le Défi Américain*.[51] His message was accurately summarised as follows:

> … Europe is falling into economic decadence because American firms dominate "key" areas like computers, electronics, space technology and aviation. They do this largely because the American government spends large sums subsidising them. Unless European governments respond to this "challenge" by jointly financed projects on a similar scale, [there will be] a future for Europe "outside the mainstream of history, leading a life without vitality or purpose".

Europe, according to the author, had already become 'an economic colony of the United States'.

In a justly dismissive review, from which the above quotations are taken, Angus Maddison described Servan-Schreiber's book as a 'science-fiction phantasy'.[52] Yet it proved a best-seller, not only in France, but across Europe and even beyond. It voiced ideas which were widely held, and which formed part of the characteristic thinking of European political leaders, top officials, senior business executives and commentators on public affairs. As time went by, the argument was extended, so that Japan as well as the United States was seen as a threat to the prosperity, even the viability, of Europe. For many, this line of thought, even though it had (and has) no basis in reality, provided the main single argument in favour of closer union among the member states of the European Community. Though less influential than it used to be, it is still in circulation.

If the advocates of a pan-European industrial strategy had had full scope to put their ideas into practice, an array of costly large-scale ventures might have gone ahead, while Community trade policies would have been less liberal. In practice, however, there has been a damage-limiting factor, in the form of constraints on the freedom of member governments and the Commission to launch Community-wide initiatives with public money, and to create protected 'European champions'. Largely as a result, the Community has been spared the full consequences of ambitious centrally directed policies founded on illusions.[53] The discretionary powers of both the Commission and the member governments were hedged round by rules of conduct which they themselves had shaped or accepted – in budgetary policy, competition policy, trade policies, and national treatment undertakings. In just the same way, the rules and disciplines that investment agreements incorporate may serve as restraints on misapplied discretion.

Anti-liberalism: the demand for international norms and standards

As noted above, the draft MAI agreement acquired over time a stronger emphasis on environmental and social aspects. Most member governments were content with this, and some, including in particular the US, wished to go further. A few governments –

51 Translated into English under the title, *The American Challenge*, London, Hamish Hamilton, 1968.

52 The review was published in the *Economic Journal* for September 1968.

53 In one area of policy, however, this situation may now change, if the idea of creating 'European champions' in the defence industries, through politically enforced mergers, should come into effect.

Australia, New Zealand and Mexico in particular – stood out against the majority, arguing that the right places for prescribing environmental rules and standards, and procedures for enforcing them, were the specialised agencies or agreements concerned – such as the International Labour Organisation (ILO) and the various multilateral environmental agreements – rather than an agreement concerned with FDI flows (or, for that matter, with international trade). Outside, many NGOs contended that the MAI would bring with it risks of lower standards, and of creating obstacles to raising them: they wanted higher standards built in, with foreign investors especially in mind. As one of them put the argument:

> Until domestic environmental substantive and procedural standards can be harmonised, international rules and mechanisms will be necessary to hold MNEs [Multinational Enterprises] accountable.[54]

Here as elsewhere, the draft agreement was assailed from different directions. But virtually all parties to the debate, despite their differences, shared a basic assumption which from a liberal viewpoint is open to question. They were and are in favour of 'higher' standards of environmental protection, and of terms and conditions of employment, to be embodied in regulations which have international as well as national scope and force. Across the spectrum of views, albeit in different forms and degrees, progress is seen in terms of ever-tighter regulations increasingly binding on all.

Both aspects are open to question – the stringency of norms and standards, and their universal application. It is not difficult to think of cases in which insistence on what appear as higher standards could be misguided. In the environmental sphere, arguably, a current example is the proposal now under discussion in the United States, to reduce pollution by tightening the National Ambient Air Quality Standards for Particulate Matter from 10 microns to 2.5: it could well be that, when all effects are taken into account, this particular 'raising' of standards would do more harm than good. As to labour standards, it is almost certain that the recent introduction in France of a statutory 35-hour week as from the year 2000 will have damaging effects on balance, and if the figure had been fixed at 34 hours the prospective net losses would be greater.

To insist on the same standards everywhere is likewise a way of making people worse off. Countries differ widely in their situation – in their physical and geographical characteristics, in levels of income per head, and in the tastes and preferences of their people; and environmental legislation should be allowed to reflect these differences, at any rate in so far as the problems are local and not cross-border. In the same way, imposed uniformity of wages and terms of employment brings with it avoidable losses, because it closes off the possibility of a whole range of mutually beneficial deals and arrangements. A case in point is Germany, where following unification employment opportunities in the eastern *Länder* have been destroyed on a large scale by the statutory elimination of wage differences. In the European Community generally, the provisions

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[54] World Wildlife Fund, 'Is the Multilateral Agreement on Investment Sustainable?', Geneva, 1997, p 7.

of the Social Chapter are likely to bring effects of the same kind. Integration is not to be identified with uniformity, and enforced uniformity may be, as in these cases, a force for disintegration.

The point is often made, and with good reason, that attempts to enforce minimum standards internationally may be prompted by the desire of businesses and workers in richer countries to raise the costs of their competitors elsewhere: imposed norms and standards are seen as a protectionist device. The more fundamental objection, however, lies not in their motivation but in their effects. They lead to impoverishment, by reducing economic freedom and depriving people of opportunities. Hence the tendency of all those concerned with the MAI, to endorse uncritically the further tightening and extension of environmental and social regulation, is not at all a sign of progress.

Making the liberal case

A feature of the MAI debate was that the opposition made virtually all the running. In part, this can be explained by the two factors that have already been noted: on the one side, the zeal and enterprise of the NGOs; and on the other, the gradual ebbing away of support for the MAI as it became increasingly watered down. However, there is another aspect of the story. Despite their many weaknesses and exaggerations, the hostile arguments of NGOs and other opponents were not forcefully countered. Neither OECD member governments nor the Organisation itself have made effective rejoinders, nor have the multinationals and the organisations that speak for them. Neither governments nor businesses have fully applied themselves to the task. Others too have been unheeding. For instance, the *Financial Times*, whose editorials consistently argue the case for free trade, poured scorn on the MAI initiative at the final stage[55] – not without reason, but missing altogether the key point that the manner and causes of its demise have disturbing implications for external liberalisation generally, and for the WTO as well as the OECD. This combination of passivity, myopia and lack of resourcefulness in the liberal camp has been a depressing aspect of the story.

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55 In a leading article, headed 'A Case of MAI Culpa', 20 October 1998.

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LOOKING AHEAD

Historians are apt to view the past in terms of two contrasting elements, continuity and change. In assessing the significance of the MAI episode, there is a place for both.

How much has changed?

The failure of the negotiations was clearly a setback for the OECD Secretariat, for the Organisation as a whole, for the national officials who had constituted the Negotiating Group and the departments from which they came, and for OECD member governments which found themselves in disarray and were forced to abandon an initiative that they had publicly sponsored. The question arises as to whether it is also, and much more significantly, a setback for the cause of liberalising not only FDI flows but international transactions more generally. Is it possible that the end of the MAI episode marks a turning point in the evolution of the external economic policies of the OECD member countries, perhaps as part of a more general reaction against 'globalisation'?

The main reason for taking such a view is the strength of the opposition to the MAI and the emergence of the NGOs as a force to be reckoned with. In terms of organisation, and in its impact on governments and public opinion, the 'stop the MAI' campaign was a notable success. It has also set a precedent. What may be significant for the longer term is the way in which the NGOs have now asserted a claim to involvement, through formal consultations and even direct participation, in the process of making official policies at national level and in international fora, a claim which up to now has not been effectively disputed. Since almost without exception they are either deeply hostile to economic liberalism or concerned to limit what they see as its excessive claims and its undue hold on the governments of today, the prospect that their influence will grow does not augur well for the further liberalisation of international trade and capital flows in the years ahead.

A second and related aspect of the MAI negotiations was the increasing tendency for governments to insist on the inclusion of clauses relating to environmental and social standards. This too may be a portent, for trade flows as well as investment, given the clear possibility that such provisions may introduce new anti-liberal elements into the system.

It remains to be seen how far these and other influences working in the same direction will make themselves felt. On present evidence, it appears that despite them the MAI episode is not to be seen as a turning point. The winding-up of the negotiations marks only the failure of an attempt to accelerate the process of liberalisation in one area of international transactions in one particular venue of negotiations. For the time being at any rate, its significance goes no wider than that.

As to the immediate impact, the decision to call off the negotiations is important as a symbol rather than for its actual consequences. Notwithstanding the highly-coloured portrayals of it by many of the opponents, the MAI – even as originally conceived and before the process of dilution set in, and still more in its final phase – did not in fact represent a dramatic new advance towards a liberal international economic order. True, it proved too ambitious, too overloaded, for OECD governments to accept; but this reflects as much on their continuing lukewarm and qualified liberalism, and the attitudes of their voters, as on the objectives that were set. As noted above, even the full MAI would have largely excluded taxation issues, while in some respects it would have gone no further than, or even not so far as, established and accepted provisions of the European Community, NAFTA, the Energy Charter, and a good many BITs. In any case, as the talks went on, dilution set in. On such issues as performance requirements, investment incentives, dispute settlement procedures, and lists of and claims to exceptions, OECD governments in the event showed themselves unwilling to move far collectively in the direction of more binding rules and obligations. Indeed, if later reservations proposed by some countries had been accepted by all, a final diluted MAI might have brought a retreat from ground that had been won for liberalism long before, within the OECD Codes of Liberalisation.[56] Those who maintained that, from a liberal standpoint, little would be lost by forgoing the MAI in what seemed likely to be its final form, had an arguable case – all the more so, if the increasing emphasis on environmental and social standards is taken into account.

This of course is a commentary on the policy stance of the OECD governments. But in judging this stance, one has to look at developments over a longer period, and over a wider range of issues. Viewed in this perspective, it is the element of continuity that appears as dominant. This can be seen from two contrasting points of view.

First, the positions taken with reference to the MAI form part of a long-established approach and pattern of behaviour on the part of the governments concerned: it is not just in the context of the MAI that heavily qualified liberalism has been, and continues to be, the order of the day. Trade policies provide a clear example of this. Despite the many and cumulatively far-reaching steps that they have taken over a long period towards free trade, all the OECD countries (many of them of course collectively, through the European Community) continue to operate forms of highly illiberal selective protection. This is to be seen in agriculture, textiles and clothing, steel, automobiles, and semi-conductors; in many if not most services; in government procurement practices; in a variety of industrial subsidies including investment incentives for foreign investors; in the enforcement of complex rules of origin that have become more pervasive as a result of the spread of regional integration agreements; and in actions, and the threat of actions, under anti-dumping legislation. The kinds of reservations that OECD governments made in relation to the MAI were consistent with their general thinking and practice in relation to cross-border transactions. Their conduct in the negotiations does not represent a break with the past.

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56 Such a possibility is to be seen in the strong French opposition, in the Lalumière Report and the statement of M Jospin, to a 'ratchet' mechanism.

Second, and notwithstanding the many remaining limits and qualifications, the general commitment on the part of OECD governments to liberalisation, now increasingly shared by others, is still in force. This is clear from recent events. In the great majority of countries, including all the OECD members, the trend to more liberal external economic policies has been broadly maintained during the period since the MAI negotiations were launched; and it is especially to be noted that over these past few years *the further freeing of* FDI *flows has gone ahead across the world*. This process of investment liberalisation has been taken forward through a range of unilateral, sectoral, bilateral, regional and even multilateral measures. There are few if any indications that, as a result of or in conformity with the failure of the MAI, it has been halted or even slowed.

Here again, the cases of both France and Australia can serve as illustrations within the OECD group. In France, as noted above, a substantial freeing of FDI flows from countries outside the European Community was effected in early 1996, so that for most investments screening is now little more than a formality. Since then, under governments both of the right and the left, privatisation and deregulation have gone ahead in ways that have further widened the scope for foreign participation and investment. In Australia also, privatisation has been continuing, in particular of electricity and transport systems within the States where few if any restrictions have been placed on foreign ownership. At federal level, the government in early 1997 announced the removal of the previous prohibition on a foreign takeover of any of the four major banks, while an opening up of the domestic aviation market now seems likely.[57] In neither country, despite strong official reservations concerning the MAI, is a departure from the generally liberal orientation of investment policies – or trade policies, for that matter – in prospect. Both governments, along with the other OECD members, have explicitly stated their continuing support for the goal of an improved multilateral framework for investment.

Beyond though including the OECD group, the same continuing orientation of policies is to be seen in:

- The growing number of BITs, more than 150 of which were concluded in 1997
- The number of countries (76 in 1997) introducing changes in their investment régimes, of which the great majority appear to promote liberalisation
- The further development of regional investment agreements, in both America and Asia
- In the WTO, the conclusion of agreements within the GATS on basic telecommunications services and financial services, both of which provide for new commitments on market access for foreign investors.[58]

Three mutually reinforcing influences, all well established and currently at work, are likely to go on providing momentum to the further freeing of investment régimes across

57 However, the statement of policy with respect to the banks included a reaffirmation of the doctrine that 'any large scale transfer of Australian ownership of the financial system to foreign hands would be contrary to the national interest'.

58 These various developments are described in UNCTAD (1998), *op cit.*

the world. These are: the continued rapid growth, and wider spread, of FDI flows; the further advance of privatisation and deregulation; and a gradual cumulative erosion of national concerns about the status of 'sensitive' industries, so that governments and public opinion become more willing to allow foreign presence and ownership where it is still restricted or closed off.[59] In addition, it is probable that, within federal systems where investment flows are now impeded by policies that operate at state or provincial level, there will be moves, also gradual, towards the establishment of a true single internal market.

Admittedly, this world-wide process of further opening-up will be untidy, uneven, long drawn out and subject to local interruptions and setbacks. It may also be accompanied by a continuing and even growing use of investment incentives which are open to question from a liberal point of view: up to now, it is only within the European Community that a systematic attempt has been made to deal with this issue. Again, moves towards mandatory international norms and standards may introduce new elements of disintegration. All the same, the present orientation of external economic policies, in which the balance is tilted, albeit uneasily, towards liberalism rather than interventionism, seems likely to continue to prevail.

Hence the failure of the MAI does not signify that the long-term trend towards more liberal trade and investment régimes in the OECD countries, and the similar though generally more recent trend elsewhere in the world, are about to be reversed. Viewed in the light of past history and recent developments, the fate of the MAI is not *in itself* a portent of change; nor indeed, except for the OECD as an organisation, does it appear as an important event.

A range of options

Now as earlier, governments can move to establish more liberal investment régimes through a variety of means and channels.

The failure of the MAI means that, for the time being, multilateral negotiations relating to rules for investment flows are unlikely to go ahead. There is little prospect of restarting the process in the OECD, while the notion of 'transferring' it to the WTO appears unrealistic, given the difficulties which the OECD governments ran into with the MAI and the fact that there is still an insufficient basis of agreement among the WTO membership generally for such a transfer to be attempted.

Before a negotiating process relating to new investment rules can be established in the WTO, a great deal of further exploratory and preparatory work will have to be done, and there is now not much time for this before the ministerial meeting that is due to take place in Seattle in November 1999, with the possibility of launching then the new 'Millennium Round'. Prolonged discussions within the WTO working group on trade and investment issues, established at the end of 1996, have revealed continuing divisions

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[59] To put this point in MAI terminology, one would expect the number and intensity of 'country-specific reservations' to fall over time.

which will not be quickly resolved: indeed, the scope of the work has been restricted to analytical aspects, with discussion of negotiations ruled out. At the same time, there is pressure for negotiations to be set in train in a new Round, notably from the European Community and Japan. The most likely outcome is that some general formula will be found at Seattle, clearing the way for negotiations on investment issues to be included within the Round without being too specific about the form that they might take.[60]

A long process is thus in prospect within the WTO – first in determining a basis for negotiations on investment, and then in trying to pursue them to a successful conclusion. The MAI failure makes it even clearer than before that agreeing on rules for cross-border investment remains a highly complex and contentious undertaking, especially when a large number of diverse and geographically scattered countries is involved and if the initial goals prove to be over-ambitious.

As in the past, however, multilateral negotiations are only part of the story – and for the time being at least, not an important part. For one thing, they are not relevant to the leading cases of China and Russia. It is here that the potential gains to both parties from a more assured status for inward FDI are probably greatest; but since neither country is as yet a member of the WTO, it is only through other channels that progress can be made. For the world as a whole, while exploratory and preparatory discussions within the WTO are taking place, action to permit or encourage FDI flows will be going ahead, as now, on many other fronts – through a variety of regional agreements, in newly-signed BITs, through direct negotiations between the European Community and the United States, and by national governments acting unilaterally, in some instances in discharge of their obligations under the OECD Codes. It is probable that the trend towards liberalisation will be maintained through all these channels, pending the time when it becomes possible for new agreements to be reached in the WTO.

This is not to undervalue the gains that might come from successful negotiations within a new WTO Round. With international investment flows as with trade, it is a multilateral system of agreed rules which offers the surest means of giving effect to the principle of non-discrimination, and in particular, of protecting the position of small countries and those that are not members of strong regional integration agreements. It is therefore to be hoped that the movement of opinion in developing countries will continue, so that governments such as those of Egypt, India and Malaysia will become ready to take part in negotiations on a broad front and with the agreed aim of further liberalisation.

For this next stage in the evolution of policies, a clear responsibility falls on the OECD member countries, including especially the United States and the European Community, precisely because of their failure to bring the MAI negotiations to a useful conclusion. It is for them to restore momentum. As already seen, they have restated their commitment

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[60] One possibility for the WTO, which has been suggested by Richard Snape, is that all investment aspects should be brought within a separate self-contained and comprehensive agreement, for which the obvious model would be the NAFTA. As a result, the GATS would lose its investment-related provisions, and would be confined to arm's-length trade in services. (Richard H Snape, 'Reaching Effective Agreement Covering Services', Chapter 10 of Anne O. Krueger (ed), *The WTO as an International Organization*, Chicago and London, Chicago University Press, 1998).

to the goal of establishing a multilateral framework of rules for investment. In this next stage, a genuine commitment implies more than just lending general support to the idea of a Millennium Round with an investment component attached to it. Through their own actions they can help to prepare the ground for negotiations within the WTO, and increase the likelihood that these will bear fruit, (i) by moving ahead themselves with further measures of liberalisation, and (ii) by confronting and making progress with leading issues, which they found themselves unable to resolve within the MAI process. While actions on these lines may well involve negotiations, there are other dimensions also.

Beyond negotiations: the role of the OECD

Just as national policies may be decided without reference to negotiations, and negotiations need not be multilateral, so international economic cooperation, here as elsewhere, is not to be viewed in terms of negotiation alone. While negotiations act as a focusing device, and are a necessary condition for agreement between governments, they are also a constraining factor since tactical considerations are ever-present. There is a place for discussions, reviews and exchanges, as also for inquiries and commissioned studies, which are independent of the conduct or prospect of negotiations, and where new formal commitments, agreed resolutions or even communiqués are not in question. It is here especially that the OECD has a continuing role.

The outstanding example is the Organisation's work on agriculture. The OECD has become the standard source of authoritative data, and of informed and independent commentary, on the evolution of member countries' agricultural policies; the locus for multilateral surveillance of those policies; and the main forum in which member governments consider and exchange views on the implications of possible reforms. This provides a firmer basis for the reform of policies that are recognised as highly distorting, and for cross-border liberalisation of agricultural trade, even though only member governments can decide actual measures and such decisions are unlikely to be taken in the OECD.

In relation to investment issues, there are four main forms of activity which remain suited to the Organisation.

- It should continue and extend its procedures, which were instituted only a few years ago, for reviewing in published documents foreign investment trends and policies in both member and non-member countries.
- In this connection, it should examine the possibility of developing systematic comparisons of the extent to which different foreign investment régimes are open and liberal, if possible with quantitative indicators, on the lines of the Organisation's path-breaking work on comparative measures of agricultural support. Progress in this admittedly difficult task would be useful not only in itself, but also as an input into discussions and negotiations at the WTO.
- It should resume the task of taking further the Codes of Liberalisation and the National Treatment instrument, which – contrary to what was sometimes suggested, at the stage

when the MAI was being talked up – are still useful channels for further liberalisation (sometimes through negotiation). Where non-member countries are willing to accept the disciplines involved, they should be admitted to membership of the Codes and of the two committees concerned (CMIT and CIME).

- In and through these and other committees, working where appropriate in conjunction with one another, the OECD should undertake by agreement studies of some of the topics and issues which the MAI negotiations have revealed or confirmed as not only difficult and contentious but also subject to argument concerning the facts and the lessons of recent experience. The list of such topics could include the working of dispute settlement mechanisms in investment agreements, performance requirements, investment incentives, reciprocity arrangements, and the extension of rules and disciplines to lower levels of government – as well as taxation matters, in which the Organisation has had a long involvement. For reasons noted in the Annex, the list of participating committees should include the Economic Policy Committee.

None of these investment-related activities is new, but all could be further developed, in particular through a greater involvement of non-member countries. They should form part of the wider attempt, now in fact being made, to involve non-member countries in a range of meetings, reviews, exchanges and inquiries, normally though not necessarily outside the framework of negotiations. This is chiefly in the context of the Organisation's continuing primary role in helping to promote the further liberalisation of international transactions, including both trade and capital flows.[61]

In relation to such concerns, the OECD and the WTO should develop closer working links, which at a minimum should involve more systematic exchange of information but could well go further. At the same time, and as the MAI affair itself suggests, the internal working of the Organisation itself is in need of overhaul with a view to realising greater coherence and effectiveness. This is not just a matter of the Secretariat: the problem extends to committees and national delegations as well.[62]

Action this day: what the OECD Ministerial Council should now say

By way of a specific proposal here, I offer my own suggested draft for the relevant section of the forthcoming OECD ministerial communiqué, where the MAI and investment issues are dealt with. The reader may derive some amusement by comparing this with the actual text which is due to appear on 27 May 1999. Another suggested paragraph, of

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[61] An alternative specification of the Organisation's *raison d'être* was suggested in late 1997 in the commissioned report of an unofficial High Level Advisory Group on the Environment, which recommended that the principle of 'sustainable development' should become 'the way of ordering and approaching all other issues on the OECD's agenda'. Not surprisingly, some NGOs have endorsed this idea. However, since the Advisory Group was unrepresentative as well as unofficial and the report itself is best forgotten, not much seems to have happened as a result. This initiative seems in fact to have been an error of judgement on the part of the OECD's top management.

[62] Both these aspects – the more effective functioning of the OECD, and its relationship to the WTO – are further explored in David Henderson, 'International Agencies and Cross-Border Liberalization: The WTO in Context', Chapter 3 of the volume edited by Anne Krueger and referred to in footnote 60 above. This essay is drawn on below, in the Annex.

key importance, will be presented later, since the issues it deals with go wider than investment. On the latter topic a suitable post-MAI text could read as follows:

1 As part of our continuing support for the open multilateral trade and investment system, we endorse the goal of developing a multilateral framework of rules for cross-border investment flows. We will work towards the achievement of such a framework.

2 This is no simple task. The recent attempt within the OECD to arrive at a comprehensive Multilateral Agreement on Investment has failed. Too much was attempted. This is not the time to reopen these negotiations. Rather, we should draw from them lessons for the future.

3 We consider that the question of rules for investment, and a possible new investment agreement, should form part of the agenda for the proposed new round of negotiations within the WTO (the 'Millennium Round'), for which we have stated our support above.

4 To establish a firm and agreed basis for such negotiations within the WTO will take time, as then would the negotiations themselves. Several years may be in question. Meanwhile we ourselves intend to go further along the path of liberalising investment flows, and strengthening the framework of rules that bears on them, through actions by national governments and the European Communities – actions to be taken both individually, and in concert, and wherever possible in conjunction with non-Member countries.

5 Within the process of strengthening international rules for investment, the OECD has a continuing role. In particular, it should:

- Continue and take further its recently-instituted reviews of FDI, covering both Member countries and those non-Members – we would hope an increasing number – that wish to take part in this process of intergovernmental exchanges and surveillance
- Provide a venue at which, normally without commitment and outside the context of negotiations, Member and non-Member governments can review together topics of common interest, and exchange views and ideas, on investment issues and matters relating to them
- Strengthen further the Codes of Liberalisation, which should now be opened, both for participation in Committee meetings and for adhesion to the Codes, to all non-Member countries that are willing to accept the obligations involved
- Carry forward its long-established work on issues of international taxation.

6 In developing this programme of activities, the OECD should establish and maintain closer working links with the WTO.

7 Here as in other areas, there is a need for greater coherence in the OECD, both within the Secretariat and between Committees. We call on the Secretary-General to examine this aspect in conjunction with the Council and chairs of Committees.

The issue of participation

The MAI episode has raised in an acute form the question of how international discussions, consultations and negotiations are best conducted, and what should be the role and status within them of the NGOs, as also of organisations representing businesses and unions. The issue is not a new one. In various UN agencies, as also in the World Bank, there has been a growing tendency to bring NGOs into discussions, consultations, and reviews, and even in some instances into the process of negotiation. Recent events, and in particular the MAI episode, have involved the NGOs more closely with both the OECD and the WTO. As seen above, the OECD has held various consultations with them, and it plans to continue and extend these. In July 1998 the Director-General of the WTO announced measures to improve the Organization's information exchanges and consultations with 'civil society'.

This general tendency in international agencies has been endorsed and promoted by OECD member governments. At the GATT's fiftieth birthday celebration in May 1998, President Clinton called for the WTO 'to open its doors to the participation of the public', and the European Commission has said much the same thing. As seen above, the OECD statement of October 1998 referred to the need 'to engage in further discussions with representatives of civil society', including NGOs.

It remains to be seen how far this trend will be taken. One extreme suggestion is to be found in a speech last year by the Secretary-General of UNCTAD, Mr Rubens Ricupero. In his opening address to a conference convened by UNCTAD, he argued that the MAI negotiations

> … have demonstrated that a meaningful international agreement in this area requires that international investment discussions *and negotiations* involve *all those* affected by such an agreement. Not only representatives of governments should be heard, but also those from civil society who have a real stake in the outcome. This is the logical consequence of the internationalization of the domestic agenda (italics added).[63]

Before such a far-reaching principle is accepted, it is necessary to look more closely at the claims thus made on behalf of the NGOs and other non-official bodies, the validity of which is much more doubtful than Mr Ricupero implies.

One claim, which is more than just a matter of language, is that the NGOs have a legitimacy which does not extend to business groups, and which means that their status and views should be formally recognised by governments, because they alone are the authentic representatives of 'civil society' as a whole, and as such voice the true concerns of ordinary people. A milder version of the same idea is that these groups, in contrast to business organisations which are profit-oriented, and possibly but not necessarily (for there are dual standards here) those that speak for farmers and trade unions, stand for the 'public interest'. Both arguments are invalid. The whole notion of a 'civil society' which has claims of its own to represent and speak for the people of a country is

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63 Rubens Ricupero, opening remarks at the Regional Symposium for Asia on 'International Investment Arrangements and Their Implications for Developing Countries', held in New Delhi in July 1998.

misguided when that country has a democratically elected and responsible government: persons who are not elected, and not accountable to a duly elected and generally representative legislature, can have no such status.[64] Even more, the notion that there exists an 'international civil society', and that the NGOs speak for it, is doubly misleading. Further, the contention that because they do not represent particular economic interests the NGOs serve the interest of all is a bold claim indeed, given that in many cases, as has been seen, their ideas are dubious or wholly mistaken, and their advice, if taken seriously, would bring results that are arguably quite contrary to the interests of citizens generally and would be found unacceptable after the event.

This is not to argue that democracy is only a matter of elections, nor that the notion of 'civil society' is without meaning or value, despite the questionable use that is often now made of it. The point at issue is one of defining admissible roles and claims, and not accepting at face value pretensions that have little or no basis.

It is in relation to the issues of transparency, consultation and participation, including in particular participation in substantive meetings and negotiations, that these questions of status and legitimacy have practical import. For the most part such issues are for debate and resolution at a national level, but the conduct of business in international agencies is the aspect considered here, with particular reference to the OECD and the WTO.

One issue that immediately arises is that of recognition. For the OECD, and perhaps more widely, there are unresolved questions, which need to be considered carefully by member governments, as to the status, credentials and rights to representation of particular NGOs. These questions are closely linked with decisions as to procedures, and the terms of reference, membership and conduct of different meetings. These are not minor matters: a lot can go wrong if the choices are not well considered.

Underlying these questions of 'modalities' is the constitutional issue of the status and claims of non-governmental organisations generally, including representatives of business and unions. In both the OECD and the WTO, and I would argue more generally, there is a dividing line to be drawn between, on the one hand, making non-sensitive information widely and promptly available and offering opportunities for discussion and consultation, and on the other, providing for active participation.

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64 A contrary view is implied in the following remarkable passage from p 60 of the UNCTAD *Investment Report*, 1998, *op cit*:

> While civil society can be seen as a counterbalance to the state, both are inextricably linked. Civil society is a "work in progress" which, while existing throughout much of the world in different shapes and forms, at different levels of organization, capacity and strength, is a socio-political reality whose continuing expansion demands active support if the goals of development, democracy, and human rights are to be realized. In this sense, the building of civil society can be seen as an objective whose achievement must be purposefully and actively sought, in order to achieve wider economic, political and social goals.

It would seem that a variant of George Orwell's 'Newspeak' has been developed in UN circles in Geneva. Readers of Orwell's novel, *1984*, will recall that Newspeak is a language specially created by government to serve ideological needs and ensure conformity, designed progressively to replace standard English ('Oldspeak') as a means of communication.

Although cases vary, that of the OECD can be used as an illustration. As seen already, the Organisation has always had a process for formal consultation and exchange of ideas with both of the 'social partners', as represented in their respective committees (BIAC and TUAC). But neither of these committees has either asked for or been given the right to take part in the actual conduct of OECD business. Hence they are not represented in the many and wide-ranging formal committee meetings within the OECD, whether or not these involve negotiations (which normally is not the case); nor (though practice can vary) are they as of right kept continuously in touch with the proceedings and results of such meetings. This is not to say that outside participation in substantive meetings by non-officials is ruled out altogether. It is for each member government to decide for itself how it should be represented in intergovernmental committees and working groups; and particularly when technical issues are prominent, and in lower-level exchanges, it may well happen that experts who are not national officials are attached to delegations, and act as full members of committees. In some cases, such people may by agreement be nominated by outside organisations, as distinct from being chosen on a personal basis by the government concerned. But when it comes to higher level issues, and where political rather than technical aspects are involved, it is ministers or (more commonly) their officials who alone have the right to take part. Responsibility rests, as it should, with elected political leaders and those who are authorised, qualified and paid to act on their behalf and in support of their role.

This is not an argument against change. The NGOs, in the OECD as elsewhere, have made a case for being kept – along with others – more fully informed than in the past, and to being consulted and brought into discussion meetings, in ways that are still evolving and need not follow a uniform pattern. In a good many agencies, national and international, action on these lines has been taken: the time has probably come for a frank comparative evaluation by the agencies and member governments of results and lessons, the more so since making consultation and discussion processes more elaborate typically brings costs as well as benefits. Now and then, there may be a case for taking participation somewhat further. Since the precise boundary between discussions and consultations on the one hand, and substantive meetings including negotiations on the other, may not always be well defined, it would be too unqualified to argue that in no circumstances whatever should participation be extended to formal intergovernmental exchanges including the negotiating process. All the same, the line should be drawn, and drawn firmly. No non-governmental organisation, whether speaking for business enterprises, trade unions or professional bodies, 'public interest' concerns, or any other groups, has a valid claim in its own right to active participation in proceedings where the responsibility for decisions and outcomes rests, and has to rest, with the governments of national sovereign states.

It is in this sphere of procedures and demands for recognition that the MAI episode, when otherwise long forgotten, may prove to have had lasting and unfortunate consequences. Just as anti-liberal arguments have gone largely unanswered, so the excessive claims made on behalf of 'civil society' have in many cases been met by agencies and governments with a surprising degree of acquiescence or even support. In this, a variety of influences has doubtless been at work: they probably include spinelessness, inadvertence, active support within governments – in environmental and labour departments, for example – for NGO arguments and causes, and a broader feeling in political circles that 'participation' is a popular and vote-winning cause. Whatever the reasons, the outcome is a matter of concern, not just for the international trade and investment régime, but for the conduct of democratic government.

Ideally, and in the light of the MAI affair, the principles outlined above should be firmly laid down in this year's communiqué from the OECD Ministerial Council. My suggested wording for this key paragraph is as follows:

> In forming and deciding policies, whether at national level or in negotiations in different venues, there is scope for a somewhat wider process of public information, discussion and consultation than has been normal in the past. *But the responsibility for the conduct of substantive discussions and of negotiations should remain with elected governments and ministers, and with those who are appointed to serve and act for them in national and international agencies.*

A more general comment on political aspects will serve to round off this story and its lessons.

The political factor

The MAI initiative broke down for three main interrelated reasons: it tried to go too far, over too wide a front; the issues proved even more sensitive than had been expected; and outside opposition, again beyond early expectations, proved highly vocal and effective. All these can be brought together under a single heading: the agreement became politically unviable.

The circumstances of the failure mean that any new moves towards external liberalisation, in trade as well as investment, are likely to prove more controversial, and to face stronger opposition, than in the past. This need not preclude such moves: as noted above, the impetus to a further freeing of investment flows in particular is still to be seen across the world, and has so far been little affected, if at all, by the fate of the MAI. But if the impetus is to be maintained, with trade flows also included, the ground has to be better prepared, politically as well as technically, than it was in this instance. Political leaders have to be well briefed in advance, and persuaded of the case: it is not every such leader who comes into office with a mission to make trade and investment flows freer, as Bob Hawke did when prime minister of Australia and Jacques Delors as president of the European Commission. Governments that want to move ahead will have to be more explicit, and more visibly open, than in the past, both to make themselves better informed and to avoid the charge of concealment which was damagingly, though unjustly, made in the case of the MAI. Procedures for discussion and consultation need to be thought through and improved, while at the same time the integrity of the negotiating process has to be maintained. Both within and outside government, the case for a liberal approach has to be put more effectively, in different ways, at different levels, and in relation to the leading issues of the day. All these could be useful lessons, and eventual outcomes, of a venture that failed.

ANNEX

THE ROLE OF THE OECD IN EXTERNAL LIBERALISATION: TWO ASPECTS

The Codes of Liberalisation and the National Treatment instrument

The history here goes back a long way. Right from its creation in 1961, the OECD was assigned by its member governments an explicit role in helping to bring about a progressive freeing of cross-border flows of goods, services and capital. Liberalisation in these areas was and remains a shared objective of all members. In the exercise of this mission, the Organisation has developed procedures for pushing forward the liberalisation of international capital movements and trade in services, including especially financial services. The work is carried out through the two committees mentioned in the text, the Committee on Capital Movements and Invisible Transactions (CMIT) and the Committee on International Investment and Multinational Enterprises (CIME).

The main single instrument here is the OECD Codes of Liberalisation. Already within its predecessor agency, the Organisation for European Economic Cooperation (OEEC), as early as 1951, the then member governments had adopted a Code of Liberalisation of Current Invisible Transactions. With the establishment of the OECD, a second parallel instrument was created at the end of 1961, the Code of Liberalisation of Capital Movements. From that date the oversight and further development of these two Codes became the task of the CMIT.

The Codes are legally binding instruments, under which, in their present form, member governments are obliged:

> … to notify the OECD of existing restrictions on foreign direct investment, capital movements and cross-border trade in services, not to introduce additional restrictions (except under specific conditions), to apply any measures without discrimination among OECD countries, and to submit themselves to a peer-review process that aims progressively to remove remaining restrictions over time.[65]

Over the decades, the range and scope of the Codes have notably increased. One aspect of this is membership. At the outset, not all the then member countries were subject to the Capital Movements Code: Canada, Greece, Iceland and Turkey were effectively exempted from the disciplines accepted by the rest. In the course of time, however, these

65 Robert Ley and Pierre Poret, 'The New OECD Members and Liberalisation', *OECD Observer*, No 205, April/May 1997, p 38.

various claims to special treatment were withdrawn. All OECD members are now subject to the full obligations of both Codes, while acceptance of these same obligations has been made a condition of accession for all the new member countries that have been admitted to the Organisation over the last five years, and can be expected equally to apply to any other candidates for admission. Again, with the passage of time, the range of transactions that are subject to the Codes, and in particular, the classes of capital movements which member governments have committed themselves to liberalise, have been greatly extended. Here the main landmarks have been three, and the process of enlargement since the introduction of the Capital Movements Code has been summarised as follows:

> In 1961, the liberalisation obligations … were essentially limited to the free disposal of non-resident-owned blocked funds and free transfers in connection with the making and liquidation of inward direct investments. The Code was revised in 1964 to include basic underlying transactions such as direct investment, certain long-term securities and credit operations and personal capital movements, and in 1984 to cover the right of establishment of direct investors … in 1989 the Code [was] amended to cover all other capital movements, such as money-market transactions, operations in forward markets, swaps, options, and other derivative instruments.[66]

By the opening of the 1990s, the effect of these and other successive extensions had been to make virtually all international capital movements subject to progressive liberalisation obligations on the part of all the OECD member governments; and as has been seen, these same obligations have since been imposed on prospective new members of the Organisation.

During the first three decades of the OECD's history, the parallel Code of Liberalisation of Current Invisible Transactions was subject to no comparable major changes, since most invisible transactions had been liberalised earlier, under the OEEC, and thereafter remained free from exchange controls. However, the provisions of this Code, as well as those of its counterpart, were substantially extended in 1989, when a new item of 'banking and financial services' was introduced 'covering a wide range of activities, including payment services ... banking and investment services … asset management … and advisory and agency services'.[67]

The commitments which member countries have made under the Codes did not, and do not, bind them to specific measures or programmes of liberalisation, nor have such actions to be undertaken in or through the OECD. The right to determine the forms, extent and sequencing of external liberalisation has remained throughout with each national government (or with the European Community). Although there are currently no profound differences in the treatment of capital flows by different OECD member countries – in part, because 15 of them are now members of the Community, while three others are hoping soon to achieve membership, and have shaped their policies

66 Pierre Poret, 'Capital Market Liberalisation: OECD Approach and Rules', Paper presented at the 10th international conference of the International Banking and Finance Institute, 1998, pp 4–5.

67 OECD, *op cit*, 1990, p 9.

accordingly – this relative uniformity is a recent development. Over the first 25 to 30 years of the OECD's existence there were large differences in the extent to which the commitment to liberalisation, which all countries broadly and explicitly accepted, was realised in practice. Each country was free to choose its own pace and menu of derestriction, and this is still the case.

In conformity with this principle of autonomy, governments have retained throughout the right to enter *reservations* which limit the extent to which, at any given time, they are prepared to forgo unconditionally the right to restrict particular classes of capital flows. At every stage of the evolution of the Capital Movements Code, as new items were brought within the scope of the obligation to liberalise, each member country was free to draw up and register its own list of reservations in relation to these items – though the reservations had always to be explained and justified. In the same way, new members are able to enter reservations with respect to the obligations they are about to assume. The reservations can be viewed as options to restrict – options which are available, though they need not be fully used, and which limit in specific ways the extent to which, at any given time, member governments are prepared to put into effect the commitments they have made within the Codes. They are in the nature of safety-valves. Where, however, reservations have not been made, or have been withdrawn, the obligation to remove restrictions applies. New restrictions not already covered by reservations are in general ruled out (a 'standstill' principle operates), while reservations once removed cannot be reimposed at will (so that a 'ratchet' effect is built in). Thus liberalisation is envisaged as a cumulative process.

In this respect too there are safety-valves, though their use is subject to formal limitations. First, a member government has the possibility of registering *derogations*, by which restrictions can be imposed, or reimposed, in cases where the possibility of invoking reservations does not exist. However, such derogations have to be viewed as temporary only; they have to have specific justification, by way of either balance of payments difficulties or 'serious economic and financial disturbance'; and like other aspects of member countries' régimes, they are subject to review within the CMIT. Second, a limited range of transactions is classed in *List B*, and in these cases restrictions can be reimposed, and reservations lodged accordingly, at any stage. Over time, however, the number of categories included in that list has been narrowed down, and it 'currently covers only short-term financial operations and non-resident acquisitions of real estate'.[68]

Notwithstanding the safety-valves, and as noted above, member governments – by their own choice, of course – are bound within the Codes by a number of obligations besides their commitments to liberalise (the obligation of 'rollback') and the standstill provisions. One such obligation is to maintain transparency: all restrictions must be open and notified. A second is to accept surveillance: all restrictions, including reservations and derogations, are subject to review and criticism within the Committee. Third, the National Treatment principle, though not formally embodied in the Codes, effectively applies within them, in particular to direct investment and the right of establishment.

68 Poret, 'Capital Market Liberalisation', *op cit*, p 3.

Fourth, 'liberalisation measures – as well as restrictions – are to be applied to all member countries on a non-discriminatory basis'.[69] In general, though specific exceptions are provided for, the most-favoured nation (MFN) principle applies. Reciprocity arrangements or conditions are thereby in principle ruled out, and where nonetheless they are entered into by member countries, as has been and continues to be the case, this also is subject to surveillance.

Within the OECD, therefore, member countries have consistently endorsed the idea of progressive and cumulative liberalisation of trade in services and cross-border capital flows; and they have evolved procedures which are designed to keep up the momentum of this process while leaving substantial though not unqualified freedom of action to each government. In the main committee concerned, the CMIT, the sequence of liberalisation appears under three principal headings: the increase in the range of transactions for which countries have accepted the obligation to liberalise; the decline over time – though it has not been an uninterrupted decline – in the number, and the degree of restrictiveness, of reservations and derogations; and the shifting of items from List B to List A.

While the obligations of the Capital Movements Code extend to FDI, both inward and outward, and have embraced since 1984 the right of establishment of foreign enterprises on terms no less favourable than those applying to domestic enterprises ('national treatment'), they do not include the treatment of such enterprises when established. Here also, however, its member governments have used the OECD as a mechanism for acting together, through the 1976 Declaration on International Investment and Multinational Enterprises. In this, a leading element is the National Treatment instrument, by which member governments bind themselves – though unlike the Codes, no legal obligation is involved – to accord to foreign enterprises already established within their borders terms no less favourable than those accorded in like situations to domestic enterprises. Issues concerning the treatment of established foreign investors, and in particular the application of the National Treatment instrument, are the responsibility of the CIME. Prospective new members of the Organisation are required to endorse the Declaration and its related complementary decisions, including the National Treatment instrument.

Despite their wide-ranging character, the Codes have limitations that go beyond the fact that the power of decision rests with national governments (and the European Community). Although as noted they are legally binding documents, they contain no formal enforcement procedures and no dispute settlement mechanisms: transparency, surveillance and peer pressure are the channels through which influence is brought to bear on member governments. Again, the obligations apply only to national governments, while in some federal states, the United States being of course the leading instance, there is a case for extending disciplines to lower levels of government. For these and other reasons, it became increasingly felt, by the national officials concerned, that it was necessary to create a wider and more binding set of rules and disciplines for FDI flows broadly defined, which would in this area extend and take over from the Codes and the National Treatment instrument. This was the origin of the MAI initiative.

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69 OECD, *Liberalisation of Capital Movements*, *op cit*, p 15.

Now that the initiative has failed, the focus has to move back to the Codes and the Instrument. In Section 5 above, suggestions are made as to how the work of the OECD in this area might be taken further.

Underdeveloped OECD assets

From a specific well established set of procedures for influencing events within and through the OECD, I turn now to more general ways of doing so which could be exploited more fully.

The OECD has three related and distinctive assets. One is its diverse portfolio of interests, concerns and expertise, while a second is its dense and continuing network of contacts within member governments and other international agencies: these two go together. Alongside them, a third asset is the flexibility of the Organisation with respect to roles, functions and procedures. While the OECD is subject to the minute and unceasing scrutiny of governments in every aspect of its work, so that its autonomy is strictly limited, within this tightly controlled environment it can be used in any way and for any purpose that its members choose. It can be versatile and adaptable, as well as wide-ranging.

These features make it possible for the Organisation, and the Secretariat within it, to treat a wide variety of issues and topics, through methods and procedures which can be tailored to suit, within a common framework. Despite the fact that it is often described as such, by way of routine compliment, the OECD is not in fact notably or distinctively 'multidisciplinary': what it can claim to be, as compared with other international agencies, is 'transdepartmental'. The Secretariat is *potentially* well placed (i) to handle topics and issues which cut across departmental and professional lines, in conjunction with teams of national officials which can be brought together as occasions demand, and (ii) to bring to these topics and issues, as also to its work in specialised areas, a consistent approach, an extra element of coherence. A recent example is the 'Jobs Study' and the programme of work that grew out of it.[70]

These advantages, despite their potential, are not easy to exploit in practice. The very range of the OECD's concerns means that the Secretariat is both fragmented and spread thin. Each of the various internal Directorates has its own subject areas, and its client committees which have their own agenda, preoccupations and procedures. Internal cohesion and quality control are hard to achieve and maintain. Coordination is an ever-present challenge.

Historically, for reasons which lie beyond the scope of this paper, effective means of coordination have never been well developed within the OECD. There are several related aspects of the problem, most notably internal procedures for decision-making and questions of recruitment, selection, career paths and promotion. In the light of the MAI episode, two further aspects, themselves interrelated, are worth noting here.

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70 OECD, *Jobs Study*, Paris, 1994.

One concerns ideas. It is clearly an advantage for an organisation that deals with diverse problems if these can be brought within a common framework of thinking, a shared professional approach. Given that virtually all the issues which the OECD has to handle are economic, or have a large economic dimension, such an approach has in its case to be based on economic ways of thinking. Given further the Organisation's assigned role as an agent of liberalisation for member governments, the obvious common framework of thinking to adopt is a broadly liberal one. This does not at all imply that the OECD Secretariat should be staffed exclusively by economists, nor that the economists that it recruits and employs should all be of one mind. Here as elsewhere, diversity and differences of view are to be encouraged rather than ruled out. All the same, the ideas of economic liberalism offer a unifying element. They can function as one means of coordination, to be set alongside others, across virtually the whole range of topics that makes up the Organisation's extensive portfolio.

The second aspect relates to roles. Within member governments, the responsibility for economic policies in general, as distinct from particular areas or sectors, is normally located in ministries of finance (including 'treasuries') or of economics: only they possess (so to speak) a general licence to comment, review and advise on the economic dimension of whatever issues may arise.[71] It is there, if anywhere, that the coordinating function in economic affairs resides. A distinctive feature of the OECD is that it is the only international agency in which ministers and officials from these ministries are able, if they so wish, to review systematically issues across the whole spectrum of microeconomic and 'structural' policies. Hence they have an opportunity within the Organisation to give a lead on the international scene: they can contribute alike to the better ordering of economic policies *as a whole* within and across member governments, and to the more effective coordination of the OECD's own activities. In particular, this opportunity exists for the main OECD committee concerned, the Economic Policy Committee (EPC). To carry out this aspect of its role, the EPC's interests, in addition to its own special concerns, need to have a continuing OECD-wide dimension.

The list of relevant topics here, within the OECD portfolio, includes both trade policies and investment policies. The future prospects for cross-border liberalisation, including progress in the areas which the MAI negotiations have confirmed as hard to deal with, depend in part on how far EPC officials and their staffs – and their ministers too, though these are rarely to be seen at the OECD – keep a sustained interest in the subject. This can by no means be taken for granted: here again, breadth of view and resourcefulness are at a premium. But at least the OECD offers here a distinctive opportunity, which member governments can take advantage of if they wish.[72]

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71 This is not true of the United States, where a clear responsibility of this kind rests with the Council of Economic Advisers.

72 As always, much depends on personalities. In my years at the OECD, the EPC came closest to realising its potential as coordinator and *animateur* under the leadership of Dr Beryl Sprinkel, in the period when he was Chairman both of the Council of Economic Advisers in the United States and of the EPC.

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GLOSSARY

ACOSS	Australian Council of Social Services
APEC	Asia Pacific Economic Cooperation
ASEAN	Association of South-East Asian Nations
BIAC	Business and Industry Advisory Committee (of the OECD)
BITs	Bilateral Investment Treaties
CIME	Committee on International Investment and Multinational Enterprises
CMIT	Committee on Capital Movements and Invisible Transactions
EC	European Community
EEA	European Economic Area
EPC	Economic Policy Committee (of the OECD)
FDI	Foreign direct investment
GATT	General Agreement on Tariffs and Trade
GATS	General Agreement on Trade in Services
ILO	International Labour Organisation
IMF	International Monetary Fund
MAI	Multilateral Agreement on Investment
MFN	Most-favoured nation
MNE	Multinational Enterprises
NAFTA	North American Free Trade Agreement
NGO	Non-Governmental Organisation
OECD	Organisation for Economic Cooperation and Development
OEEC	Organisation for European Economic Cooperation
REIOs	Regional Economic Integration Organisations
TRIMS	Agreement on Trade Related Investment Measures
TRIPS	Agreement on Trade Related Property Rights
TUAC	Trade Union Advisory Committee (of the OECD)
UNCTAD	United Nations Conference on Trade and Development
WDM	World Development Movement
WTO	World Trade Organization
WWF	World Wildlife Fund