Comments on Conceptual and Empirical Papers
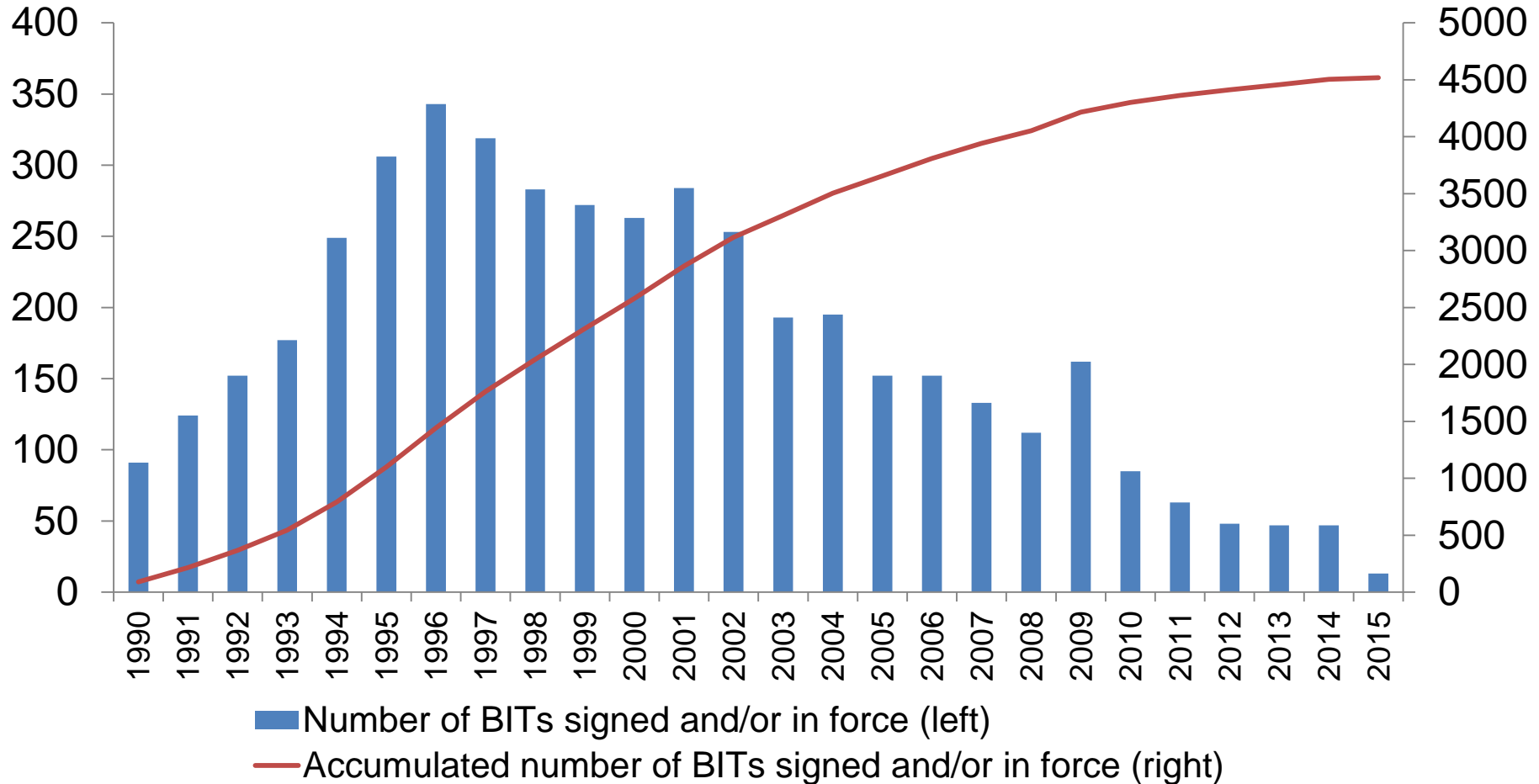
2 June, 2016
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Why BITs/FTAs Investment chapters matter in FDIs

Questions rise from three things: Policy realities, costs, and impact research

- **UNCTAD: Bilateral Investment Treaties**
  - Total: **2926**
  - Total in force: **2278**

- **UNCTAD: Other International Investment Agreements**
  - Total: **360**
  - Total in force: **285**

- Costs: administrative, political and socio-economic cost to engage, conclude and implement BITs and IIAs
  - (ex) ISD: complicated and a sovereign issue

- Impact: existing Research on BIT(FTA) and Impacts on FDI: lack of consensus

Number of BITs signed and/or in force

Number of BITs signed and/or in force (left)

Accumulated number of BITs signed and/or in force (right)

Source: UNCTAND Investment Policy HUB (http://investmentpolicyhub.unctad.org/IIA)
Coverage: World
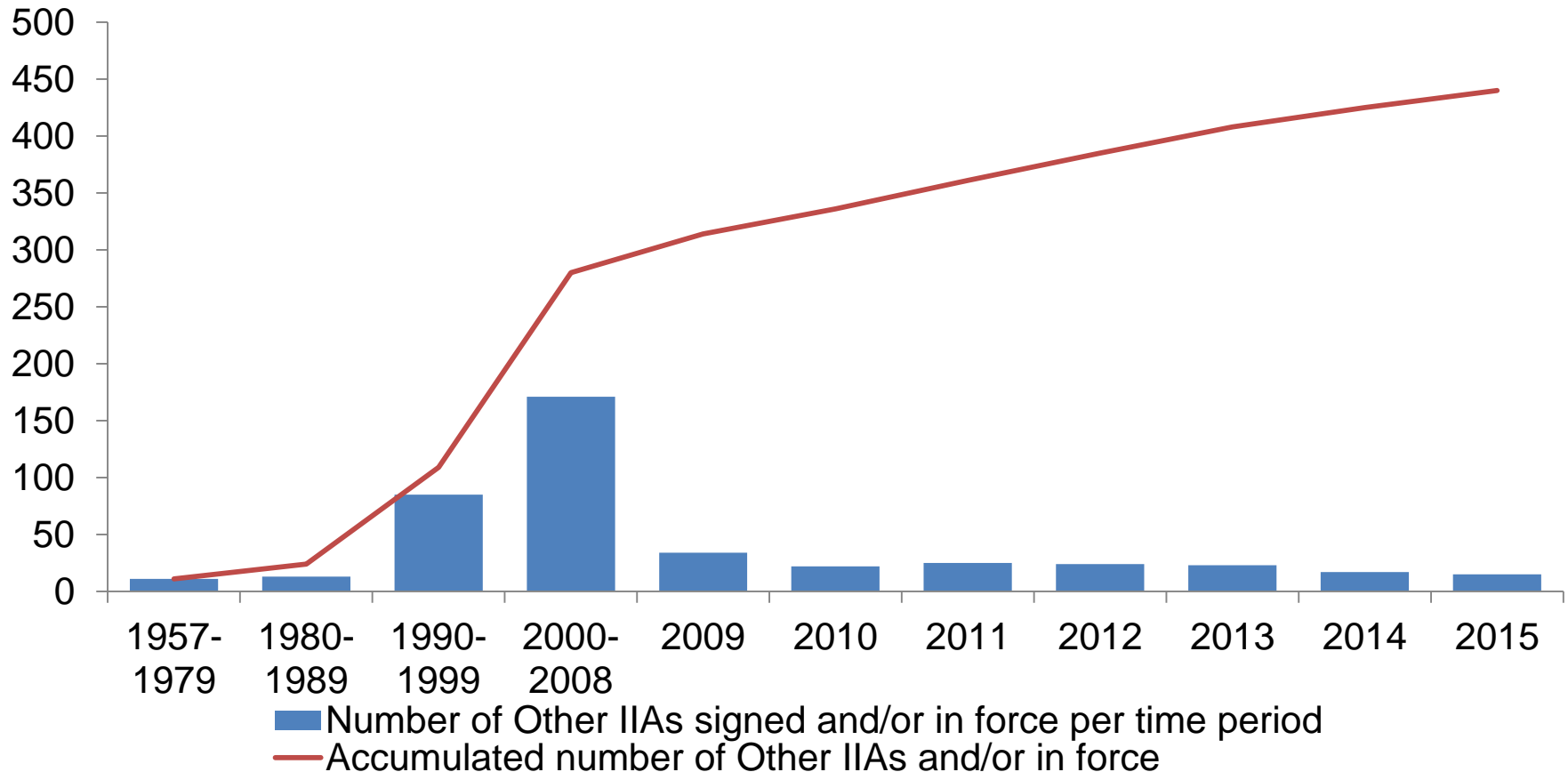Period: Year of signature and/or year of entry inot force
Status: Signed and /or in force
Availability of treaty texts: Regardless of texts
Protocols and side instruments: Regradlss of protocols and side instruments
Relationship with other agreements: Regardless of relationship

Number of Other International Investment Agreements (IIA)

Source: UNCTAND Investment Policy HUB (http://investmentpolicyhub.unctad.org/IIA)
Coverage: World
Period: Year of signature and/or year of entry inot force
Status: Signed and /or in force
Availability of treaty texts: Regardless of texts
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Relationship with other agreements: Regardless of relationship

- BITs and RTAs are treated as homogeneous entities despite the fact that the provisions they include can vary widely across treaties.

	2012 US BIT model (2004 US BIT model), CANANDA and Japan model	2014 EU BIT(EU-Singapore FTA): Establishment vs Investment
TREATMENT	NT, MFN, Minimum Standard of treatment, transfers, PR, Senior Management and Board of directors, (KORUS: Subrogation), derogation	NT, STANDARD TREATMENT, Subrogation
Expropriation, Indirect Expropriation	yes	Yes
ISD	yes	Yes
Non conforming measures: Ratchet and negative list	Yes and elaborated	no
Investment with environment and labor	yes	no

The contributions of the papers

- The conceptual paper: provides legal and policy perspectives on the FDI impact of BITs and RTAs.

- The empirical paper:
  - Effects of heterogeneous BITs and RTIAs on heterogeneous FDI projects in heterogeneous countries.
  - BITs and RTIAs strongly encourage greenfield and M&A FDI projects in all sectors and most countries as long as these treaties include specific investment provisions.
  - In the case of BITs, the presence of an ISD is the only provision which appears to matter.
  - In the case of RTIAs, anti-discrimination provision (TREAT) may matter.

- Conceptual paper
- Structures and concepts are well set up, and contents will be filled further
- Policymakers want to know: design, implementation, benefits (impact), costs,
  - How to design and implement BITs/FTAs BITs to promote FDIs to meet development policy goals: developing countries' policy goals, advanced countries policy goals
  - While decreasing the cost of engaging negotiations and implementation of BITs

- Lessons may come from Actual Case Analysis:
  - what kind of BITs/FTAs' BITs other countries are engaging and concluding:
  - what are the main components, features, issues, what were concluded, getting BITs concluded, and the impact of BITs
  - NAFTA, North-South FTAs such as Korea-US FTA, EU FTAs, German BITs with Developing economies, in particular China..

- Common Templates (NT, MFN, PR, Derogation, SMBD, Subrogation…); differences and coherent elements concluded in new BITs; **how to design pro-FDI BITs while observing 'right to regulate' (so called public policy purposes such as public health and welfare)**

- ISD cases analysis in the conceptual perspective with some policy examples: NAFTA and other cases with EU, developing economies

- Actual cases with convergence or fragmentation of BITs and FTAs' BITs:
  - all BITs are different;
  - Why they are different;
  - What are different
  - What are commonly included: recently US BITs, EU BITs
  - EU BITs/FTAs and or EU countries BITs(Germany) vs US BITs/FTAs

- For example, in actual ISDs, the most frequently used arguments against the governments' measures are (i) NT; (ii) Expropriation and compensation; (iii) and Fair and Equitable Treatment.

- NAFTA ISD Cases: the 77 known NAFTA investor-state dispute settlement (ISDS) claims up to January 1 2015.
  - These include 35 against Canada, 20 against the U.S., and 22 against Mexico.
  - Canada has paid out NAFTA damages totaling over $CAD172 million, while Mexico has paid damages of $US204 million.
  - The U.S. has yet to lose a NAFTA chapter 11 case.

- Based on conceptual and actual cases, policy makers may receive objective advice of having better design, implementation, and negotiation of BITs/FTAs BITs to foster FDIs, and job creation.

Main Innovation of the Empirical Paper

- The paper estimates the impact of bilateral investment treaties (BITs) and regional trade investment agreements (RTIAs) on foreign direct investments (FDIs).

- The main innovation of the paper is the use of a granular approach :
  - using detailed and under-exploited databases (such as BITsel),
  - accounting for the heterogeneity of both BITs and RTIAs as wells as FDIs,
  - distinguishing between entry modes and destination sectors, and controlling for country-specific and FDI-specific factors.
  - 11 provisions to 5 categories: Entry, Treat, Scope, Protec, ISDM

DATA: BITSel (11 provisions) to 5 categories

FTA			BIT		
Definition of investment	narrow = 1, broad = 2		Definition of investment	narrow = 1, broad = 2	1
Admission vs establishment	Admission = 1, establishment = 2		Admission vs establishment	Admission = 1, establishment = 2	2
National Treatment	Yes = 2, No = 1		National Treatment	broad = 2, narrow = 1	3
Most Favoured Nation Clause	Yes = 2, No = 1		Most Favoured Nation Clause	broad = 2, narrow = 1	4
Fair and Equitable Treatment	Yes = 2, No = 1		Fair and Equitable Treatment	Yes = 2, No = 1	5
Direct and Indirect Expropriation coverd	Yes=2; No=1		Expropriation	direct and indirect = 2; direct only = 1	6
free Transfer of investment-related funds	Yes=2; No=1		Free Transfer of investment-related funds	Yes = 2; restricted = 1	7
Non-economic standards	Yes=1; No=2		Non-economic standards	Yes=1; No=2	8
Investor-State Dispute Mechanism	Yes = 2, No = 1Subject to unilateral condition=3(in bracket reserving state)		Investor-State Dispute Mechanism	Yes = 2, No = 1Subject to unilateral condition=3(in bracket reserving state)	9
Umbrella clause	Yes = 2, No = 1		Umbrella clause	Yes = 2, No = 1	10
Temporal scope of application	Short = 1, Long = 2		Temporal Scope of Application	Short = 1, Long = 2	11

- Empirical analysis

- Better have BITs Trend analysis and or FTAs' BITs analysis (from signed BITs over the period)
  - Investigate various BITs components
  - Descriptive statistics to explain current features, trends in BITs/FTAs BITs

- Details of the elements of the vector CONTij:
  - the paper shows that the vector of dyadic control variables, which include geographical distance, time zone difference, and the existence of a common border/language/religion/legal origin/colonial past
  - May need details on these data, for example source, measurement, and specification in the regression models

- The inclusion of FDI03ij and the reporting of the estimated coefficients of FDI03ij
  – Specific justification of FDI03ij
  – Persistence of FDI or demonstration effects?
  – All of the regression results do not report the estimated coefficient of FDI03ij
- Table 1 and Table 2: aggregate analysis
  – BITs and RTAs tend to have a large and positive impact on FDI:
  – When DTT is signed, FDI tends to increase significantly.
  – (interesting result): **none of interaction dummies such as BIT*Governance, BIT*Rule of Law, BIT*OPENNESS, BIT*BITSTOCK,** are statistically significant.
  – (interesting result) : In the column (6) in table 1, the effects of BITs depending on **the direction of the country pairs** (North-South, South-South) **do not appear:** this result shows the similar outcome in table 5 (hetero analysis)

- In the specification of difference-in-difference approaches in page 14
  - In the table 3, the results of columns (5)-(7) confirms the hypothesis of the BIT impact on larger **FDI in investment intensive sectors** relative to investment-light sectors.

  - But, given developing economies' status where some DMCs are service focused (usually investment light sectors), we may want to consider interaction terms of, for example, (BIT*manufacturing), (BIT*Services industry), (BIT*Business services including financial services), etc.

  - Is there any specific reason not to include interaction terms between BITijt and year dummies in the analysis?

Heterogeneous BITs

- Table 4 presents important findings on the effects of heterogeneous BIT provisions on FDIs.
  - At the individual impact of each main category of investment provisions: significant, positive, and large
  - (interesting): **'Entry' effect** is particularly large: interesting results; 'Treat' shows the least in size of the coefficient;
  - (proposal): Given the heterogeneity, fragmentation, and different sets of elements in BIT: we may think some mix of combinations of those elements such as 'ENTRY*TREAT*ISDM' based on the Conceptual Paper's guidance.

- Most important BIT provisions: ISDM

  – (interesting estimation results): **In table 8, among all provisions, <u>ISDM is the only category which remains statistically significant</u>**.

  – (Policy implication): ENTRY, TREAT, SCOPE, PROTECT **<u>do not individually matter</u>** once we control for the presence of ISDM.

RTIAs and FDI

- TABLE 10: **favorable investment provisions in RTIAs(ENTRY, PROTECT) are particularly relevant when South countries are involved,** possibly because the latter provide a more uncertain and regulated business climate than North countries.

- Table 12: disaggregating FDI by entry and sectors
  - (interesting in table 12):
    - Potential exception is FDI in service sectors which appears to be strongly influenced by the presence of an anti-discrimination provision with RTIAs.
    - Interesting is a comparison with the table 7, the service interaction term of "SERV*PROVISION' was insignificant with BITs.
  - (policy implication): (i): Service sectors are more regulated than other industries; (ii) Either push BITs or RTIAs to promote service sector development.

- Relative importance of the RTIA provisions in table 13
  - **Different from the table 8 (most important BIT provisions), the table 13 shows that 'TREAT'** is the only category which remains statistically significant.
  - (policy implication): how we can interpret is a question as RTIA effect takes place in more comprehensive ways than BITs.
  - Recently, more and more RTIAs include goods, services, investment, IPR, pharma, etc.

Some points to think

- The potential link between some provisions and sectors (or modes)
  - The effects of these various provisions **do not appear** to differ across entry modes and destination sectors of FDI.
  - However, for example, market access and local presence may attract more services sector FDI. Financial services may consider 'transfer of funds' issue more.

- North-South BIT/FTAs: ratchet mechanisms and subrogation may be important as much as NT in terms of promoting FDIs due to policy natures of developing economies.

- PR, Ratchet effects, subrogation: how we can include and reflect those important treatments in the conceptual and empirical analyses is a matter of further consideration

- Templates and policy focus may be different among DMCs and between US BITs and EU BITs: US BITs appear focused more on treatment, protection, ISDM while EU BIT seems more flexible.

- Asian DMC policymakers may have to think what types of BITs/FTAs BITs given a country specific circumstance and development goals.

- (Scope Category): the definition of investment should in most of the cases, especially over the 2003-2010, be 'broad based', not narrow based.

- <u>Fair and equitable treatment may move to TREAT</u>: seeking comments from the conceptual paper.

- Quality of ISD matters: transparency and ethics of arbitrators, domestic remedies, government agreement prior to the ISD, exemptions of ISD, amicus curiae, arbitration process.