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Columbia FDI Perspectives
Perspectives on topical foreign direct investment issues by
the Vale Columbia Center on Sustainable International Investment
No. 99 July 15, 2013
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The global significance of transatlantic investment rules

by
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Investment is the bedrock of the economic relationship between the European Union and the United States. Together, EU and US firms have invested more than US$ 4 trillion in each others' markets, and bilateral investment dwarfs transatlantic trade in goods and services.[1] As the EU and US begin negotiating a Transatlantic Trade and Investment Partnership (TTIP) -- an agreement that could be unprecedented in both its scale and scope -- investment is shaping up to be one of the more difficult areas of discussion, both substantively and politically. The EU's process for developing an overall TTIP negotiating mandate revealed deep fissures among EU institutions and stakeholders on investment, with Germany and other member states, certain non-governmental and public interest organizations and the European Parliament concerned about the commercial and legal implications of investment agreements with large economies.

Notwithstanding the public debate over investment in both Europe and the United States, it is critical that negotiators take advantage of the opportunity that the TTIP presents for the world's two largest economies indirectly to craft state-of-the-art *global* standards for cross-border investment, for example in the following areas.

Forced localization measures. Some of the most pernicious barriers to international investment are "forced localization measures." These require that firms locate operations, consume goods or services or conduct other activities within a country's territory. Such

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[1] See Daniel S. Hamilton and Joseph P. Quinlan, *The Transatlantic Economy 2013: Annual Survey of Jobs, Trade and Investment between the United States and Europe* (Washington, DC: Center for Transatlantic Relations, Johns Hopkins University, 2013).

measures include requirements that firms achieve certain levels of "local content" in their products, ensure that a certain percentage of senior management are nationals and transfer proprietary technology to the government or local competitors (or both), among other measures. The US has taken an aggressive approach to such "performance requirements" since issuing its 2004 model bilateral investment treaty (BIT), adding to that a discipline on "indigenous innovation requirements" (i.e., requirements that economic actors use domestically developed technology in their production processes) in its 2012 revision. While the EU is only beginning to negotiate investment provisions since the Lisbon Treaty gave it competence over investment in 2009, evidence from intra-EU deliberations suggests that it will support a similarly tough approach to forced localization measures. If the two sides agree to strong prohibitions on such measures, they will help create pressure on the many third countries that rely on such requirements to reconsider or revise their practices.

Government influence and control. Few developments in the global economy over the past decade have been as significant as the growing participation of state-owned enterprises (SOEs), sovereign wealth funds and other government-controlled entities. As the involvement of such firms in international commerce has increased, so too have concerns over the financial, regulatory and other advantages that governments provide them (and that such firms, by extension, may also provide to favored entities). The EU has well-developed approaches to manage the competitive distortions that may arise where government entities participate in the economy, which one would expect to affect its approach to international agreements. The US recently tightened its coverage of SOEs in its investment chapters and added to its competition chapters disciplines on SOEs acting in a commercial capacity. Combining the EU and US approaches, the TTIP could help ensure that SOEs -- whether acting as government regulators or economic competitors -- do not upset the playing field in their own favor.

Investor-state dispute settlement. Many governments (in places like Latin America, Australia and India) are retreating -- subtly but perceptibly -- from the idea of allowing foreign investors to enforce their investment treaty rights through binding international arbitration. Fearing not so much investor-state claims but the *possibility* of investor-state claims, some countries are stepping back from the remedy and embracing a vague and malleable notion of "policy space." The TTIP negotiations offer the possibility of an approach to dispute settlement that maintains a robust investor-state remedy while responding to the legitimate concerns of governments. Both the US model BIT text and EU policy positions envision an investor-state mechanism that includes procedural safeguards to prevent frivolous claims, enhance transparency and public participation in the arbitration process and ensure the ultimate ability of governments to set their public policy priorities. By agreeing on a dispute-settlement mechanism that provides both effective recourse for aggrieved investors and appropriate protections to defending governments, the EU and US could set an example of balance and pragmatism for other governments struggling to justify the remedy to skeptical stakeholders.

Many of the gains of the TTIP will rebound to the benefit of companies operating across the Atlantic, for example where the two sides lower tariffs, simplify customs procedures

or eliminate needless regulatory differences. Other gains, however, will help firms operating in third countries, for example where the EU and US have the ability to shape globally relevant norms and principles regarding the treatment of cross-border investment. The TTIP investment negotiations provide the two sides an opportunity to do just that and, in so doing, to begin to define global investment policy for the next generation.

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