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Multilateral investment disciplines: Don't forget the GATS!

by

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"To see what is in front of one's nose needs a constant struggle."

– George Orwell

A number of recent studies have discussed the implications of most-favored-nation (MFN) clauses in bilateral investment treaties (BITs) and the possible need for, and role of, a multilateral framework for investment. Surprisingly, the relevance of existing multilateral disciplines, in particular under the General Agreement on Trade in Services (GATS), is seldom acknowledged in this context.

Pursuant to its Article I:1, the GATS applies to "measures by Members affecting trade in services". In turn, trade in services is defined in terms of four modes of supply: conventional cross-border trade (mode 1), consumption of services abroad (mode 2), as well as services supplied via commercial presence (mode 3) and the presence of natural persons (mode 4). Mode 3 is further specified to mean any type of commercial or business establishment, including through the constitution, acquisition or maintenance of a juridical person or a branch or representative office. With the exception of certain market-access commitments and transparency disciplines, it is difficult to find elements in this definition and the ensuing obligations that are not also covered by BITs.¹

Investment in services, within the remit of mode 3, is subject to the GATS's cross-cutting MFN requirement. Moreover, in those sectors inscribed in their schedules of GATS commitments, WTO members are bound to respect the specified levels of market access, including in terms of foreign equity participation and national treatment. In the absence of inscribed limitations, national treatment consists of extending to foreign services and service suppliers the same competitive conditions that are afforded to their domestic counterparts—across all stages of a commercial project.

In addition, in sectors subject to specific commitments, WTO members need to respect certain additional obligations that are essentially intended to protect the commitments from being undermined by excessively restrictive regulations or

administrative practices, foreign exchange restrictions, monopolistic arrangements, and the like. Similar provisions can be found in BITs. For example, the obligation under GATS Article VI:1 concerning the reasonable, objective and impartial administration of measures of general application is conceptually similar to the notion of fair and equitable treatment found in BITs.

Of course, it is disturbing that current WTO disciplines cover only commercial presence/investment in services. The increasing “servicification” of production processes that seamlessly integrate goods- and services-related operations certainly calls for uniform treatment. Cross-sectoral consistency is all the more important as the definitional distinctions are blurred. Manufacturing processes that are conducted on a “fee or contract basis”, i.e., using inputs not owned by the producer, show up in the classification generally used for GATS commitments. Depending solely on an ownership criterion, such processes thus qualify as services productions even though they are otherwise completely identical to conventional manufacturing operations.²

A comprehensive multilateral investment regime would ideally be informed by the GATS. Why re-invent the wheel if some two-thirds of the world's FDI stocks are in services and, thus, largely covered by an existing framework?³ Furthermore, this framework appears flexible enough to accommodate at least some of the issues that are typically addressed in BITs, including compensation for expropriation, for which no direct equivalents exist in the GATS (“additional commitments” under Article XVIII could complement any scheduled market access or national treatment obligations). However, while ever more regional trade agreements (RTAs) contain investment chapters covering goods and services, WTO-focused initiatives are currently subject to a particular constraint: in reference to the relationship between trade and investment and two other proposed issues, the WTO General Council decided in 2004 that there be “no work towards negotiations” during the Doha Round.⁴

In addition to the multilateralization effects associated with MFN clauses in BITs, it is important also to consider the existence of an external “multilateralizer”—the GATS. As noted before, whenever a measure affects trade in services as defined in the GATS, its MFN obligation kicks in, regardless of the scheduling of specific commitments. Consequently, in areas of mutual overlap, the most advantageous conditions contained in a member's BIT are to be extended to the full WTO membership.

Apart from RTAs, the GATS allows for additional departures from MFN treatment. In particular, WTO members had the right to list MFN exemptions at the Agreement's entry into force or upon accession. Among the WTO's 160-odd members, close to 100 have done so for a variety of measures. While not all entries are equally precise, at least 17 members clearly exempted, to varying degrees, their BITs from MFN treatment. Apparently, the governments concerned were not only conscious of the scope of the GATS, but also felt uncomfortable with its possible multilateralization effects. They saw, and acted upon, what was in front of their nose.

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¹ See Rudolf Adlung and Martin Molinuevo, "Bilateralism in services trade: Is there fire behind the (BIT-)smoke?", *Journal of International Economic Law* 11(2) (2008); Martin Molinuevo, *Protecting Investment in Services: Investor-State Arbitration Versus WTO Dispute Settlement* (New York: Kluwer Law International, 2012).

² Rudolf Adlung and Weiwei Zhang, "Trade disciplines with a trapdoor: Contract manufacturing," *Journal of International Economic Law* 16(2) (2013).

³ UNCTAD, *World Investment Report 2013* (New York: United Nations, 2013).

⁴ WTO, Decision Adopted by the General Council on 1 August 2004, Document WT/L/579.

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