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Space for Local Content Policies and Strategies

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Space for Local Content Policies and Strategies

A crucial time to revisit an old debate



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1 Introduction

Roughly 20 years ago, the World Trade Organization's (WTO) entry into force established a broad multilateral framework governing trade in goods and services and establishing certain rules regarding international investment. In the decades that have followed, negotiations on additional bilateral and multilateral agreements have deepened and expanded international rules on trade and investment. With significant negotiating activity continuing on these texts, now is a key time for assessment of their implications.

The need for an assessment of the scope and extent of this growing body of international rules is particularly important in light of the agreed consensus on (1) the need for governments to take robust action to achieve sustainable development,¹ and (2) the need for international rules to leave domestic governments adequate policy space to implement appropriate steps in that regard.²

This paper aims to aid that exercise, focusing both on the role that local content measures can play in advancing sustainable development, and the impact that trade and investment treaties concluded over the past 20 years have had and will continue to have on the ability of governments to employ those tools. Local content measures include a wide range of actions – from import substitution policies to requirements on firms to establish manufacturing facilities in the host country as a condition for receiving market access rights or other incentives. Some of those measures such as import substitution policies were restricted under the WTO due to wide agreement by negotiating parties that the costs of those measures outweighed their benefits. But the WTO left many other local content measures in governments' policy toolboxes. As is discussed in this paper, however, that is changing, with the menu of permissible actions for many countries being significantly smaller than it was even a decade ago.

The following sections elaborate on these trends and their implications. Section Two of this paper begins by discussing the connections between local content policies and sustainable development objectives. In particular, it examines how local content policies relate to three Sustainable Development Goals (SDGs) adopted by the UN General Assembly in September 2015:

- **Goal 8** – *promote sustained, inclusive and sustainable economic growth, full and productive employment and decent work for all*
- **Goal 9** – *build resilient infrastructure, promote inclusive and sustainable industrialization and foster innovation*
- **Goal 10** – *Reduce inequality within and among countries*

These three SDGs were selected because of the importance of domestic and international economic law and policy in achieving their targets.

Section Two also briefly explores the role of global value chains (GVCs) as both a phenomenon ordering and a way of understanding the modern global economy. It highlights the relevance of GVCs for policy interventions to achieve development objectives.

Section Three of this paper then examines the constraints that international law imposes on local content policies relevant to the SDGs. It discusses core aspects of law of the WTO and the extensive and still evolving body of international investment agreements (IIAs) that often impose "WTO+" obligations on governments, illustrating the overall ratcheting up of restrictions imposed by international economic law, and the corresponding ratcheting down of policy space.

Finally, Section Four presents conclusions and options aimed at enabling countries – developing countries in particular – to pursue local content policies and strategies that contribute to the SDGs.

1 Transforming Our World: The 2030 Agenda for Sustainable Development, Resolution adopted by the General Assembly on September 25, 2015, A/RES/70/1.

2 Id. para. 21.

2 The New Sustainable Development Agenda

Worldwide, governments and other stakeholders are devoting renewed energy to achieving sustainable development. Defined by the Brundtland Commission nearly 30 years ago as “development which meets the needs of current generations without compromising the ability of future generations to meet their own needs,” sustainable development is increasingly being used as a foundational objective to orient and guide both public and private action.

Three landmark processes in 2015 marked and helped solidify the current international consensus regarding sustainable development as an orienting principle. The first is the formulation of an “Action Agenda” on Financing for Development (FfD). In that Agenda, agreed in July 2015 at the Third International Conference on FfD, world leaders set forth a holistic framework and outlined priorities and concrete actions to mobilize the necessary resources for achieving crucial objectives.³

In September 2015, the UN General Assembly adopted the set of 17 Sustainable Development Goals and associated targets to be met by 2030. As detailed in the United Nations’ outcome document, “Transforming Our World: the 2030 Agenda for Sustainable Development,” achieving the SDGs requires commitment by and strategic collaboration between the public and private sectors to address a wide range of pressing environmental, social, and economic challenges.

The third process is the negotiation and conclusion of an agreement on climate change mitigation and adaptation, which was accomplished in December 2015,⁴ and will be implemented in part through countries’ “Intended Nationally Determined Contributions.”⁵

Together, these texts emphasize the need for action that will promote development that is economically, socially and environmentally sustainable. They also recognize the importance of government action as a force to leverage and shape private sector activity. Tackling the challenges that the Action Agenda, the SDGs, and the climate change negotiations are responding to requires a government hand in the market. Given governments’ limited resources, the need for private sector capital and skills, and the risk that government measures may hinder rather than foster sustainable private sector action, it is fundamental for governments to be particularly coherent in their policy choices and strategic in how they use and leverage resources to catalyze and channel private sector resources in complementary directions.

BOX 1

Common Terms Used in this Paper

Local Content Policy: Definitions of a “local content policy” vary widely depending on the context and user. This paper defines it broadly as a policy governing foreign investors or investments that aims to more actively embed foreign investment in, and catalyze spillovers into and linkages with, the domestic economy. This definition includes, but is not limited to, measures expressly requiring or incentivizing use of local goods, services, and labor. It can also include measures such as those requiring foreign investors to incorporate firms in the host economy, or to make intra-firm expenditures in the host economy. IIAs (defined below), often use the term “domestic content”; but generally do not define the term.

International investment agreement (IIA): A treaty between countries that governs international investment. An IIA may be a bilateral treaty, or a multilateral agreement. It may focus solely on investment (as is the case in many bilateral investment treaties [BITs]), or may include a chapter on investment within a broader free trade agreement (FTA). A key feature of IIAs is that most allow investors to take their host states to arbitration to enforce the treaty’s investment protection provisions and recover damages for breach. This method of dispute resolution is commonly referred to as “investor-state dispute settlement” (ISDS).

3 Addis Ababa Action Agenda of the Third International Conference on Financing for Sustainable Development, July 13–16, 2015, para. 2.

4 Adoption of the Paris Agreement, Proposal by the President, FCCC/CP/2015/L.9/Rev.1, December 12, 2012 (including the Paris Agreement as an annex to the Decision).

5 Individually Nationally Determined Contributions or “INDCs” represent countries’ respective plans for reducing emissions and may also address other issues such as their adaptation plans and support needed from, or provided to, other countries. For a collection of INDCs, see <http://cait.wri.org/indc/>.

Performance requirements: As used in this paper, performance requirements are measures in law, regulation or contract that require investors to meet specified goals (e.g., on local content) when entering, operating in, expanding in, or leaving a host country.⁶ These measures can be a flat requirement, or can be required as a condition for the investor to receive a benefit from the government such as a tax incentive.

Technology transfer: There is no single accepted definition of “technology” or “technology transfer”; rather, the terms often differ based on the particular purpose and context in which they are used (e.g., in domestic law or contract, or in multilateral environmental agreements). One broad definition of “technology” is “the complete body of knowledge applicable to human endeavour (as well as the physical embodiments of this).”⁷ A definition of “technology transfer”, adopted for the purpose of the United Nations Framework Convention on Climate Change, but which may also be instructive for other contexts, is:

*a broad set of processes covering the flows of know-how, experience and equipment for mitigating and adapting to climate change amongst different stakeholders such as governments, private sector entities, financial institutions, [NGOs] and research/education institutions. ... The broad and inclusive term “transfer” encompasses diffusion of technologies and technology cooperation across and within countries. It covers the transfer of [environmentally sound technology] processes between developed countries, developing countries and countries with economies in transition, amongst developed countries, amongst developing countries and amongst countries with economies in transition. It comprises the process of learning to understand, utilize and replicate the technology, including the capacity to choose it and adapt it to local conditions and integrate it with indigenous technologies.*⁸

This paper does not adopt a definition of “technology” or “technology transfer”. This is because of both the lack of any clear consensus definition to adopt, as well as the fact that IIAs likewise do not define or otherwise provide clarity regarding the meaning of those terms. This silence in IIAs gives rise to significant uncertainty about the breadth of IIA prohibitions on requirements to “transfer technology”.

6 UNCTAD, Foreign Direct Investment and Performance Requirements: New Evidence from Selected Countries (2003), available at http://unctad.org/en/docs/iteiia20037_en.pdf.

7 Klaus Bosselmann, “Poverty Alleviation and Environmental Sustainability Through Improved Regimes of Technology Transfer,” 2/1 Law, Environment & Development Journal 19, 22 (2006).

8 Intergovernmental Panel on Climate Change, Special Report: Methodological and Technical Issues in Technology Transfer – Summary for Policy Makers 1 (2000).

Why a Focus on Space for Local Content Policies is Crucial

One key area where there may be a particularly strong need for policy space, and where there are increasingly IIA-based constraints on that space, is in the context of local content policies applied to foreign investors and their investments. “Local content” policies, as used in this paper, are defined broadly as any policy governing foreign investors or investments that aims to more actively embed foreign investment in, and catalyze spillovers into and linkages with, the domestic economy (see Box 1). They include:

- **Basic local content requirements:** measures that require or encourage investors/investments to use a certain amount or proportion of local resources (including labor, services, materials and parts) when producing goods or providing services;
- **Export restraints:** measures such as quantitative restrictions, export taxes, licenses, or other restraints used to require or encourage domestic value-addition;⁹
- **Joint venture requirements:** measures requiring foreign investors to partner with domestic firms or other entities such as research institutions;
- **Local management requirements:** measures requiring nationals to be on boards or in senior management;
- **Local equity requirements:** measures that require firms to have a certain share of domestic ownership;
- **Location requirements:** measures requiring companies to locate their global or regional headquarters in the host state, or to establish operations in a particular location in the host state; and
- **Technology transfer requirements** (see Box 1).

These local content policies can be incorporated in laws or regulations as flat requirements on firms, or as a condition for firms to receive tax incentives or other government benefits; local content policies can also be incorporated and implemented in contracts negotiated between firms and government entities.

Local content policies have been and continue to be used by countries of all income levels, in different sectors, and with varying levels of success in achieving their policy

aims of maximizing the benefits that foreign direct investment can, but does not necessarily, bring (see Box 2). These policy aims include establishing and deepening linkages between foreign investment and the domestic economy that will promote domestic development;¹⁰ building local skills, capacity and employment; encouraging specific types of activities such as research and development (R&D) in the host country; securing domestic support for policies such as encouraging deployment of renewable energy; and promoting technology exchange between foreign and domestic companies.¹¹

Many debate the advantages and disadvantages of local content measures. Proponents of local content measures assert, for instance, that countries – particularly developing countries – should be able to implement them to protect and strengthen infant industries not yet able to compete in the world market. According to proponents, without such measures, undeveloped domestic infant industries could not compete with foreign firms in the short-run, even though, in the long-run, they may have a comparative advantage.¹² Proponents also argue that local content requirements help to promote development goals by increasing local production and employment and encouraging transfers of technology between local and foreign entities.

In contrast, opponents argue, among other things, that local content policies produce economic inefficiency and discourage foreign investors from investing in a country. According to such critics, these measures force companies to use local inputs and restrict access to global markets. They argue that by limiting the available supply of inputs that foreign investors can use to produce goods, local content requirements “raise foreign companies’ production costs and ultimately discourage foreign investors from investing in the host countries,” while also increasing the costs to local consumers.¹³ Furthermore, critics contend, local content measures can be difficult and costly to

9 This domestic value-added may be desirable for generally increasing domestic economic activity, as well as generating additional revenues that can help compensate for the negative environmental or other externalities of producing the raw materials used in the processing.

10 WTO/UNCTAD, Trade-Related Investment Measures and Other Performance Requirements, Part II, Evidence on the Use, the Policy Objectives, and the Impact of Trade-Related Investment Measures and Other Performance Requirements, Joint Study by the WTO and UNCTAD Secretariats, Document G/C/W/307/Add.1 (2001), 235.

11 International Economics, The Chinese University of Hong Kong, available at <http://intl.econ.cuhk.edu.hk/topic/index.php?did=23>.

12 Id.

13 Id.

enforce properly. As a result, opponents argue, these tools only increase administrative costs for governments, while failing to achieve their goals of increased local employment and production.¹⁴

Overall, the debate, which involves many more arguments and issues than noted briefly above, is complex, and each side of the argument raises important points that should be considered in shaping policy. Whether local content requirements are good policy tools depends on the nature of the requirement, the fit between the requirement and its intended purpose, the circumstances in the host country, the needs and characteristics of the relevant firms, and the drivers behind those firms' decisions to invest abroad. The issue is much too nuanced and context specific for there to be a simple rule on whether, when and how a government should employ many of these tools.

Over the past several decades, local content policies have been the subject of extensive analysis and debate, helping policy makers and other stakeholders better understand whether, in what circumstances, and how, to use these tools to harness foreign investment for domestic development objectives.

BOX 2

Local Content Requirements in the Renewable Energy Industry

One area in which a number of countries – developed and developing – have introduced local content requirements is in the context of their renewable energy industries. Four main arguments have been offered for using local content measures for renewable energy investments:

→ “First, the political economy argument is made that [local content requirements (LCRs)] augment public support for renewable energy projects. Second, proponents point to the classic case for protecting infant industries, especially in developing countries, until they can compete on the international market. Third, and, quite importantly, the creation of “green” jobs, especially in developed countries, is put forward as a justification for the use of LCRs. Fourth, proponents point

to the potential environmental benefits of greater competition between renewable energy firms over the medium-term.”¹⁵

Yet strong arguments have also been raised in opposition:

*Opponents to local content requirements in renewable energy policies point to the economic costs – inefficient allocation of resources, higher retail power prices, negligible employment gains and a negative impact on trade – and question the environmental gains in the medium-term.*¹⁶

To seize the benefits and avoid undue costs of local content requirements, careful design is necessary. Some researchers have sought to identify criteria for local content requirements in renewable energy production to be successful in terms of global objectives of promoting global growth and innovation in the renewable energy industry, and spurring domestic economic growth and job creation.¹⁷ These include:

1. Stability and size of market: LCRs need a stable market with sufficient size and potential, without which there will be little incentive to invest in building up the necessary manufacturing capacity.
2. Restrictiveness of LCRs: To increase their chances of success, local content requirements should not be set too high, too quickly.
3. Cooperation between government and firms: Dialogue and information sharing can help governments set targets based on realistic assessments of supply and demand; financial assistance from governments to help firms meet targets can also help improve positive outcomes, though care needs to be taken to ensure costs of any subsidies are tailored to (and do not outweigh) their benefits, and that subsidies are appropriately limited in duration.
4. Technology and knowledge transfers: LCRs can produce benefits when technologies from or needed by the project spill over into the domestic economy and increase competitiveness of domestic suppliers. For technology and knowledge transfers to occur, there must be adequate absorptive capacity in the host country, and a bridgeable gap between foreign and domestic technologies.¹⁸

15 Sherry Stephenson, “Addressing Local Content Requirements in a Sustainable Energy Trade Agreement,” (ICTSD 2013) 4.

16 Sherry Stephenson, “Addressing Local Content Requirements in a Sustainable Energy Trade Agreement,” (ICTSD 2013) 5.

17 Jan-Christoph Kuntze and Tom Moerenhout, “Local Content Requirements and the Renewable Energy Industry – A Good Match?” (ICTSD 2013) 11–13.

18 Jan-Christoph Kuntze and Tom Moerenhout, “Local Content Requirements and the Renewable Energy Industry – A Good Match?” (ICTSD 2013) 11–13.

14 UNCTAD, Foreign Direct Investment and Performance Requirements: New Evidence from Selected Countries (2003) 35.

Experiences of countries like Norway, for example, are often cited to show how local content requirements can produce long-term domestic benefits (see Box 3). Yet in addition to the growing number of legal barriers to the use of local content measures (discussed in section 3), there are, as noted above, practical challenges to efficient and effective employment of those policy tools. One commonly cited ingredient for success is the existence of necessary capacity and appropriate conditions in the host country. For local content requirements to be effective, for example, there must be (or must be a plan to develop) existing and competitive suppliers of the labor, goods, and services necessary to meet specified local content targets. Otherwise companies may be unlikely to invest in the host economy, may become less competitive due to lower quality or higher priced inputs, and/or may fail to meet the desired or required levels of local content.

Similarly, professionals and potential domestic joint venture partners need to have appropriate skills in order to maximize cooperative relationships and minimize the risk of being effectively sidelined in management roles in and corporate agreements with foreign partners. And requirements to invest in a particular location or to establish headquarters in a particular country or region will discourage investment if those locations lack the requisite fundamentals such as availability of transportation, information and communication technologies (ICT), and energy infrastructure needed for operations.

While taking into account the importance of building up domestic capacity and conditions for local content policies to work, and recognizing that certain local content policies may still fail to achieve their objectives or may achieve them at a high cost relative to their benefits, this paper takes the position that, properly designed and implemented, and complemented by an appropriate domestic enabling environment and absorptive capacity, local content policies can form an important part of governments' strategies to achieve their sustainable development objectives.

BOX 3

Local Content Policies in the Extractive Industries: Norway's Experience

Traditionally, extractive industries have operated as enclaves, producing limited beneficial spillovers into their host economies in terms of economic growth and diversification. Yet, as data on spending by extractive industry companies indicate, the potential advantages of cracking that enclave model are significant. According to British Petroleum (BP) and Anglo American, for example, they spent an estimated 87% and 64%, respectively, of total value created on suppliers in 2014. These expenditures dwarf tax and royalty payments which, for BP and Anglo American, amounted to 2% and 11%, respectively.¹⁹ These figures help explain why governments are increasingly seeking to require or encourage extractive industry firms to purchase goods and services from domestic providers.

One country that has been relatively successful in such efforts to fight the enclave model is Norway.

When oil was first discovered offshore in 1969, Norway did not have the expertise to supply offshore oil rigs. But within roughly thirty years, companies were sourcing more than 50% of capital inputs and more than 80% of operations and maintenance inputs from Norwegian firms. The acquired expertise has also enabled Norwegian firms to expand into export markets, with exports comprising nearly half of their sales by the early 2000s.²⁰

Norway achieved these results through a mix of various measures. In 1972, for example, Norway passed the Royal Decree, requiring all operations to source from Norwegian companies unless the Norwegian suppliers were not competitive in terms of quality, service and price. The 1985 Petroleum Act further stipulated local content provisions to be used when allocating licenses in the North Sea. As a result of these measures, Norway provided preferential treatment to Norwegian companies in all bidding rounds between 1974 and 1994. The licenses also included provisions requiring the transfer of skills and technologies to Norway's infant domestic petroleum industry.

19 These figures were calculated based on the companies' respective annual reports.

20 Håvard Halland et al, "The Extractive Industries Sector: Essentials for Economists, Public Finance Professionals, and Policy Makers," (World Bank Group 2015) 95.

A 2015 World Bank Group publication describes other efforts designed at promoting R&D, technology transfer, and linkages with domestic firms in Norway:

[I]nternational petroleum companies were, in the early phase of oil extraction, encouraged to enter cooperative agreements with research units at national universities. This resulted in the upgrading of oil-sector-specific skills among academic staff and degree programs tailored to the oil sector and related industries. ... Financial support for [R&D] was taken into account in the award of contracts, as was the transfer of skills and technology. A corporate income tax rate for the oil sector of 78 percent, with all R&D expenses immediately deductible, provided a strong incentive for investment in domestic R&D.

Similar policies were established at the firm level, encouraging multinational oil companies to integrate domestic firms and enterprises in large development projects and fostering joint ventures and cooperation agreements between domestic and foreign companies. International oil companies were required to set up fully operating subsidiaries in Norway.²¹

In 1994, Norway joined the European Economic Area, a single market with the European Union, and as a condition of membership was not allowed to continue with its preferential treatment policies. However, by that point, the backward linkages were already established.

It is estimated that in 2014 the oilfield services industry was one of the largest contributors to the Norwegian economy with 1,100 companies employing 122,000 people. The industry is composed of (1) the seismic segment, which includes the manufacturing of equipment for the exploration of oil and gas, and gathering and interpreting seismic results; (2) the exploration and production drilling segment, which includes companies that own and operate drilling rigs and associated services; (3) the engineering, fabrication and installation segment, which focuses on the construction and installation of offshore oil platforms; (4) the operations segment, which supports oil companies during the production phase; and (5) the decommissioning segment, which advises companies on abandonment.²²

3.1 Achieving the SDGs: The Role of Local Content Policies

In light of the important role that the SDGs will play in shaping domestic and international policy, and the need to ensure that international legal frameworks promote, rather than hinder, efforts to achieve those goals and associated targets, this section seeks to identify the types of measures that may need to be adopted to achieve SDGs 8, 9 and 10, and the policy space that therefore may need to be maintained. It focuses on these particular goals due to the especially important role that domestic and international economic policy will need to play in meeting them.

3.1.1 Goal 8 – Promote Sustained, Inclusive and Sustainable Economic Growth, Full and Productive Employment and Decent Work for All

Goal 8 focuses on improving the quality and availability of productive employment and decent work for all, including women, minorities and others that may face particular challenges gaining access to necessary education, training, and job opportunities. Foreign investment can play a crucial role in achieving this goal by bringing capital, employment, skills, technology, possible linkages with the local economy, and channels to help local firms integrate and expand in global value chains.

Supportive policies are necessary to facilitate these impacts. Policies must aim, among other things, at improving opportunities and reducing discrimination in education, training and employment, and addressing imperfect information and other market failures that can result in discriminatory outcomes and disadvantages for host country producers and suppliers.

These policies consist of various measures to improve the capacity of all for productive employment, with a particular focus on those suffering from historic or systematic discrimination, along with special measures designed to require or encourage firms to employ and source from marginalized, vulnerable, and historically disadvantaged groups. There is therefore both an element that consists of capacity building to improve the absorptive capacities for (targeted) local content measures, and an element that

21 Håvard Halland et al, “The Extractive Industries Sector: Essentials for Economists, Public Finance Professionals, and Policy Makers,” (World Bank Group 2015) 95.

22 “The Norwegian Oilfield Services Analysis 2014,” (Ernst & Young 2015).

TABLE 1 Illustrative Local Content and Supportive Policies for SDG 8

Examples of SDG Targets	Examples of Relevant Local Content and Supportive Capacity Building Policies
8.2 Achieve higher levels of economic productivity through diversification, technological upgrading and innovation, including through a focus on high-value added and labour-intensive sectors	<ul style="list-style-type: none"> • Increase diversification and domestic value-addition through requiring or incentivizing use of local suppliers of goods, services, labor • Provide support to domestic individuals and firms to increase their competitiveness as suppliers for foreign investments • Require/incentivize joint ventures or other collaborative agreements to facilitate linkages and technology transfer • Require or incentivize R&D and education and training in the host country in order to help build domestic capacity
8.3 Promote development-oriented policies that support productive activities, decent job creation, entrepreneurship, creativity and innovation, and encourage the formalization and growth of micro-, small- and medium-sized enterprises, including through access to financial services	<ul style="list-style-type: none"> • Provide technical and financial support for micro-, small- and medium-sized enterprises to aid their development and growth
8.5 By 2030, achieve full and productive employment and decent work for all women and men, including for young people and persons with disabilities, and equal pay for work of equal value	<ul style="list-style-type: none"> • Provide education, skills training and other support necessary for employment • Implement positive measures and policies to help marginalized, vulnerable, and historically disadvantaged groups to gain access to business and employment opportunities • Require or incentivize employment of qualified domestic labor

consists of local content policies to help promote economic diversification as well as diversity of suppliers and employees. Table 1 above lists some of these policies.

3.1.2 Goal 9 – Build Resilient Infrastructure, Promote Inclusive and Sustainable Industrialization and Foster Innovation

Among the benefits that foreign investment can bring are technology transfer and investments in infrastructure.

Through, for example, working with local suppliers or building the capacity of local citizens who subsequently bring their know-how to another firm, foreign investors can introduce new technologies in the host country that can, in turn, improve the competitiveness of labor and firms in that country.

But, as noted above, technology transfer requires adequate absorptive capacity in the host country, and government support for education and training is fundamental for developing that capacity. Similarly, while technology transfer may happen organically, local content policies

requiring or encouraging use of local providers of goods, services, and labor can help ensure and speed that transfer.

In terms of infrastructure development, investors can bring the capital, experience and technology necessary to build and/or operate crucial infrastructure to facilitate the delivery of public services. Foreign investment may also contribute to development of infrastructure even when not specifically built for a public purpose. When firms in the extractive industries, for example, construct transport, power, ICT, or other infrastructure necessary for their operations, those investments can be designed to also provide other users access and rights to use that infrastructure.

A government role – whether established through regulation, a government equity stake, managerial role, and/or other mechanism – in infrastructure projects is essential for ensuring that those projects result in affordable and equitable access to the infrastructure and associated services consistent with SDG 9. Additionally, traditional models of “enclave” development in the extractive industries illustrate that, in the absence of government intervention, extractive industry firms that develop their own

infrastructure will often not provide for broader access to or use of that infrastructure even if doing so only marginally increases costs or operational challenges and is the only viable way of expanding access to remote regions. In summary, government policies are crucial to ensure

that foreign investment results in the technology transfer and infrastructure development that can advance progress on Goal 9. Table 2 below lists some of these policies that can be enlisted to advance progress on SDG 9.

TABLE 2 Illustrative Local Content and Supportive Policies for SDG 9

Examples of SDG Targets	Examples of Relevant Local Content and Supportive Capacity Building Policies
9.1 Develop quality, reliable, sustainable and resilient infrastructure, including regional and transborder infrastructure, to support economic development and human well-being, with a focus on affordable and equitable access for all	<ul style="list-style-type: none"> Require or encourage firms to invest in developing infrastructure connected with their projects (e.g., providing shared use of infrastructure developed in conjunction with extractive industry projects)²³ Use state equity or government managerial control to guide operations of public infrastructure services and ensure they meet public policy objectives
9.2 Promote inclusive and sustainable industrialization and, by 2030, significantly raise industry's share of employment and gross domestic product, in line with national circumstances, and double its share in least developed countries	<ul style="list-style-type: none"> Increase domestic diversification and value-added – particularly in least developed countries – through requiring or incentivizing use of local suppliers of goods, services, labor Provide support to domestic individuals and firms to increase their competitiveness as suppliers for foreign investments Require/incentivize joint ventures or other collaborative agreements to facilitate linkages and technology transfer Require or incentivize R&D and education and training in the host country in order to help build domestic capacity
9.3 Increase the access of small-scale industrial and other enterprises, in particular in developing countries, to financial services, including affordable credit, and their integration into value chains and markets	<ul style="list-style-type: none"> Provide technical and financial support to small-scale and other enterprises to develop their capacity and assist them in integrating in global value chains
9.4 By 2030, upgrade infrastructure and retrofit industries to make them sustainable, with increased resource-use efficiency and greater adoption of clean and environmentally sound technologies and industrial processes, with all countries taking action in accordance with their respective capabilities	<ul style="list-style-type: none"> Impose requirements to use or not use certain technologies Impose technology-forcing requirements designed to meet environmental and efficiency objectives²⁴
9.5 Enhance scientific research, upgrade the technological capabilities of industrial sectors in all countries, in particular developing countries, including, by 2030, encouraging innovation and substantially increasing the number of research and development workers per 1 million people and public and private research and development spending	<ul style="list-style-type: none"> Require or encourage firms to locate R&D activities in the host country to develop spillovers and encourage technology transfer within the host country Require or encourage firms to provide education and training for employees Provide government/university support for collaborative R&D programs among businesses, government, and/or universities, and establish policy frameworks that aim to promote transfer and use of developed technologies Promote development of industry clusters

²³ Columbia Center on Sustainable Investment (CCSI), “A Framework to Approach Shared-Use of Mining-Related Infrastructure” (March 2014); Perrine Toledano and Clara Roorda, “Leveraging Mining Demand for Internet and Telecommunications Infrastructure for Broad Economic Development: Models, Opportunities and Challenges” (CCSI June 2014).

²⁴ “Technology forcing refers to regulatory efforts that direct the development of technologies along specific paths. These standards force firms either (1) to innovate technologies, forcing the creation of new technologies, or (2) to disseminate technologies, requiring firms to incorporate existing technologies into their products. This use of technology-forcing regulation has varied by industry... Despite the difficulties in implementation, technology-forcing regulation has led to numerous innovations, including improved environmental quality, safer automobiles, cleaner automobile emissions, and improved disclosure of corporate financial information. Jay P. Kesan and Rajiv C. Shah, “Shaping Code,” 18 Harvard Journal of Law & Technology 319, 333–337 (2005).

3.1.3 Goal 10 – Reduce Inequality Within and Among Countries

While recent decades have seen a decline in absolute poverty, largely due to significant changes in China, developing countries today are, according to some analyses, “somewhat more unequal than three decades ago.”²⁵ Similarly, within wealthy countries, “[i]nequality increased (almost) everywhere over the 1970–2010 period.”²⁶

The causes of this increasing inequality are complex, multifaceted, and heavily debated; additionally, new data and understanding of global value chains (GVCs) has prompted increased analysis of how the degree and depth of integration in GVCs affect these rising patterns of inequality.²⁷ While many questions remain unanswered about the root causes of inequality, SDG 10 calls for policy responses to address them.

At the domestic level, some of these policy responses echo ones that can be used for achieving other SDGs, including using public revenues to invest in education and training,²⁸ and adopting efforts to ensure equality of opportunities for all irrespective of their “age, sex, disability, race, ethnicity, origin, religion, or economic or other status.”²⁹

Importantly, Goal 10 also addresses the importance of ensuring that developing countries have a voice in shaping international economic rules, and calls for those rules to reflect the “principle of special and differential treatment for developing countries, in particular least developed countries.”³⁰ These principles can help ensure that developing countries retain policy space to attempt to reduce inequality vis-à-vis other countries and within their own borders.

TABLE 3 Illustrative Local Content Policies and Supportive Measures for SDG 10

Examples of SDG Targets	Examples of Relevant Local Content and Supportive Capacity Building Policies
<p>10.2 By 2030, empower and promote the social, economic and political inclusion of all, irrespective of age, sex, disability, race, ethnicity, origin, religion or economic or other status</p>	<ul style="list-style-type: none"> • At the international level, protect the ability of developing and least developed countries to maximize benefits of foreign investment for all within their borders by using policy tools to build up domestic capacity, develop linkages with international firms, increase investment in disadvantaged regions, integrate and benefit from global value chains, and increase economic opportunities for marginalized, disadvantaged and vulnerable individuals and communities • At the domestic level, use supportive measures such as education and skill building to increase the capacity of and opportunities available to all to participate in social, economic, and political life, and use local content policies to better enable individuals and firms to seize those opportunities

25 Facundo Alvaredo & Leonardo Gasparini, “Recent Trends in Inequality and Poverty in Developing Countries,” in *Handbook of Income Distribution*, vol. 2A, 699 (Elsevier BV 2015).

26 Savatore Morelli, Timothy Speeding & Jeffrey Thompson, “Post-1970 Trends in Within-Country Inequality and Poverty: Rich and Middle-Income Countries,” in *Handbook of Income Distribution*, vol. 2A, 688 (Elsevier BV 2015).

27 Javier Lopez Gonzalez, Przemysław Kowalski and Pascal Achard, “Trade, global value chains and wage-income inequality,” *OECD Trade Policy Papers*, No. 182 (OECD Publishing, Paris, 2015).

28 Javier Lopez Gonzalez, Przemysław Kowalski and Pascal Achard, “Trade, global value chains and wage-income inequality,” *OECD Trade Policy Papers*, No. 182, 7 (OECD Publishing, Paris, 2015).

29 2030 Agenda on Sustainable Development, Target 10.2.

30 2030 Agenda on Sustainable Development, Targets 10.6 and 10.a.

3.2 Implications of Global Value Chains

Crucially, policies adopted to achieve sustainable development objectives must take into account modern realities of and changes in international trade and production. Facilitated by advances in transportation and communication technologies and liberalization of trade and investment policies, production has become increasingly fragmented in global value chains (GVCs), defined as “the full range of activities that firms and workers perform to bring a product from its conception to its end use and beyond.”³¹ The concept of GVCs captures three characteristics of the modern world economy: (1) “the increasing fragmentation of production across countries;” (2) “the specialization of countries in tasks and business functions rather than specific products;” and (3) “the role of networks, global buyers and global suppliers.”³² These characteristics of trade and production in GVCs present new opportunities and challenges for countries and the firms within them. While myriad questions have arisen regarding appropriate policy strategies to cope with and capitalize on these trends, efforts to collect data on the nature and impacts of GVCs are increasingly helping to provide answers.³³

Some studies indicate that a country’s growth in terms of its participation in GVCs is correlated with higher rates of economic growth in general.³⁴ Such data has prompted policy makers to focus on taking steps to ensure their firms become integrated in those chains.³⁵ Additionally, studies have emphasized the importance of countries expanding and upgrading their roles in GVCs over time,

and increasing the country’s share of value added embedded in exports, as strategies for achieving development objectives.³⁶ Yet success in terms of expanding and upgrading participation in GVCs (within a particular industry or across industries) and increasing domestic value added is not automatic; appropriate policies are important for realizing those outcomes, as well as for ensuring that participation in GVCs produces social and environmental benefits (or, at a minimum, does not result in undue social and environmental harms).³⁷

Notably, some policies to expand and upgrade participation in GVCs align with those identified as being relevant for SDGs 8, 9, and 10. These include supportive measures to build capacity and competitiveness of domestic labor and firms through education and training as well as through improving fundamentals of success such as the availability and reliability of infrastructure and necessary financing; investing (and collaborating with the private sector) in R&D and technology transfer; and creating and nurturing linkages between foreign and domestic firms through permitting (and even actively encouraging) foreign direct investment and employing local content policies to promote or require use of domestic goods, services, and/or labor.³⁸ For policy makers, data on GVCs and a solid understanding of the relevant jurisdiction’s legal and economic picture are key for identifying where and how to design those measures.

31 Efforts to collect more detailed data on GVCs have produced the World Input-Output Database, and the Trade in Value-Added database.

32 Sébastien Miroudot and Koen De Backer, “Mapping Global Value Chains,” (OECD 2012), TAD/TC/WP/RD(2012)9, 4–5.

33 Gary Gereffi and Karina Fernandez-Stark, “Global Value Chain Analysis: A Primer,” (Center on Globalization, Governance and Competitiveness 2011) 4.

34 UNCTAD, “World Investment Report 2013: Global Value Chains: Investment and Trade for Development,” 151. The type of participation also seems to matter. One study found that backward participation (i.e., the extent to which domestic firms use foreign inputs in exports) is not correlated with income level while “countries with higher per capita GDP tend to have higher forward participation ratios” capturing the extent to which a country’s exports are used as inputs in products exported by other countries.

35 See, e.g., *id.* See also Dominique Bruhn, “Global Value Chains and Deep Preferential Trade Agreements: Promoting Trade at the Cost of Domestic Policy Autonomy?,” German Development Institute Discussion Paper 23/2014.

36 UNCTAD, “World Investment Report 2013: Global Value Chains: Investment and Trade for Development,” 170. As UNCTAD notes, increasing the country’s share of domestic value added “should not be equated with upgrading. Upgrading may be one (important) factor behind increasing domestic value added. But even countries with decreasing shares of domestic value added in exports may well be on an upgrading path, if they increasingly participate in GVCs that create higher overall value, or engage in GVC tasks and activities at higher levels of technological sophistication that generate more value in absolute terms but at the same time depend on increasing foreign content in exports.” *Id.* at 172. See also Przemyslaw Kowalski et al., “Participation of Developing Countries in Global Value Chains: Implications for Trade and Trade-Related Policies,” OECD Trade Policy Papers, No. 179 (2015) 32–33 (distinguishing between upgrading and increasing the share of domestic value added).

37 UNCTAD, “World Investment Report 2013: Global Value Chains: Investment and Trade for Development,” 177–191.

38 *Id.* See also Isabelle Ramdoo, “Resource-based Industrialization in Africa: Optimising Linkages and Value Chains in the Extractive Sector,” European Centre for Development Policy Management Discussion Paper No. 179 (2015); Przemyslaw Kowalski et al., “Participation of Developing Countries in Global Value Chains: Implications for Trade and Trade-Related Policies,” OECD Trade Policy Papers, No. 179 (2015) 82–86.

4 International Trade and Investment Treaties and Impacts on Policy Space for Achieving Sustainable Development

As highlighted above, policies aimed at achieving certain SDGs call for a combination of (1) efforts to support development of domestic capacity and (2) efforts to effectively leverage foreign investment to increase the quantity and quality of employment, promote economic diversification, develop critical infrastructure, and increase technology transfer and innovation.

Given the government interventions that are required, it is important to examine existing and possible future limits to policy space that may hinder relevant government actions. The scope of commitments under modern trade and investment treaties (discussed further below in this section) raises questions about whether and to what extent those treaties are consistent with the policies and policy space needed in this new era of sustainable development. While the FfD, the SDGs, and the climate change texts envision an active role for the government in influencing and regulating economic activity, international trade and investment agreements seem to increasingly narrow permissible forms of state intervention. Given these two arguably divergent directions governments are currently heading in, it is therefore crucial to query whether trade and investment treaties leave domestic governments adequate policy space to achieve agreed upon development objectives and what policy options may exist to preserve and make good use of this policy space.

The Action Agenda on FfD and the 2030 Agenda on Sustainable Development each recognize these issues. The Action Agenda on FfD, for example, states:

*The goal of protecting and encouraging investment should not affect our ability to pursue public policy objectives. We will endeavour to craft trade and investment agreements with appropriate safeguards so as not to constrain domestic policies and regulation in the public interest.*³⁹

The 2030 Agenda on Sustainable Development similarly addresses the need to comply with restraints imposed by international law, and the related need to ensure that international law rules do not unduly impose on domestic policy space:

*We will respect each country's policy space and leadership to implement policies for poverty eradication and sustainable development, while remaining consistent with relevant international rules and commitments. At the same time, national development efforts need to be supported by an enabling international economic environment, including coherent and mutually supporting world trade, monetary and financial systems, and strengthened and enhanced global economic governance. ... We commit to pursuing policy coherence and an enabling environment for sustainable development at all levels and by all actors, and to reinvigorating the Global Partnership for Sustainable Development.*⁴⁰

The importance of ensuring policy coherence between domestic and international law frameworks, and safeguarding crucial areas of domestic policy space, is therefore widely agreed. The challenge is in implementing those aims at both the domestic and international levels.

This section thus seeks to identify the extent of that challenge. It begins by highlighting the key features of relevant WTO rules that restrict the use of certain supportive policies and local content measures. Those multilateral rules, established roughly 20 years ago, now form a baseline (with certain exceptions and flexibilities granted to low income countries) agreed to by over 160 countries.

Against that backdrop, this section then turns to examine IIAs and, in particular, the “WTO+” prohibitions that IIAs increasingly place on a wider range of policy tools designed to support domestic industry and efforts to harness foreign investment for domestic benefits.

39 Para. 91.

40 Para. 63.

4.1 Overview of key World Trade Organization Rules

With the entry into force of the WTO in 1995, Member States committed to abide by a set of agreements that, among other things, place certain restrictions on investment-related measures. Relevant agreements are the Agreement on Trade-Related Investment Measures (TRIMs Agreement),⁴¹ the Agreement on Subsidies and Countervailing Measures (SCM Agreement), and the General Agreement on Trade in Services (GATS). These agreements – the policy restraints they impose, the exceptions they include, and the mechanisms for enforcing their provisions – are discussed briefly below.

4.1.1 TRIMs Agreement

Scope

The TRIMs Agreement restricts countries' use of certain types of performance requirements that apply to trade in goods. It covers two main types of measures: (1) measures that require firms (whether domestic- or foreign-owned) to use local goods, thereby discriminating against like products from other WTO Member States; and (2) measures that impose quantitative restrictions on imports or exports of goods.

The TRIMs Agreement therefore limits the ability of WTO Members to promote domestic economic activities by requiring firms to use local goods or barring firms from exporting unprocessed raw materials; WTO Members are left to encourage those activities by other policy tools such as supporting the competitiveness of their local goods producers. However, the TRIMs Agreement leaves a variety of local content measures untouched such as measures requiring use of local service providers, technology transfers, joint ventures or domestic equity participation, and location of certain activities in the host country or a particular region of the host country.

41 The TRIMs Agreement did not establish new disciplines on performance requirements but codified certain prohibitions on performance requirements that had previously been interpreted to be inconsistent with the 1947 General Agreement on Tariffs and Trade (GATT)'s articles on national treatment (Article III) and quantitative restrictions (Article XI).

Exceptions

The TRIMs Agreement incorporates exceptions in the GATT, including the GATT's general exceptions, an exception for government procurement, and certain flexibilities for developing countries.

Enforcement

Violations of the TRIMs Agreement are enforced through state-to-state dispute resolution under the WTO's dispute settlement system. Because of reluctance to incur political or resource costs of bringing claims, measures arguably inconsistent with the TRIMs Agreement may go unchallenged.

4.1.2 SCM Agreement

Scope

The SCM Agreement prevents WTO Member States from granting certain subsidies to firms within their borders. Two types of subsidies are flatly prohibited: (1) subsidies that are contingent on export performance; and (2) subsidies that are contingent on use of local goods. Other subsidies are not prohibited but are "actionable" if they cause "adverse effects" to the interests of another WTO Member. Establishing "adverse effects" involves a complex, fact-specific inquiry that may make successful challenges difficult.⁴²

Under these provisions, grants, loans, equity infusions, fiscal incentives, and other measures provided by the government and designed to support development and growth of local industries may be restricted under the WTO, and are obviously WTO-inconsistent if they are contingent on export performance or have provisions requiring use of local goods.

Exceptions

The SCM Agreement, unlike the TRIMs Agreement, does not incorporate exceptions from the GATT. Nevertheless, it does include certain flexibilities for developing coun-

42 Under one recent case against the United States, subsidies for R&D that were particularly effective in promoting rapid development of new and improved product lines were deemed to violate the SCM Agreement because they had "adverse effects" on competing products produced by another WTO Member. Panel Report, *United States—Measures Affecting Trade in Large Civil Aircraft*, para. 7.1764, WT/DS353/R (Mar. 31, 2011). The panel's findings were later upheld on appeal. Appellate Body Report, *United States—Measures Affecting Trade in Large Civil Aircraft*, paras. 960–1012, WT/DS353/AB/R (Mar. 12, 2012).

tries. For example, least-developed countries and other countries with a Gross National Product of less than \$1000 per capita are not bound by the SCM Agreement's restrictions on export subsidies. Additionally, special rules apply regarding the measures that can be taken against developing countries if they are found to have violated the SCM Agreement.

Enforcement

Alleged violations of the SCM Agreement can be challenged through the WTO's dispute settlement system. In certain circumstances, WTO Members can also impose "countervailing measures" on subsidized imports of another Member State.

4.1.3 GATS

Scope

As explained above, the TRIMs Agreement only covers investment measures that affect trade in goods. Measures that affect trade in services – including trade that occurs through foreign investment – are covered under a separate WTO agreement, the GATS.

The GATS covers foreign investment in services as one of four modes of supply of services. This is "Mode 3" on "commercial presence" (e.g., foreign direct investment) by the service provider of one WTO Member in the territory of another WTO Member receiving the service.⁴³ Core provisions of the GATS that restrict states' abilities to impose local content policies on investments in services are its articles on market access and national treatment.

First, the GATS' article on market access (Article XVI) prevents Members from applying measures that:

- a) limit the number of service suppliers,
- b) limit the total value of service transactions or assets,
- c) limit the total number of service operations or quantity of service output,
- d) limit the total number of natural persons permitted to be employed,
- e) restrict or require certain types of legal entities or joint ventures, or
- f) limit the participation of foreign capital.

Subparagraphs (a)–(d) prohibit measures that could be used to protect domestic service suppliers (individuals and firms) by limiting foreign investors' ability to access the host country's market; subparagraphs (e) and (f) further restrict countries' abilities to impose certain local content measures on foreign investors seeking to gain market access. Subparagraph (e), which prohibits restrictions on or requirements for investments to be made through certain types of legal entities or joint ventures, can prevent a WTO Member from requiring foreign firms to partner with local companies, or to make an investment through an established subsidiary in the host country; and subparagraph (f), which prevents restrictions on participation of foreign capital, can prevent WTO Members from requiring firms to have a certain percentage of domestic equity.

Second, the GATS national treatment article (Article XVII) requires WTO Members to treat foreign investors no less favorably than domestic investors. This GATS obligation aims to limit the use of protectionist measures that can reduce economic efficiency and harm consumers. It restricts governments' abilities to impose on foreign-owned service firms measures that are not similarly imposed on domestic-owned entities, and to provide domestic-owned entities fiscal, financial, or other incentives that are not similarly provided to foreign-owned firms. These provisions can therefore prevent governments from using various supportive measures to increase the competitiveness of domestic service firms and their ability to integrate and upgrade in domestic and global value chains.

The "Positive List" Approach

One important feature of the GATS is that it adopts a "positive list" approach to its core obligations. In other words, a WTO Member's market access and national treatment obligations under the GATS only apply if and to the extent that the WTO Member has affirmatively "scheduled" the relevant services sector in its Schedule of Commitments. As a result, each WTO Member retains freedom to impose local content requirements that would contravene the market access and national treatment rules of the GATS in service sectors that it has not specifically identified in its schedule.

43 GATS, art. I.

Exceptions

As noted above, even in sectors that are identified in a WTO Member's schedule, certain reservations and exceptions may still allow that country to impose performance requirements otherwise inconsistent with the GATS obligations. In particular, the GATS contains a number of exceptions provisions similar to the GATT, which can protect the use of local content measures in certain circumstances. These include exceptions permitting states to avoid or address balance-of-payments difficulties;⁴⁴ exceptions carving out government procurement from the agreement's obligations;⁴⁵ exceptions for measures necessary to achieve specified policy objectives such as protection of public morals, maintenance of public order, and protection of human, animal or plant life or health;⁴⁶ and measures that states consider necessary to protect their essential security interests.⁴⁷

Enforcement

The GATS, like the TRIMs Agreement, GATT, and SCM Agreement, is enforced through state-to-state proceedings under the WTO's dispute settlement mechanism.

4.1.4 Conclusions Regarding WTO Rules and Restrictions on Policy Space for Local Content

Several WTO agreements – the TRIMs Agreement, SCM Agreement and GATS – restrict the use of certain performance requirements. These restrictions focus to a great extent on preventing measures that discriminate against goods providers located in other WTO Member States in favor of goods providers established within the domestic jurisdiction. The GATS also places certain limits on measures affecting foreign investors, including measures favoring local service suppliers over foreign service suppliers, and measures requiring foreign firms to enter into joint ventures with domestic entities as a condition of market access; yet those GATS provisions only apply to sectors if and to the extent WTO Member States have expressly agreed. Thus, notwithstanding the limits WTO agreements do place on policy space, they also leave

states some degree of flexibility to adopt local content measures, including those:

- providing SCM-Agreement-consistent subsidies or other supports to domestic firms (to the extent there is no relevant GATS commitment);
- requiring or incentivizing use of domestic service suppliers (to the extent there is no relevant GATS commitment) and domestic labor;
- requiring joint ventures or a certain share of domestic equity (to the extent there is no relevant GATS commitment);
- requiring or incentivizing transfers of technology (to the extent there is no relevant GATS commitment);
- restricting exports (through measure other than quantitative restrictions) in order to encourage development of downstream segments of the value chain;
- requiring or incentivizing R&D or other expenditures to be made in the host state; and
- requiring or incentivizing firms to locate their headquarters or particular activities in the host state, or to locate their investment in a particular area in the host state.

As is discussed in section 3.2 below, however, much of this policy space preserved under WTO law is being reduced through IIAs. Additionally, although not discussed in this paper, negotiations on the Trade-in-Services Agreement (TISA) among 23 economies, which is reported to be using a negative list approach for the national treatment obligation, may further erode states' flexibilities to use local content measures.

⁴⁴ Article XII.

⁴⁵ Article XIII.

⁴⁶ Article IV.

⁴⁷ Article XIV.

4.2 Investment Treaties

Alongside the emerging consensus on the role that the public sector must play in guiding and shaping private economic activity for sustainable development, there is another emerging trend: a proliferation of bilateral and multilateral IIAs that constrain the policy flexibility of governments (see Box 1). In brief, IIAs are international agreements between two or more countries that set forth rules regarding host countries' treatment of covered foreign investors and investments. As a general principle, those rules govern conduct by all branches (e.g., executive, legislative, and judicial) and levels (e.g., local, state/provincial, federal/central) of government. In certain circumstances, IIAs also govern conduct of state-owned enterprises (SOEs).⁴⁸

The number of IIAs has skyrocketed in recent years. In the early 1990s, there were only 400 of these agreements. Roughly ten years later, that number had increased to over 2,000.⁴⁹ Presently, there are over 3,000 IIAs, though not all have entered into force. Roughly 2800 of those IIAs are stand-alone bilateral investment treaties (BITs). The remaining IIAs are either multilateral investment treaties, or investment chapters embedded within more comprehensive free trade agreements (FTAs) that, in addition to investment, govern other issues such as trade in goods, trade in services, and protection of intellectual property.

The strongest regulations on local content are increasingly being embodied in these agreements. This section therefore examines IIAs and the ways in which they limit policy space in this area.

There are four main ways in which investment treaties can restrict states' use of local content measures. One is through the non-discrimination provisions that are present in most, if not all, IIAs. Importantly, in a smaller

but growing share of IIAs, these obligations also cover market access issues by preventing discrimination at the "pre-establishment" phase. The second is through core "absolute" standards of protection including, in particular, the "fair and equitable treatment" (FET) obligation.⁵⁰ The FET obligation is similarly present in the vast majority of IIAs, and has been used to challenge measures that have negatively impacted investors' business operations. The third way that IIAs can restrict use of local content measures is through express restrictions on "performance requirements". Although only a minority of IIAs contains express restrictions on performance requirements, those IIAs have deep and broad impacts. Moreover, the number of IIAs with restrictions on performance requirements has been on the rise in recent years. Fourth, IIAs can limit local content measures through restrictions on requirements regarding the nationality of board members and senior management. Like pre-establishment provisions on non-discrimination and restrictions on performance requirements, such provisions on the nationality of board members and senior management are an increasingly common feature of IIAs. Together, and as discussed further below, these four types of restrictions go well beyond the WTO in terms of the types of local content policies that they restrict.

Moreover, the key mechanism for dispute settlement under IIAs is fundamentally different than that under the WTO. IIAs typically give foreign investors direct rights to sue countries to recover damages for violations of investment treaties. These suits take place in arbitration proceedings referred to as "investor-state dispute settlement" (ISDS). A broad range of foreign investors who have direct investments, portfolio investments, loans, franchises, licenses, contracts, intellectual property or other assets in the host state can potentially sue that state and recover damages for alleged violations of IIAs. In contrast, under the WTO, allegations of breach are resolved through state-to-state proceedings, and compensation need not be paid for past harms resulting from violations of WTO commitments.

48 Some IIAs will set forth their own specific rules regarding the circumstances under which conduct by an SOE can lead to state liability under an IIA. Absent explicit rules in the treaty on that issue, arbitral tribunals tend to apply the International Law Commission's Articles on the Responsibility of States for Internationally Wrongful Acts to determine whether conduct of an SOE will be attributable to the government and give rise to state liability.

49 Cancun WTO Ministerial 2003, *Trade and Investment: From Bilaterals to a Multilateral Agreement?*, available at www.wto.org/english/thewto_e/minist_e/min03_e/brief_e/brief07_e.htm.

50 "Relative" standards of protection are those for which the treatment owed to foreign investors and investments depends on the treatment provided to domestic investors and investments. Foreign investors and investments must not be treated less favorably than domestic investors or investments, but are not entitled to better treatment. In contrast, "absolute" standards require host states to provide foreign investors and investments a certain degree of protection irrespective of whether domestic investors and investments are entitled to or receive the same treatment.

Over roughly the past 20 years, the number of publicly known ISDS claims have increased in number from less than 10 to nearly 700.⁵¹ Known ISDS cases now surpass the number of WTO disputes that have been initiated.⁵² And given that disputes can remain confidential, this count of roughly 700 ISDS disputes likely does not capture the full amount of such cases.

Importantly, the respective interests of different state parties to the WTO may align more closely regarding interpretation and application of WTO agreements than the respective interests of investors and states regarding interpretation and application of IIAs. This, in turn has implications for the frequency of disputes and interpretations of treaty obligations. Under the WTO, for example, notwithstanding complaints by State A's firms regarding a measure adopted by State B, State A may have various diplomatic and policy reasons for not challenging State B's allegedly WTO-inconsistent measure. Those reasons might include that State A maintains a similar measure to State B and shares State B's perception regarding the legitimacy of those measures. If there is an IIA between State A and State B, however, a firm from State A could bring a claim against State B to challenge that measure and, in the ISDS proceedings, might advance (and secure tribunal acceptance of) an interpretation of the IIA that is in the investor's interest, but might not necessarily align with the interpretation of the IIA held by either State A or B.

Any consideration of the impact of IIAs' obligations must also take into account the role of ISDS in treaty interpretation and enforcement.

4.2.1 Scope of IIA Obligations

As noted briefly above, there are four main ways in which IIAs' obligations restrict the use of local content measures. This section describes those four channels in more detail.

Non-Discrimination

Like the GATS, investment treaties contain national and most-favored nation treatment provisions prohibiting discrimination against foreign-owned or foreign-based entities. While the GATS prohibits discrimination between "like service suppliers", investment treaties restrict discrimination between "like investors" and/or "like investments". Moreover, while the GATS applies on a "positive list" basis, only imposing restrictions if and to the extent a service sector is scheduled, the national treatment obligation in IIAs typically covers all sectors and activities unless an exception is included in the treaty.

As is described further below, there are various ways through which practices and policies relating to local content measures may breach these types of non-discrimination provisions in IIAs. Government initiatives that accord disparate treatment to investors or investments based on their ownership and their sourcing raise the most obvious concerns.

Differential treatment based on ownership of firms and/or their sourcing of inputs

Measures that provide permissions, preferences, subsidies or other supports to domestic-owned firms but not to foreign-owned firms based on ownership-related criteria would likely be inconsistent with a national treatment obligation. Such measures could include rules restricting who may operate certain businesses, as well as tax breaks, preferential consideration in tenders, or other preferences or advantages offered to firms owned by any domestic citizens, or special groups such as indigenous or socially or economically disadvantaged groups within the country. Preferences or advantages available to domestic SOEs that are not likewise available to private firms may similarly violate the national treatment obligation,⁵³ as might

51 UNCTAD, Investor-State Dispute Settlement Navigator, <http://investmentpolicyhub.unctad.org/ISDS> (listing, on February 10, 2016, 696 cases).

52 According to the WTO's publication, "WTO Dispute Settlement: Resolving Trade Disputes between WTO Members," WTO Member States had brought 488 cases to the WTO's dispute settlement system as of the end of 2014; roughly half of those cases were resolved through consultations. See https://www.wto.org/english/thewto_e/20y_e/dispute_brochure20y_e.pdf.

53 See, e.g., *United Parcel Service of America v. Canada*, Award, May 24, 2007. This case involved a claim by a US investor that Canada violated the national treatment obligation by providing more favorable treatment to a Canadian SOE than to the US company with respect to their provision of postal and courier services. The fact that the Canadian company was state-owned did not, by itself, mean that the company was "unlike" privately owned companies.

restrictions on investments by foreign-owned SOEs that do not similarly apply to privately owned firms (whether foreign or domestic).⁵⁴

Additionally, measures that *indirectly* favor local firms by providing subsidies or other supports to any firm (domestic or foreign) that purchases or accords a preference to goods or services produced by locally owned entities would also likely breach the national treatment obligation.

As noted above, to the extent these measures favor production of goods in the host country, they may also be barred under the TRIMs Agreement. Depending on the relevant country's schedule of commitments under the GATS, measures favoring domestic service providers that would be barred under the national treatment provision in IIAs may also have already been prohibited under the GATS. Yet although there is some overlap between national treatment obligations under IIAs and those under the WTO agreements, important distinctions between the two systems are (1) their different dispute settlement mechanisms, and (2) that IIAs cover all sectors and activities (whether related to goods or services) on a negative list basis. The practical effect of these differences is that IIAs produce a further reduction of policy space relevant for local content measures.

BOX 4

Issue of Specific Investor-State Contracts and Incentives Packages

In some cases, an investor enters into a specific agreement with the government in which the investor commits to make a certain contribution to the local economy through local sourcing, local hiring, employee training, development of economic activities or other undertakings. In exchange for those and potentially other commitments, the investor is given certain benefits such as market access or fiscal and financial incentives. These types of arrangements are often established on a case-by-case basis, and can result in differential treatment of different investors and investments engaged in the same or similar economic activities

such as automobile manufacturing, development of natural resources, generation of renewable energy, or any other industry or activity governments seek to facilitate and encourage.

This differential treatment established through particular investor-state agreements, in turn, may give rise to discrimination claims. An investor that has entered into one investment contract with the host government might argue, for instance, that it is bound to more onerous local sourcing, hiring or training commitments than another domestic or foreign investor that has a similar investment contract with the host government, or that it has not been given the same advantages or benefits in exchange for those commitments. Such disparate treatment, the investor could argue, constitutes improper discrimination between “like” investors. Similarly, if one investor obtains certain advantages such as access rights or incentives pursuant to an investor-state contract in which it also makes commitments for local development, but other investors engaged in the same economic activities are subject to the general regulatory framework which neither requires domestic development commitments nor grants preferential treatment, investors in that latter group might argue that the treatment afforded through the investor-state contract is more favorable than the treatment they receive and breaches the relevant investment treaty's non-discrimination obligations.

The success of such investor claims depends on a range of factors including the specifics of the particular contract or contracts, whether the investors and investments allegedly receiving different treatment are actually “like”;⁵⁵ and whether treatment of one is less favorable than another. But, as illustrated by *Mesa v. Canada*,⁵⁶ investors have spotted these issues, and are raising them

54 See, e.g., Yuri Shima, “The Policy Landscape for International Investment by Government-controlled Investors: A Fact Finding Survey,” OECD Working Papers on International Investment, 2015/01, OECD Publishing; Mark Feldman, “The Standing of State-Owned Entities under Investment Treaties,” in Karl P. Sauvant (ed.), *Yearbook on International Investment Law and Policy 2010–2011* (Oxford University Press 2012).

55 The non-discrimination obligations – national treatment and most-favored nation treatment obligations – bar discrimination between “like” investors or investments. A threshold inquiry for a discrimination claim is therefore whether two or more investors or investments are actually “like” or in “like circumstances”. Governments seeking to accord different treatment to investors based on their impacts on domestic development may argue that investors with different impacts are not “like”; and, indeed, investment tribunals interpreting investment treaties have indicated that the nature and characteristics of investment projects – and their impacts on domestic society – are relevant to determining “likeness” of investors. (See, e.g., *Parkerings-Compagniet AS v. Lithuania*, ICSID Case No. ARB/05/8, Award, September 11, 2007). It is not clear, however, whether all tribunals would follow such an approach or, even if they were open to the argument, what degree of scrutiny they would apply when reviewing assertions that one type of investment provides more development benefits than another. Consequently, and as some governments have done, it may be wise for governments seeking to pursue such development related policies to include relevant clarifications or exceptions in their investment treaties.

56 *Mesa Power Group LLC v. Canada*, PCA Case No. 2012–17.

to challenge local content schemes and incentives offered in connection with investor-state contracts.

In *Mesa v. Canada*, the claimant is a US investor that unsuccessfully participated in a tender to obtain a 20-year fixed-price feed-in-tariff (FIT) contract to sell renewable energy into the Ontario power grid. A key part of Mesa's claims is that Canada violated the NAFTA's non-discrimination obligations by entering into a \$7 billion dollar deal with a "Korean Consortium" of companies. Under that deal, in exchange for commitments by the Consortium to establish local manufacturing facilities, the government gave the Consortium a number of benefits that were not available to investors such as Mesa under the standard procedures and terms of the FIT program. Those contractually agreed benefits enjoyed by the Consortium included preferential access to sell power into the grid and a higher price for energy produced.

According to Mesa, the Korean deal established a non-transparent and privileged legal and business framework for one particular group of investors that discriminated against other investors seeking market access. Canada, in response, has responded that such investor-state contracts are a useful tool for promoting investment and advancing sustainable development objectives like increasing employment and speeding deployment of renewable energy.

As of February 1, 2016, the tribunal had not yet issued a decision on the investor's claims.

To the extent that differential treatment of "like" investors is being effected through these investor-state contracts, such claims may arise more frequently in the future.

Pre-Establishment Reach

Most IIAs only expressly cover investors and investments that are already established in the host country, and leave states relative freedom to determine whether to open their economy to foreign investors in the first place and, if so, to what extent and under what conditions. Some IIAs, however, extend protections to potential foreign investors and investments prior to their establishment in the host country.

When states grant national treatment rights to investors and investments on such a "pre-establishment" basis, they are effectively liberalizing their markets and opening them to foreign investors on the same terms and under the same conditions as domestic investors. In contrast, if national treatment is only accorded to investors who have established their investments, or to established investments, states retain more policy space to determine when, whether and under what circumstances to allow foreign investors to establish investments in their territories.

By including "pre-establishment" protections against discrimination, states thus narrow their abilities to shape the terms and conditions under which potential foreign investors enter their markets. This can include requirements relating to ownership and control (e.g., that foreign firms must have a certain amount of domestic equity or establish a joint venture with a local company), and may also include conditions such as incentives and requirements to transfer technology to or use technology of local firms, establish the company in a particular location, invest in research and development, or reinvest a certain amount of capital in the host country.

Core "Absolute" Standards of Protection

IIAs' substantive standards including, most notably, the FET obligation, prevent states from imposing measures on foreign investors or investments that interfere with investors/investments' rights and, according to some interpretations, their "expectations". Due in particular to the varying approaches tribunals have taken to defining the meaning of the FET obligation and the scope of rights and "expectations" that are protected under that obligation from government interference, it is difficult to identify whether a given government action will violate the standard. Yet as a number of cases have shown, these standards can be used to challenge a range of local content and other measures that increase the cost or reduce the profitability of investors' operations.

Such standards have been used, for example, to challenge aspects of South Africa’s Black Economic Empowerment mining policy which, inter alia, required mining companies to offer to Black or Historically Disadvantaged Individuals 26% of their shares at market price.⁵⁷ They have also been used to challenge conditions, duties and a future ban on copper concentrate that were imposed by Indonesia in an effort to increase domestic processing of copper.⁵⁸ Both proceedings were discontinued before any decision on the merits was reached; thus, it is unclear how a tribunal would have decided the cases. Nevertheless, particularly due to the cost of litigating IIA claims (which are reported to approach \$5 million per case for respondent states),⁵⁹ the mere threat or initiation of a claim may prompt a government to abandon its local content policies.

Express Restrictions on “Performance Requirements”

A small but growing share of IIAs include provisions restricting the use of “performance requirements”. “Performance requirements”, as used in IIAs, include mandatory and incentive-based local content measures. Box 5 provides an example of a recent IIA article on “performance requirements”, which comes from the IIA negotiated between Japan and Mongolia. It is included in full to illustrate the reach of some of these provisions and common language that is used to express the treaty obligations.

Paragraph 1 lists flat government requirements and investor commitments or undertakings that are barred under the IIA; this paragraph does not address performance requirements that are only mandatory as a condition for receiving government advantages such as tax incentives. Such incentive-based performance requirements are still permitted unless they are barred by Paragraph 2.

BOX 5

Example of IIA Article Restricting Performance Requirements

Japan-Mongolia FTA, article 10.7

1. *Neither Party shall impose or enforce any of the following requirements, or enforce any commitment or undertaking, in connection with investment activities of an investor of a Party or of a non-Party in its Area to:*
 - (a) *export a given level or percentage of goods or services;*
 - (b) *achieve a given level or percentage of domestic content;*
 - (c) *purchase, use or accord a preference to goods produced or services provided in its Area, or to purchase goods or services from persons in its Area;*
 - (d) *relate in any way the volume or value of imports to the volume or value of exports or to the amount of foreign exchange inflows associated with an investment of the investor;*
 - (e) *restrict sales of goods or services in its Area that an investment of the investor produces or provides by relating such sales in any way to the volume or value of its exports or foreign exchange earnings;*
 - (f) *restrict the exportation or sale for export;*
 - (g) *appoint, as executives, managers or members of boards of directors, individuals of any particular nationality;*
 - (h) *locate the headquarters of that investor for a specific region or the world market in its Area;*
 - (i) *hire a given number or percentage of its nationals;*
 - (j) *supply one or more of the goods that the investor produces or the services that the investor provides to a specific region or the world market, exclusively from the Area of the former Party; or*
 - (k) *adopt:*
 - (i) *given rate or amount of royalty under a license contract; or*
 - (ii) *a given duration of the term of a license contract,*

with respect to any license contract freely entered into between the investor and a person in its Area, whether it has been entered into or not, provided that the requirement is imposed or the commitment or undertaking is enforced by an exercise of governmental authority of the Party.

Note: A “license contract” referred to in this subparagraph means any license contract concerning transfer of technology, a production process, or other proprietary knowledge.

57 Piero Foresti et al. v. South Africa, ICSID Case No. ARB(AF)/07/1, Award, August 4, 2010.

58 See, e.g., PT Newmont Nusa Tenggara, Press Release: Arbitration Filed Over Export Restrictions in Indonesia (July 1, 2014); Nusa Tenggara Partnership B.V. and PT Newmont Nusa Tenggara v. Indonesia, ICSID Case No. ARB/14/15, Order of the Secretary-General Taking Note of the Discontinuance of the Proceedings, August 29, 2014.

59 Matthew Hodgson, Counting the Costs of Investment Treaty Arbitration, 9 Global Arbitration Review, March 24, 2014 (finding that average costs for respondent states were US\$ 4,437,000 and US\$ 4,559,000 for claimants).

2. Neither Party shall condition the receipt or continued receipt of an advantage, in connection with investment activities of an investor of a Party or of a non-Party in its Area, on compliance with any of the following requirements to:
 - (a) achieve a given level or percentage of domestic content;
 - (b) purchase, use or accord a preference to goods produced or services provided in its Area, or to purchase goods or services from persons in its Area;
 - (c) relate in any way the volume or value of imports to the volume or value of exports or to the amount of foreign exchange inflows associated with an investment of the investor;
 - (d) restrict sales of goods or services in its Area that an investment of the investor produces or provides by relating such sales in any way to the volume or value of its exports or foreign exchange earnings; or
 - (e) restrict the exportation or sale for export.

3. (a) Nothing in paragraph 2 shall be construed to prevent a Party from conditioning the receipt or continued receipt of an advantage, in connection with investment activities of an investor of a Party or of a non-Party in its Area, on compliance with a requirement to locate production, supply a service, train or employ workers, construct or expand particular facilities, or carry out research and development, in its Area.
 - (b) Subparagraph 1(k) shall not apply when the requirement is imposed or the commitment or undertaking is enforced by a court or competition authority to remedy an alleged violation of laws controlling the anti-competitive activities.
 - (c) Subparagraphs 1(a), 1(b), 1(c), 2(a) and 2(b) shall not apply to qualification requirements for goods or services with respect to foreign aid programs.
 - (d) Subparagraphs 2(a) and 2(b) shall not apply to requirements imposed by an importing Party related to the content of goods necessary to qualify for preferential tariffs or preferential quotas.

4. Paragraphs 1 and 2 shall not apply to any requirement other than the requirements set out in those paragraphs.

Restrictions on performance requirements can also be found in many of the other IIAs concluded by Japan as well as IIAs concluded by the United States and Canada with third states or groups of states.⁶⁰ The Trans-Pacific Partnership Agreement (TPP) is one recent and particular notable example of this trend. Concluded in 2015 between Australia, Brunei Darussalam, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, the United States and Vietnam, the TPP, like the excerpt from the agreement between Japan and Mongolia illustrated in Box 5, includes restrictions on a range of flat and incentive-based performance requirements.⁶¹

In addition to Canada, Japan, and the United States, countries with a longer history of seeking to include restrictions on performance requirements in their investment treaties, a wider range of countries and negotiating blocks are also now adopting the same or similar practices of pursuing restrictions on performance requirements in their investment treaties.⁶² The IIA concluded between the European Union and Vietnam in December 2015 is an example of the spread of this practice as European countries had typically not previously included such provisions in their investment treaties. The restrictions on performance requirements in the European Union-Vietnam IIA, however, differ from those that can be found in other agreements in that they only apply on a positive list basis.⁶³

Some IIAs that include these restrictions on performance requirements do so by merely incorporating the TRIMs Agreement. The substantive obligations are therefore no greater than they would be under the WTO, though ISDS makes challenges more likely and enforcement easier.

As illustrated by the Japan-Mongolia FTA, however, a number of IIAs go further, adding TRIMs+ obligations in

60 See, e.g., U.S.-Sri Lanka Bilateral Investment Treaty, May 1, 1993, available at <http://2001-2009.state.gov/documents/organization/43588.pdf>; U.S.-Rwanda Bilateral Investment Treaty, January 1, 2012, available at www.state.gov/documents/organization/101735.pdf.

61 Trans-Pacific Partnership Agreement, art. 9.9.

62 See, e.g., Mexico-Chile Free Trade Agreement, Art. 9-07, available at www.wipo.int/wipolex/en/other_treaties/text.jsp?file_id=196020. See also IISD, *South-South Bilateral Investment Treaties: The Same Old Story?*, available at www.iisd.org/pdf/2011/dci_2010_south_bits.pdf, at 4. See, e.g., the BITs between El Salvador and Peru (1996), the Dominican Republic and Ecuador (1998), and Bolivia and Mexico (1995). UNCTAD Report at 5.

63 European Union-Vietnam FTA, Investment Chapter, art. 4.

their text. These TRIMs+ obligations may include provisions barring states from *imposing* or *enforcing* any:

- Flat⁶⁴ or incentive-based⁶⁵ measure requiring foreign investors to use or accord a preference to local providers of services. These provisions have been interpreted as barring states from requiring investors to make local expenditures on services, including on in-country R&D or education and training.⁶⁶ Following this line of interpretation, it seems that requirements to make domestic expenditures in other activities such as construction or provision of shared-use infrastructure might also be restricted under these provisions (see Boxes 3 and 7).
- Flat or incentive-based measures requiring foreign investors to achieve set levels or percentages of “domestic content.”⁶⁷ “Domestic content” is typically not defined, but can be interpreted broadly as covering measures that can be satisfied through domestic expenditures on labor, services, and/or goods.
- Commitment or requirement for foreign investors to hire a given number or percentage of host country nationals.⁶⁸
- Commitment or requirement for foreign investors to locate their global or regional headquarters in the host country.⁶⁹
- Export restrictions.⁷⁰ While the GATT and TRIMs Agreement prevent quantitative restrictions on exports, some IIAs include a flat prohibition against any restriction on exports, including measures such as taxes and permit conditions on exports. These types of measures restricting exports are tools that could be used by host states, for example, to try to encourage domestic processing of raw materials.
- Commitment or requirement for investors to “transfer a technology, a production process or other proprietary knowledge to a person in its territory.”⁷¹ There is typically no definition of “technology transfer” in these

agreements, but they could be interpreted broadly to include such activities as providing employee training.⁷²

- Terms specifying the royalty under or duration of a license or contract for transfer of technology entered into between a foreign investor and state- or non-state-entity.⁷³ Such provisions can arguably prevent the government from promoting dissemination and application of technologies generated through government- or university-supported R&D programs undertaken with industry. When supporting private R&D, governments often have the right to and do impose certain conditions on intellectual property rights associated with results of the R&D programs in order to maximize use of those resulting technologies. Such IIA provisions seem to restrict those types of practices.

In addition to the sheer scope of these restrictions, there are other aspects of these IIA provisions that are important to highlight.

First, they often prohibit state parties to the IIA from imposing or enforcing performance requirements on *any* investor or foreign investor, not just investors of the other state party. The TPP illustrates; it states that its restrictions on performance requirements “apply to all investments in the territory” of the host state.⁷⁴ When a state signs an agreement containing this type of text, the obligation is effectively multilateralized. While an investor from a state that is not party to the IIA would not be able to enforce this multilateralized obligation, the obligation could potentially be enforced by the other state party (or parties) to the IIA through state-to-state dispute resolution. The multilateralized obligation could also potentially be enforced by a foreign investor covered by the IIA through ISDS proceedings. If, for example, the terms of a government tender called for the government to consider performance on local content metrics when awarding contracts, and an investor covered by the IIA lost its bid for a government contract, that covered investor may be able to challenge the bid process and decision through ISDS on the ground that consideration of local-content-related criteria violated the IIA and led to an improper award.

64 Canada-Benin BIT, art. 10(1)(c).

65 Japan-Mongolia FTA, art. 10.7(2)(b).

66 *Mobil v. Canada*, ICSID Case No. ARB(AF)/07/4, Decision on Liability and Principles of Quantum, May 22, 2012.

67 Japan-Mongolia FTA, art. 10.7(1)(b) & (2)(b); Canada-Benin BIT, art. 10(1)(b) & (3)(b).

68 Japan-Mongolia FTA, art. 10.7(1)(i).

69 Japan-Mongolia FTA, art. 10.7(1)(h).

70 Japan-Mongolia FTA, art. 10.7(1)(f).

71 NAFTA, art. 1106(1)(f).

72 Canada-Benin BIT, art. 10(1)(f).

73 Japan-Mongolia BIT, art. 10.7(1)(k).

74 TPP, art. 9.2(1)(c).

Second, even when an IIA does not include express restrictions on performance requirements, an investor may be able to use the IIA's most-favored nation provision to "import" restrictions on performance requirements from other IIAs the host state has signed. This possibility makes it imperative for states to consider policy coherence across the range of IIAs they have concluded.⁷⁵

Third, the provisions typically make clear that it is not only the imposition of performance requirements through law or regulation that is prohibited, but also the *enforcement of investors' commitments or undertakings* to comply with performance requirements. One implication of such language is that when there is an investor-state contract in which an investor has agreed to comply with certain performance requirements (in exchange for benefits it has negotiated for from the government), a state may later be barred from actually enforcing the investor's obligation. This potentially alters the balance of costs and benefits secured through contract negotiations (see Box 6).

Fourth, as noted above, IIAs differ from WTO-based restrictions on performance requirements in that they allow covered foreign investors to bring claims for breach of these obligations, thus creating a large pool of potential "enforcers" (see Box 7 for examples of ISDS cases, including three ISDS claims by US investors that were brought to challenge a Mexican tax which was also the subject of a WTO dispute between the US and Mexico).⁷⁶ Although claims and decisions alleging violations of these provisions have thus far been relatively limited, that is likely to change due to (1) the growing number of IIAs overall,

and, accordingly, the amount of investors and investment that IIAs cover, (2) the increasing inclusion of restrictions on performance requirements in IIAs, and (3) the overall rise in ISDS claims. As claims and decisions mount, there will likely be (potentially costly) arbitration proceedings to provide further clarification on key terms such as "domestic content",⁷⁷ an "advantage"⁷⁸ and "transfer of technology."⁷⁹ The precise meaning of these terms given by ISDS tribunals will have a significant – and as yet unknown – impact on the scope of government exposure to litigation and liability.

BOX 6

Investor-State Contracts, Local Content Policies, and Enforceability of Commitments

With the rise in contract transparency in investment in extractive industries and land,⁸⁰ it is increasingly possible to see the terms of investor-state contracts. One feature of many of these contracts is a provision or series of provisions on local content, which aim to ensure that the project produces positive spillovers into the domestic economy through job creation, linkage creation, and diversification.

As noted in one study of 12 investor-state contracts regarding agricultural projects in Africa, these deals often have provisions (of varying strength and specificity) requiring local employment, mandating establishment of local outgrower schemes, obliging firms to use or strive to use local providers of goods and services, and/or requiring local processing of agricultural commodities.⁸¹

While these provisions can be key to enabling host countries and communities to benefit from investment projects, there is a risk that IIAs render them unenforceable. This is because provisions in

75 This issue of importation is similar to the first point on multilateralization. Through multilateralized obligations, IIAs provide that state parties may not impose or enforce performance requirements on any investor, not just investors covered by the treaty. In contrast, importation through the MFN provision allows a covered investor to benefit from restrictions on performance requirements contained in other treaties. Thus, while multilateralization expands the reach of a host state's obligations to cover a broad range of investors, including investors not covered by an IIA signed by the host country, importation expands the scope of protections that are enjoyed by covered investors. There are also differences between multilateralization and importation in terms of who can enforce the obligation: A multilateralized obligation in an IIA does not give foreign investors that are not covered by that IIA the right to enforce the IIA's multilateralized restrictions on performance requirements through ISDS. Yet when a foreign investor that is covered by an IIA without any provisions on performance requirements uses the most-favored nation obligation to import restrictions on performance requirements from another IIA, that foreign investor can use the ISDS mechanism in its IIA to enforce the "imported" provisions.

76 Notably, the European Union-Vietnam IIA excludes the obligations on performance requirements from the treaty's ISDS mechanism.

77 "Domestic content" targets set in legislation or contract often are satisfied by expenditures on goods, services, and labor. Thus the term, at least in some contexts, has a broad meaning. The meaning under IIAs is arguably also broad. In particular, as can be seen in the excerpt from the Japan-Mongolia FTA, IIAs often contain (1) restrictions on requirements to use local providers of goods; (2) restrictions on requirements to use local providers of services; and (3) restrictions on targets for "domestic content". In order for "domestic content" to have any meaning in the treaty, it is arguable that it goes beyond use of domestic goods and services, and also prohibits targets on use of domestic labor or other expenditures.

78 See Box 7 (discussion of decision in *Mobil v. Canada*).

79 See Box 1.

80 See, e.g., resourcecontracts.org and openlandcontracts.org.

81 Lorenzo Cotula, *Land Deals in Africa: What is in the Contract?* (IIED 2011) 26–27.

IAs that restrict the use of mandatory performance requirements often not only bar states from both “imposing” local content requirements, but also bar them from “enforcing” Investors’ contractual “commitments or undertakings” to comply with those requirements.

Restrictions on Senior Management and Boards of Directors

A number of more recent IAs contain provisions limiting the types of requirements host states can impose on the nationality or residence of senior management and/or boards of directors. In IAs with these provisions, governments are typically prohibited from requiring that senior management be of any particular nationality; neverthe-

less, governments commonly retain some measure of freedom to require that a majority of the board of directors be nationals or residents of the host state, “provided that the requirement does not materially impair the ability of the investor to exercise control over its investment.”⁸² Having board members be resident in the host country can help increase the value added of and spillovers generated by activities of that affiliate in the host country, and can also help promote management decisions beneficial to the host country.

Table 7 below summarizes the restrictions that WTO agreements and IAs – depending on the language of the particular agreement – may impose on local content measures and supportive policies.

TABLE 7 Local Content Measures, Supportive Policies, and Restrictions under WTO Law and IAs

Local Content and Supportive Policies	International Law Restrictions
<p>Basic local content requirements – measures that require or encourage inventors/investments to use a certain amount or proportion of local resources (including labor, services, materials and parts) when producing goods or providing services</p>	<p>TRIMs Agreement –</p> <ul style="list-style-type: none"> • prevents local measures mandating or making incentives contingent upon use of local goods • prevents quantitative restrictions on imports that can be used to favor local goods <p>GATS – <i>if and to the extent the service sector is sector is scheduled</i>, the GATS prevents requirements that would favor use of domestically owned service providers over foreign-owned service providers</p> <p>IAs can –</p> <ul style="list-style-type: none"> • prevent mandatory and incentive-based measures requiring foreign investors to achieve a level or percentage of domestic content through expenditures on domestic labor, goods, and services • prevent states from requiring or, in some cases incentivizing, investors to use or accord a preference to local providers of goods or services • prevent states from requiring use of domestic labor • prevent states from requiring investors to make in-country expenditures (including intra-firm expenditures) on services such as company expenditures on R&D or education and training • bar enforcement of contractual provisions containing commitments by investors to comply with any of these requirements • result in liability for any measure that has the effect of discriminating against the operation or, in some cases, establishment of foreign-owned investments in the host country, or that otherwise negatively affects the operations or establishment of foreign-owned investments.

82 See, e.g., Canada-Benin BIT, art. 9; Canada-Peru FTA, art. 806(2); NAFTA, art. 1107.

Local Content and Supportive Policies	International Law Restrictions
<p>Export restraints including quantitative restrictions, export taxes, or other restraints used to require or encourage domestic value-added;</p>	<p>TRIMs Agreement – prevents quantitative restrictions on exports that can be used to promote or require domestic beneficiation/processing.</p> <p>IAs – can prevent a broader array of restrictions on exports through restrictions on performance requirements or, depending on the effects of the measure on the investor’s operations, the FET or other substantive obligations.</p>
<p>Joint venture requirements requiring foreign investors to partner with domestic firms or other entities such as research institutions;</p>	<p>GATS – <i>if and to the extent the service sector is scheduled</i>, prevents states from imposing restrictions or requirements on the type of foreign-owned entity established in the host country, including requirements that investments be made through joint ventures.</p> <p>IAs – prohibit joint venture requirements if the IAs provide <i>pre-establishment</i> national treatment protections (and no relevant exceptions are included in the treaty). Under the national treatment, FET or other substantive provisions, IAs may also restrict introduction of joint venture requirements if a foreign firm has already been established and is operating and is then made subject to the joint venture requirements.</p>
<p>Local management requirements requiring nationals to be on boards or in senior management;</p>	<p>IAs – may prohibit requirements regarding the nationality of senior management but have typically permitted requirements on the nationality or residence of members of boards of directors.</p>
<p>Local equity requirements requiring firms to have a certain share of domestic ownership; and</p> <p>Location requirements requiring companies to locate their global or regional headquarters or certain other operations (e.g., R&D operations) in the host state, or to establish operations in a particular location in the host state (e.g., in underdeveloped regions)</p> <p>Supportive policies such as subsidies designed to help support development of local businesses (all businesses, SMEs, minority-owned businesses, etc.)</p>	<p>GATS – <i>if and to the extent the service sector is scheduled</i>, prevents states from imposing domestic equity requirements.</p> <p>IAs – prevent local equity requirements if the IAs provide <i>pre-establishment</i> national treatment protections (and no relevant exceptions are included in the treaty). Under the national treatment, FET or other substantive provisions, the IAs may also restrict introduction of local equity requirements if a foreign firm has already been established and is operating and is then made subject to the joint venture requirements.</p> <p>IAs may –</p> <ul style="list-style-type: none"> • expressly prevent these requirements in their restrictions on performance requirements • be interpreted to prevent these requirements due to restrictions on requirements/incentives to “use” local services or achieve “domestic content”. As suggested in at least one arbitral decision, IIA provisions preventing requirements on investors to use or accord a preference to local providers of goods or services may prohibit measures requiring R&D, headquarters, or other operations to be located in the host country. <p>SCM Agreement – prevents use of subsidies that are contingent on use of local goods or that cause “adverse effects” to the interests of other WTO Members.</p> <p>GATS – <i>if and to the extent the service sector is scheduled</i>, the GATS prevents subsidies that are given to domestically owned service firms but not provided to foreign-owned firms; it may also prevent subsidies given to domestically incorporated firms that are not given to service firms located abroad but providing services in the country.</p> <p>IAs – non-discrimination provisions will restrict governments’ abilities to provide subsidies or other supports to domestically owned firms that aren’t similarly provided to foreign-owned firms.</p>

4.2.2 Exceptions

As noted above, IIAs generally apply to all investments in all sectors unless the treaty states otherwise. Most investment treaties have contained no or only very limited exceptions to their provisions, although the number of exceptions is growing in recent treaties. Among the more common of these still limited exceptions have been provisions protecting governments' abilities to take measures necessary to protect their "essential security" interests, and measures carving out taxation measures from some or all of the agreement.

In more recent agreements states have begun to include exceptions or reservations that can help protect some measure of policy space. These include:

- Exceptions to their pre- and post-establishment national treatment obligations for advantages or preferences given to indigenous peoples or historically disadvantaged groups; governments subsidies; government procurement; and certain social services;

EXAMPLE: Canada's reservations to the TPP's provisions on non-discrimination, performance requirements, and senior management and boards of directors include the following carve-outs for existing and future measures:

*Canada reserves the right to adopt or maintain a measure denying investors ... and their investments, or service providers of a Party, any rights or preferences provided to aboriginal peoples.*⁸³

*Canada reserves the right to adopt or maintain a measure conferring rights or privileges to a socially or economically disadvantaged minority.*⁸⁴

- Exceptions to restrictions on performance requirements for environmental, health or other specified objectives;

EXAMPLE: The TPP includes the following exception to its restrictions on performance requirements:

Provided that such measures are not applied in an arbitrary or unjustifiable manner, or do not constitute a disguised restriction on international trade or investment, paragraphs 1(b) [prohibiting domestic content requirements], 1(c) [prohibiting requirements to use or accord a preference to locally produced goods], 1(f) [prohibiting technology transfer requirements], 2(a) [prohibiting incentives tied to compliance with domestic content requirements] and 2(b) [prohibiting incentives tied to compliance with requirements to use or accord a preference to locally produced goods] shall not be construed to prevent a Party from adopting or maintaining measures, including environmental measures:

*(i) necessary to secure compliance with laws and regulations that are not inconsistent with this Agreement; (ii) necessary to protect human, animal or plant life or health; or (iii) related to the conservation of living or non-living exhaustible natural resources.*⁸⁵

- And exceptions to restrictions on requirements regarding senior management and boards of directors for investments receiving particular government benefits, and investments in particular industries or activities.

EXAMPLE: In the TPP, the states included the following exception:

*Article 9.4 (National Treatment), Article 9.5 (Most-Favoured-Nation Treatment) and Article 9.10 (Senior Management and Board of Directors) shall not apply to: (a) government procurement; or (b) subsidies or grants provided by a Party, including government-supported loans, guarantees and insurance.*⁸⁶

Individual countries also included specific exceptions to this obligation, including exceptions for certain investments over a particular size in agriculture, investments in various categories of public services, and investments in formerly state-owned enterprises.⁸⁷

⁸⁵ TPP, art. 9.9(3)(d).

⁸⁶ TPP, art. 9.11(6).

⁸⁷ TPP, Annex II, Schedule of Australia.

⁸³ TPP, Annex II, Schedule of Canada, at 2.

⁸⁴ TPP, Annex II, Schedule of Canada, at 6.

Nevertheless, the vast majority of existing IIAs contain no or only very limited exceptions to the national treatment requirements and no or only very few exceptions to substantive obligations such as the FET obligation which, as described above, can impose significant restraints on governments' abilities to use local content measures and supportive policies to help ensure the effectiveness of such measures.

BOX 7

ISDS Cases Finding Governments Liable for Using Performance Requirements

To date, there have only been a limited number of publicly known ISDS cases in which investors have claimed that the host government violated an IIA's restrictions on performance requirements. Almost all of those 12 cases have been brought under the North American Free Trade Agreement (NAFTA), concluded between the United States, Canada and Mexico.⁸⁸

Of those 12, the investor succeeded on its claims that the government imposed prohibited performance requirements in three disputes.⁸⁹ Those cases are discussed below.

The "Corn Products" Cases

Two of the cases in which investors prevailed on their performance requirements claims involved claims against Mexico relating to a 20% tax it imposed on beverages and other products that contained sweeteners other than cane sugar such as high fructose corn syrup (HFCS).⁹⁰ When the tax was imposed, HFCS was either produced outside of Mexico, or by primarily foreign-owned firms in Mexico; in contrast, cane sugar was produced by Mexican-owned companies in Mexico.⁹¹ Justifications given for the tax were that it was needed to address a deepening crisis in

Mexico's domestic sugar industry, which had been driven in part by increased imports of HFCS from the United States, and restrictions the US placed on imports of Mexican cane sugar into the US market.⁹²

In 2004 and 2005, several US investors initiated arbitration against Mexico challenging Mexico's tax under the NAFTA. (The US also challenged the tax before the WTO, and received a favorable panel decision in October 2005;⁹³ Mexico subsequently, and unsuccessfully, challenged the WTO panel's findings.⁹⁴) Mexico repealed the tax on January 1, 2007.

A US investor that brought one of the ISDS cases, Cargill, Inc., produced HFCS in the United States and had established a subsidiary and distribution centers in Mexico to sell and distribute HFCS in the Mexican market. Cargill argued that Mexico's tax made the use of HFCS prohibitively expensive and effectively destroyed its sales and distribution business in Mexico. In its performance requirements claim, Cargill asserted that the tax violated Article 1106 of the NAFTA, which states in part:

3. No Party may condition the receipt or continued receipt of an advantage, in connection with an investment in its territory of an investor of a Party or of a non-Party, on compliance with any of the following requirements:

...

(b) to purchase, use or accord a preference to goods produced in its territory, or to purchase goods from producers in its territory[.]⁹⁵

According to Cargill, although the tax was imposed on firms operating in the downstream segment of the value chain (producing soft drinks) and did not directly apply to Cargill's upstream operations or products (selling and distributing HFCS to beverage companies), the tax was prohibited under Article 1106 because it provided an advantage (i.e., the opportunity to avoid the tax) conditioned on use of domestically produced cane sugar.

88 Data on the number of cases in which investors alleged violation of IIAs' articles on performance requirements, and on the status and outcome of those cases, comes from UNCTAD's database of ISDS cases, available at <http://investmentpolicyhub.unctad.org/ISDS>.

89 In four of the 12 cases, the investor prevailed on other claims of IIA breach, but not on its arguments that the host state breached the treaty's restrictions on performance requirements. In two of the cases, the investor did not prevail on any of its claims. One of the cases settled; another was discontinued; and another is still pending. This data is drawn from UNCTAD's database on ISDS claims (as of December 15, 2015), <http://investmentpolicyhub.unctad.org/ISDS/FilterByBreaches>.

90 Archer Daniels Midland Company (ADM) v. Mexico, ICSID Case No. ARB(AF)/04/05, Award, November 21, 2007; Cargill, Inc. v. United States, ICSID Case No. ARB(AF)/04/05, Award, September 18, 2009.

91 Cargill, at 105–106.

92 Id. at paras. 62–100.

93 Mexico – Tax Measures on Soft Drinks and Other Beverages, WT/DS308/R (issued October 7, 2005, adopted by the DSB as modified by the Appellate Body, on March 24, 2006).

94 Mexico – Tax Measures on Soft Drinks and Other Beverages, WT/DS308/AB/R, March 24, 2006.

95 NAFTA, art. 1106.

In a 2009 award, the ISDS tribunal agreed with Cargill's arguments. The tribunal's decision shows that performance requirements designed to support one segment of the value chain (e.g., upstream agricultural producers) can result in liability if those requirements negatively affect foreign investors in other segments of that chain (e.g., downstream distributors).

The *Cargill* tribunal ordered Mexico to pay Cargill over US\$ 77 million in damages plus interest, which included losses suffered by Cargill's operations in Mexico, as well as losses of Cargill's production facilities in the United States.⁹⁶

In the other "Corn Products" case finding that Mexico's tax violated the NAFTA's restrictions on performance requirements, the claimants were US companies that had invested in a Mexican subsidiary to produce and sell HFCS in Mexico. In a 2006 decision, the tribunal ordered Mexico to pay the claimants roughly US\$ 33.5 million as compensation for breach of NAFTA Article 1106 as well as breach of the NAFTA's national treatment obligation.⁹⁷

There was a third case brought against Mexico challenging this tax, *Corn Products International v. Mexico*.⁹⁸ In a 2009 decision, the tribunal determined that Mexico's tax violated the NAFTA's national treatment obligation, but rejected the investor's arguments that Mexico had violated the NAFTA's restrictions on performance requirements.⁹⁹ The fact that this tribunal decided against the investor on its performance requirements claims, while the other two ISDS tribunals found that the same Mexican tax violated the NAFTA's restrictions on performance requirements, helps illustrate the inconsistencies that can arise in ISDS disputes, and the difficulties in predicting their outcomes. The *Corn Products* tribunal ordered Mexico to pay the investor US\$ 58 million in damages based on the national treatment violation.¹⁰⁰

Mobil v. Canada

The third case holding a state liable for imposing prohibited performance requirements involved a case against Canada challenging requirements on investors in the offshore oil and gas industry to invest in R&D and education and training (E&T) in the host country.¹⁰¹

When oil was discovered off the coast of Newfoundland (NL) in Canada in the late 1970s, the government of NL and the federal government of Canada adopted legislation (the "Accord Acts") seeking to ensure development of those oil resources was used to catalyze sustainable growth and development. Part of that legislation requires any petroleum operator looking to be licensed for activities in the area to submit and secure approval of a Development Plan, which lays out the general approach for developing an oil field, and a Benefits Plan explaining how NL and Canada would benefit from the project. Among other things, the Benefits Plan has to set forth the company's plans for conducting R&D and E&T in the area. The legislation also established a board (the "Board") to ensure compliance with the Accord Acts requirements.

When the NAFTA came into force in 1994, Canada included the Accord Acts (and subordinate measures adopted pursuant to this legislation) as part of its schedule of "non-conforming measures", exempting it from the treaty's restrictions on performance requirements.

In 2004, the Board issued guidelines seeking to strengthen companies' contributions to R&D and E&T. Shortly thereafter, two US companies, each of which indirectly owned minority shareholdings in two offshore oilfields in NL that were governed by the Accord Acts, challenged the guidelines before Canadian courts as impermissibly expanding the companies' obligations. Those Canadian courts, however, rejected the companies' arguments, determining that the Board had acted within its authority under the Accord Acts to "monitor research and development expenditures and intervene by issuing guidelines requiring higher expenditures should the [companies'] level of expenditures fall below that which the Board considered appropriate."¹⁰²

96 The United States, Canada, and Mexico all objected to the portion of the tribunal's decision determining that damages should include losses suffered by Cargill's investments in the United States. In addition to finding that Mexico violated Article 1106 of the NAFTA, the tribunal determined that it breached the treaty's national treatment and FET obligations. *Cargill*, at 160.

97 *ADM*, at 93.

98 ICSID Case No. ARB(AF)/04/1, Award, August 18, 2009.

99 *Id.* at paras. 79-80.

100 UNCTAD, Investment Policy Hub, ISDS Database (as of December 15, 2015), available at <http://investmentpolicyhub.unctad.org/ISDS/Details/166>.

101 *Mobil v. Canada*, ICSID Case No. ARB(AF)/07/4, Canada's Counter-Memorial, December 1, 2009, para. 14.

102 *Mobil Investments and Murphy Oil v. Canada*, ICSID Case No. ARB(AF)/07/4, Canada's Counter-Memorial, December 1, 2009, para. 6 (citing a decision by the Canadian Court of Appeal).

Subsequently, in 2007, the companies filed a case against Canada under the NAFTA, arguing that the strengthened guidelines requiring investors to conduct R&D and E&T in Canada violated the NAFTA's restrictions on performance requirements. More specifically, the companies argued that the guidelines violated the treaty's provision prohibiting states from "*impos[ing] or enforc[ing] ... requirements ... to purchase, use or accord a preference to goods produced or services provided in its territory, or to purchase goods or services from persons in its territory.*" [NAFTA, Art. 1106(1)(c)].

The tribunal of three arbitrators appointed to decide this dispute agreed with the claimants. The arbitrators concluded that R&D and E&T are "services", and that requirements to *make local expenditures* on those services as a condition of receiving development approvals constituted requirements to *purchase or use services in the host country* in violation of the NAFTA. A majority of the tribunal also determined that the guidelines were not protected by Canada's reservation for non-conforming measures. Two of the three arbitrators determined that, although Canada had carved out the Accord Acts (and "subordinate measures") from the NAFTA's restrictions on performance requirements, the Board's guidelines represented such a significant change as compared to prior practice that the guidelines could not be considered to be "subordinate measures" similarly protected by the carve-out for non-conforming measures.¹⁰³

The tribunal subsequently ordered Canada to pay CDN\$ 17 million to the companies as compensation for the unlawful performance requirements.¹⁰⁴

This decision illustrates several key issues. One is that the tribunal apparently considered the R&D and E&T requirements to be mandatory obligations, as opposed to conditions imposed on investors in order to gain a particular "advantage" (i.e., the "advantage" of securing eligibility for development approvals). As noted above, IIA provisions on performance requirements often prohibit a wide range of flat, mandatory local content measures, but may permit local content measures if relevant requirements are imposed as a condition for the investor to obtain an "advantage". Under the NAFTA, for example, requirements to purchase, use, or accord a preference to local services are not barred if those requirements are imposed as a condition in order to obtain an

"advantage". Thus, the meaning of an "advantage" is key for assessing the scope of IIA restrictions.

A second issue illustrated by *Mobil* is the wide interpretations given by the tribunal to the term "services" and to the meaning of requirements to "purchase" or "use" a service of a domestic provider. On that latter point, the tribunal seemed to equate domestic *expenditures* on services (even intra-firm expenditures) with *purchase or use* of services from local providers.

A third issue highlighted by *Mobil* is the importance and difficulty of appropriately listing non-conforming measures in schedules designed to maintain a degree of policy space in "negative list" IIAs.

4.3 Summary of Trends in International Law Toward Policy Space for Local Content Measures

As shown above, with entry into force of the WTO, Member States committed to a number of obligations that limited their ability to accord preferences to domestic economic actors. Measures restricted under the WTO include provisions that discriminate against foreign-manufactured goods in favor of locally produced items and, to the extent states have consented, measures that discriminate against foreign-owned or foreign-based service suppliers to the benefit of locally owned or locally established services firms.

Yet under WTO law, states have retained significant freedom to use non-discriminatory subsidies to support development and improve the competitiveness of domestic industry, to spur development in disadvantaged regions, and to provide preferential treatment to minorities, indigenous communities, or other groups entitled to special treatment under domestic or international human rights law; to control terms of market access (unless they had agreed otherwise) and condition access and operations on compliance with joint venture, domestic equity, or other local content requirements; to require or encourage technology transfer through various policies; to encourage or require local hiring; and to encourage or require R&D to be conducted within their territories.

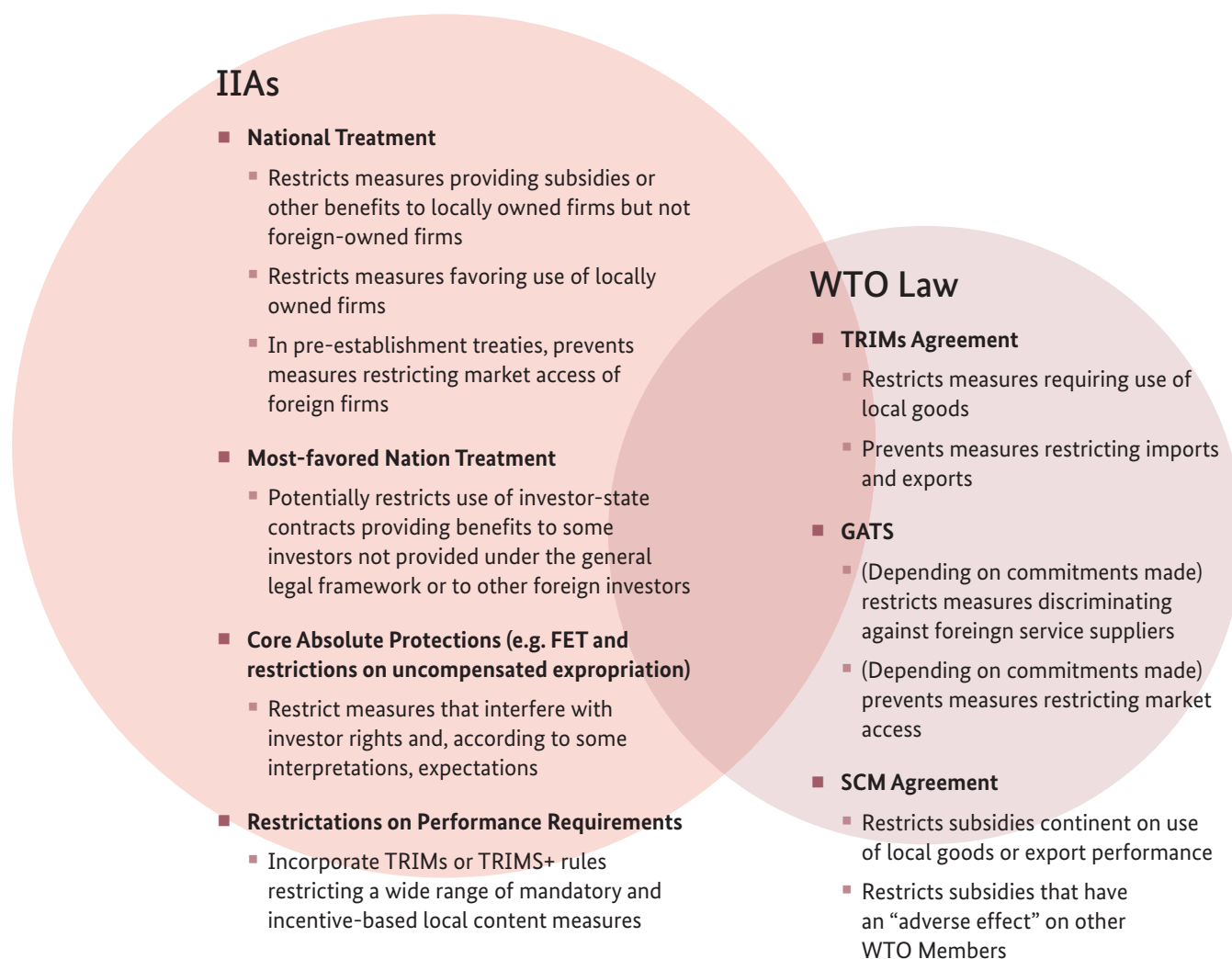
103 *Mobil Investments and Murphy Oil v. Canada*, ICSID Case No. ARB(AF)/07/4, Decision on Liability and Principles of Quantum, May 22, 2012.

104 *Mobil Investments and Murphy Oil v. Canada*, ICSID Case No. ARB(AF)/07/4, Award, February 20, 2015.

With the proliferation and deepening of IIAs, however, much of the policy space left to countries under WTO law has been receding, and governments are left with fewer tools to both support development of local firms, and to establish and create the linkages with foreign investors that can, in turn, promote diversification, facilitate technology transfer and innovation, and provide a channel for

domestic firms to move into and up GVCs. Crucially, these restrictions on policy space are also made easily enforceable by investors who can challenge and seek compensation for host state measures directly through ISDS. The policy space left to governments now is thus dramatically different than it was 20, and even just 10 years ago.

FIGURE 1 Illustrative List of Restricted Measures – IIAs and WTO Law



5 Policy Conclusions and Options

Comparing relevant policy measures listed under Tables 1–3 and policy restraints listed under Table 7 highlights that governments are presently being pulled in two different directions in terms of, on one hand, their commitments to advance sustainable development and, on the other, commitments to refrain from interfering in private sector operations through adoption of local content policies. As countries are currently involved in establishing policies for implementing the SDGs, and also continuing to engage in negotiations for new IIAs, it is a crucial time to revisit an old debate on the appropriate degree of policy space that should be allowed for local content measures, and seek to improve the consistency and maximize the synergies between these traditionally separate policy spheres.

There are various levels at which action can be taken. First, at the domestic level, it is critical for governments (federal/national, state/provincial, and local) to do an assessment of the policy needs and strategies they have used and may use to advance SDG aims. These include assessments of types of local supports, technology transfer, and linkages policies that have been or may be employed. By better understanding existing and potential future industrial policy strategies, governments can gain a better understanding of the types of policy tools that should be safeguarded.

At the domestic level, it is also important for those involved in formulating trade and investment policy and negotiating (or renegotiating) trade and investment treaties to provide for effective multistakeholder dialogue. This dialogue can help increase understanding of the costs and benefits of supportive measures and local content policy tools from the perspective of affected businesses as well as the actual or intended beneficiaries of such measures. Similarly, such dialogue is imperative for ensuring that commitments made in trade and investment agreements advance, and do not undermine, commitments on sustainable development objectives.

In this context, the roles of developing capital exporting states and developed capital importing states may differ. Consistent with the principle of special and differential treatment, and the need to ensure that developing countries have an effective voice in shaping international economic rules, both concepts that are highlighted in the SDGs, it is crucial for developed states to consider the impacts of their trade and investment policies on developing country partners. Among other things, developed countries should refrain from taking advantage of weak bargaining power or relatively limited resources of negotiating parties to secure commitments that effectively lock developing, capital importing states into positions as mere passive recipients of foreign investment that are largely powerless to more actively shape and maximize the potentially transformative benefits such investments can provide.

Similarly, there is an important role for developed states and development institutions to ensure that states understand the implications of IIAs including, in particular, implications for achievement of sustainable development objectives. In this context, one additional area of future action would be to enhance analysis and understanding of new provisions of IIAs, their effects on different local content policies and the goals sought to be obtained by those policies, and the costs and benefits of expanded enforcement mechanisms and compensation requirements for violations of relevant IIA provisions.

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