

Dispute Prevention: Rationale and Tools

Forum on Dispute Prevention: 56th Session of UNCITRAL

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WORLD BANK GROUP
Finance, Competitiveness & Innovation

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Agenda



**Why does
investor-State
dispute prevention
matter?**



What are the
challenges
governments face in
minimizing
disputes?

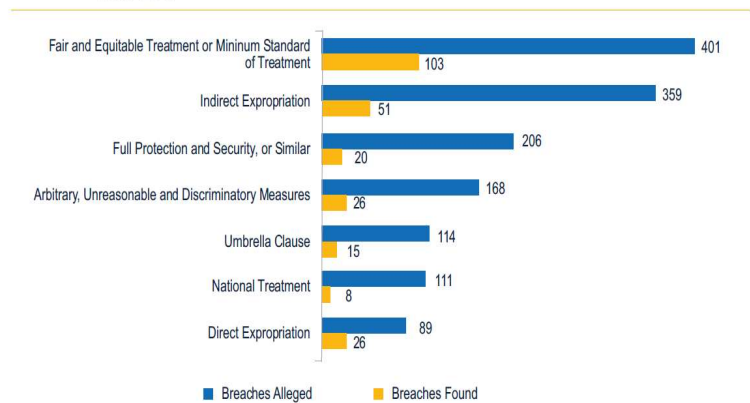


What are some tools
to prevent investor-
State disputes?

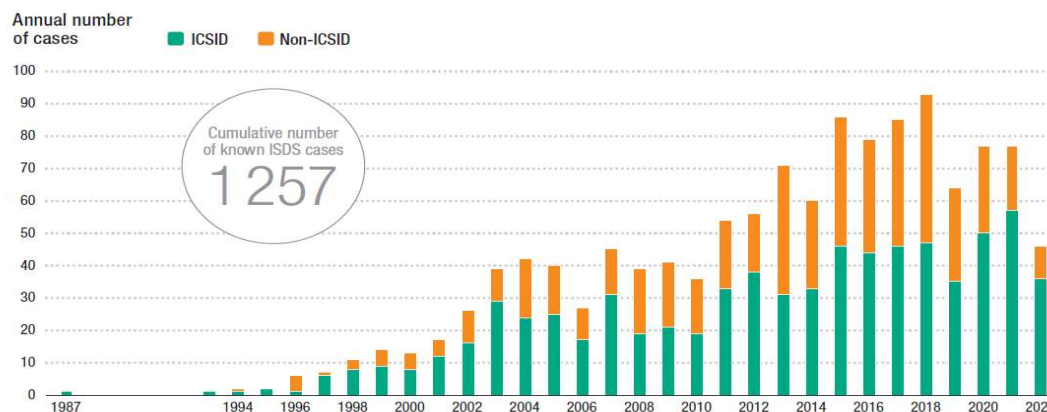
Disputes are expensive

- Number of publicly known ISDS claims: **1257** (1987-2022).
- Per ISDS case, average legal fees for respondents (states) are about **\$4-5 million**. Tribunal costs average around **\$1 million** per case. Damages can run into billions of dollars.

FIGURE 23. BREACHES MOST FREQUENTLY ALLEGED AND FOUND IN TREATY-BASED ISDS CASES, 1987-2017



Source: UNCTAD.
Note: ISDS = Investor-State Dispute Settlement.



Source: UNCTAD, ISDS Navigator.

Note: Information has been compiled from public sources, including specialized reporting services. UNCTAD's statistics do not cover investor-State cases that are based exclusively on investment contracts (State contracts) or national investment laws, or cases in which a party has signalled its intention to submit a claim to ISDS but has not commenced the arbitration. Annual and cumulative case numbers are continually adjusted as a result of verification processes and may not match exactly case numbers reported in previous years.

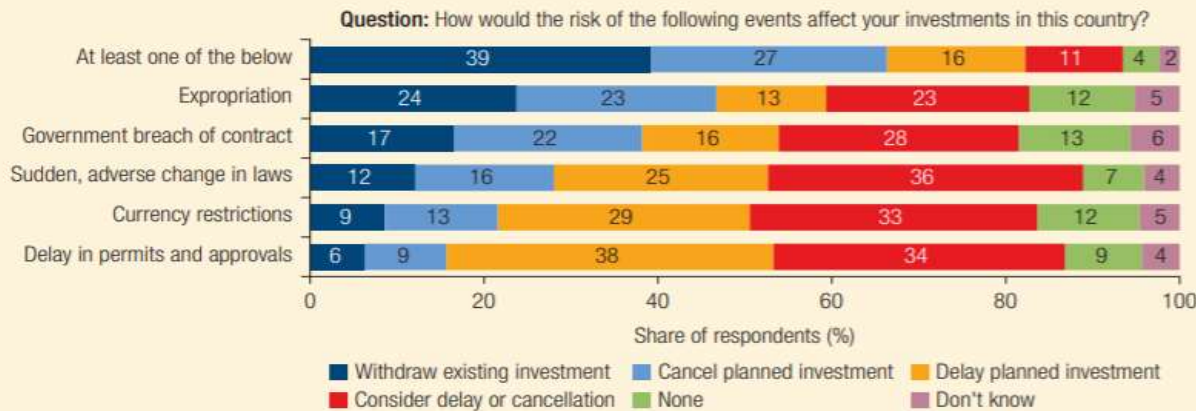
Issues leading to disputes, also impact investment competitiveness of countries

What factors impact investor decisions to continue their investment in a country?

BOX 4.3

Importance of Political Risk and a Stable Regulatory Framework for Investment Decisions: Confirmation from the 2019 GIC Survey (continued)

FIGURE B4.3.2 Expropriation and Breach of Contract Are the Most Likely to Affect Investments Adversely



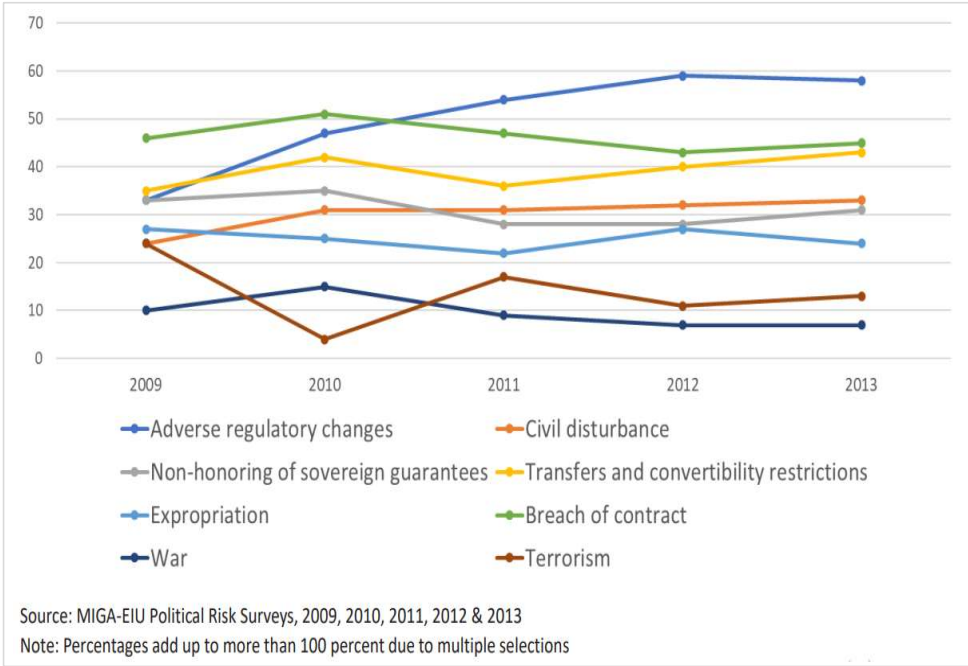
Source: Calculations based on the 2019 GIC Survey.

Note: Affiliates of multinational enterprises were surveyed in 10 middle-income countries: Brazil, China, India, Indonesia, Malaysia, Mexico, Nigeria, Thailand, Turkey, and Vietnam.

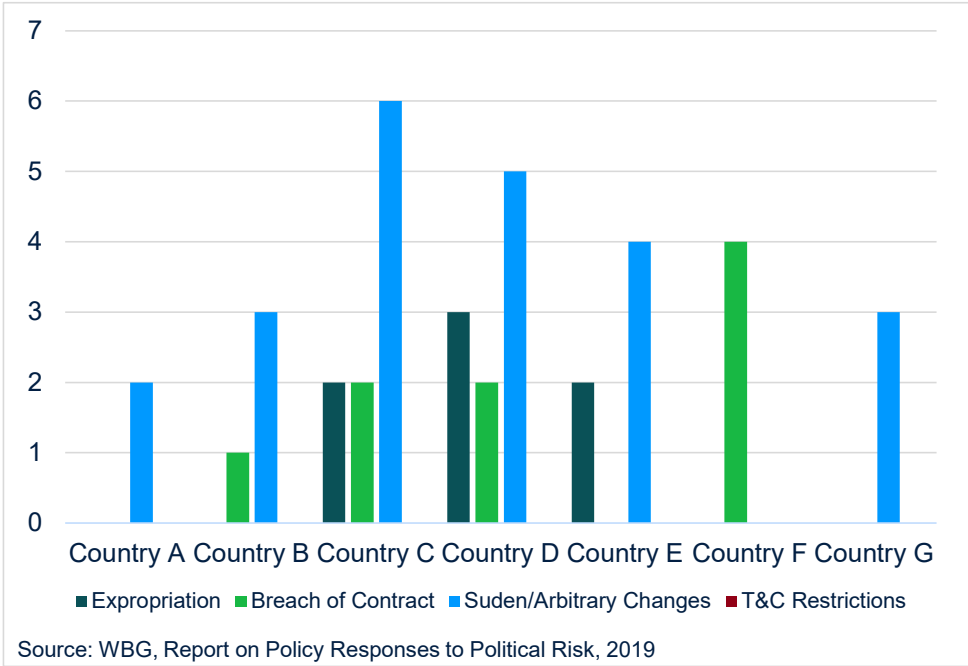
- Political risk have consistently been seen to impact investor decisions to stay and expand in the country. (WBG 2009-20)
- Certain operational risks may also put investment at risk of continuation – highlighted by Covid 19.

Issues affecting investor decisions to continue operations

Types of political risks of most concern to investors in developing countries (MIGA 2009-13)



Types of issues registered in investment retention pilot projects (World Bank pilot projects 2018-19)



Types of issues affecting investor decisions to continue operations

Political Risks

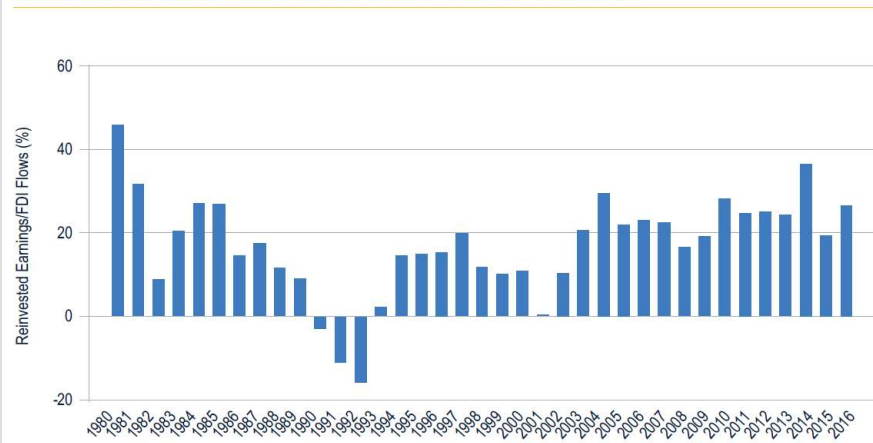
- Caused by government conduct
 - Can lead to divestment
 - Investors protected under domestic and/or international law- issues can lead to investor-State disputes
-
1. Expropriation
 2. Breach of Contract
 3. Transfers and Currency Convertibility
 4. Sudden/Arbitrary Regulatory Changes:
 - 4.1. Contradictory government action
 - 4.2. Lack of transparency
 - 4.3. Discriminatory treatment against foreign investors
 - 4.4. Abuse of authority
 - Abuse of discretion
 - Disguised targeted harassment through regulations
 - Lack of proportionality
 - Abusive interpretation of laws

Operational Risks

- Caused by government conduct
 - Can lead to divestment
-
1. Licensing and permits approval and renewal
 2. Access to land
 3. Construction permits
 4. Access to utilities (speed, quality, consistency and price)
 5. Customs procedures (import/export)
 6. Immigration (work permits and visas)
 7. Stability and predictability of taxes and incentives
 8. Local content requirements
 9. Local capacities (workers, suppliers, partners)
 10. Political stability, courts, corruption, crime, and disorder

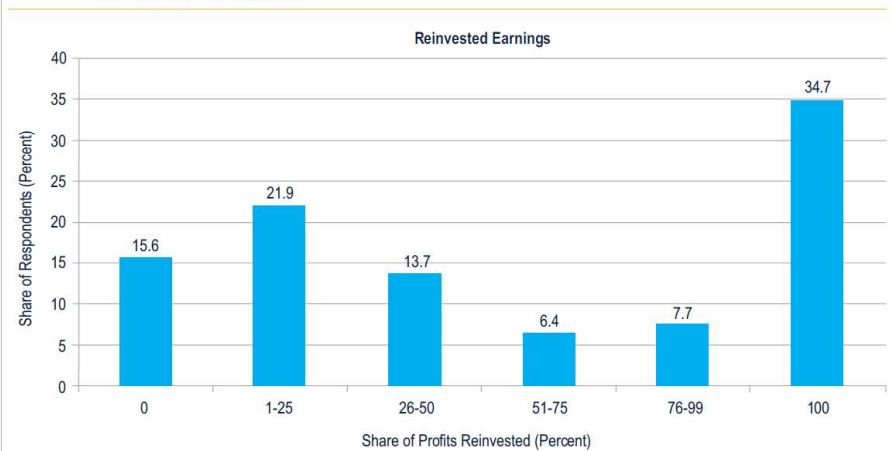
Why does investment retention matter? (1)

FIGURE 3. WORLDWIDE REINVESTED EARNINGS: SHARE OF FDI INFLOWS



Source: International Monetary Fund Balance of Payments, 2019.
Note: FDI = foreign direct investment.

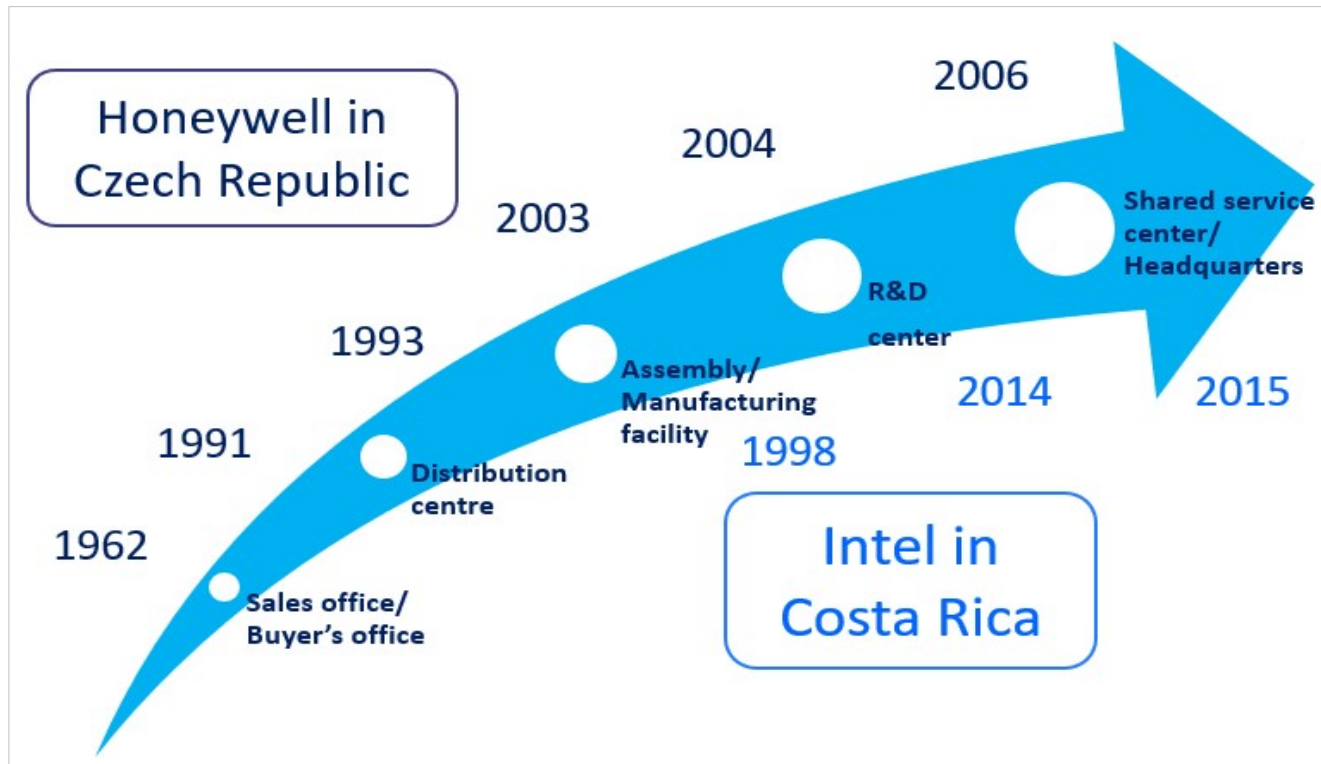
FIGURE 7. MORE THAN A THIRD OF INVESTORS REINVEST ALL THEIR AFFILIATE-GENERATED PROFITS BACK INTO THE AFFILIATE



Source: World Bank Group 2017/2018 Global Investment Competitiveness Report.

- The share reinvested earnings in global FDI has tended to fluctuate between **20 – 40%**
- In **2019 it was over 50%** of FDI flows.
- In Africa (e.g., Kenya -54%; Egypt -41%; Nigeria - 26%)– reinvested earnings and internal funds of firms are major source of funding FDI expansion in fixed assets.
- **Lower corporate earnings** of MNCs in the wake of COVID-19, other ongoing crises will affect reinvested earnings.

Why does investment retention matter? (2)



The longer investors remain in a country, not only the possibilities for linkages increase, but also the activities of FDI **projects themselves tend to evolve.**

Agenda



Why does investor-State dispute prevention matter?



What are the challenges governments face in minimizing disputes?



What are some tools to prevent investor-State disputes?

What are some of the challenges governments face? (1)

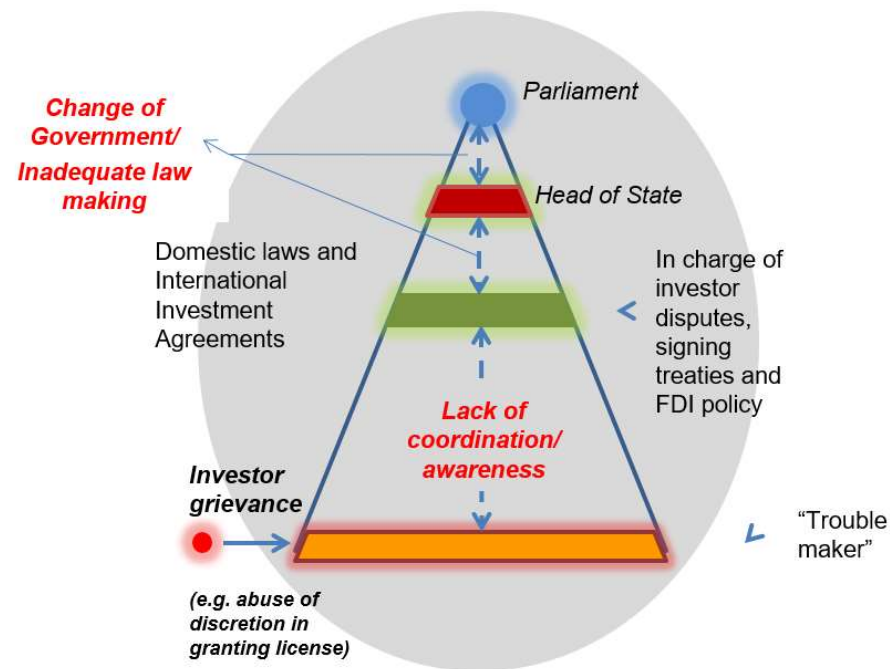
Governments are not monolithic structures

- Different priorities
- Information asymmetries within agencies
- Turf battles

Investments often outlive governments

- Short-term political cycles while businesses need longer term policy and regulatory stability

Address lack of coordination and awareness amongst different levels of the government

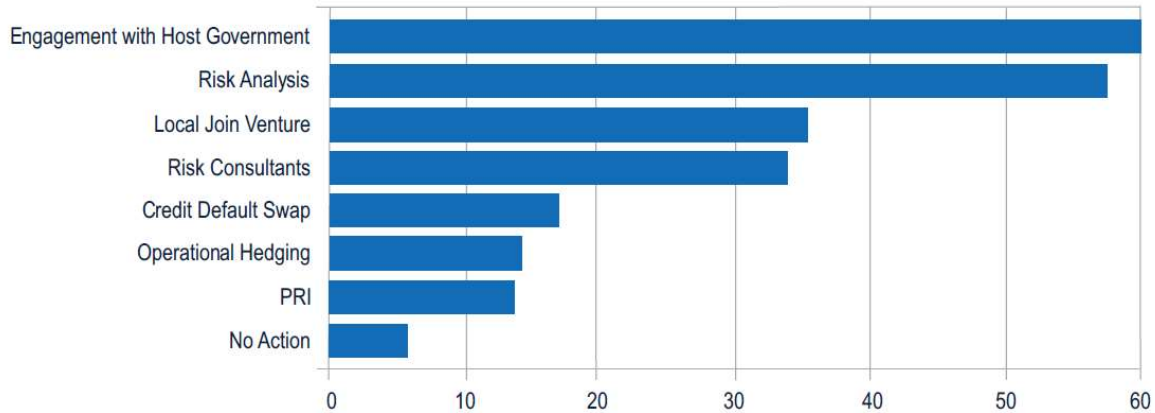


What are some of the challenges governments face? (2)

Poor service delivery, especially to existing investors

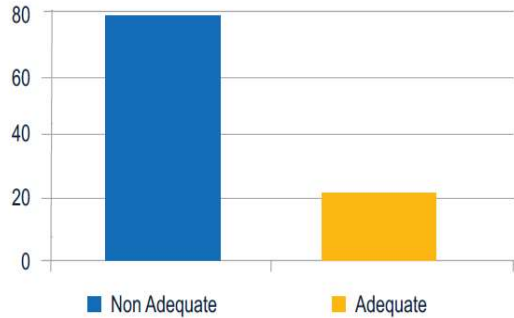
Survey data indicates that direct engagement with governments is the most frequently used tool to address adverse government conduct. Yet the level of satisfaction is low.

FIGURE 20. MECHANISMS USED BY INVESTORS TO MITIGATE POLITICAL RISK IN EMERGING MARKETS, 2009 (% OF RESPONDENTS)



Source: Multilateral Investment Guarantee Agency–Economist Intelligence Unit Political Survey, 2009.

FIGURE 22. INVESTORS' PERCEPTIONS OF EXISTING MECHANISMS TO ADDRESS GRIEVANCES (%)



Source: World Bank Group 2017/2018 Global Investment Competitiveness Report Survey.

What are some of the challenges governments face? (3)

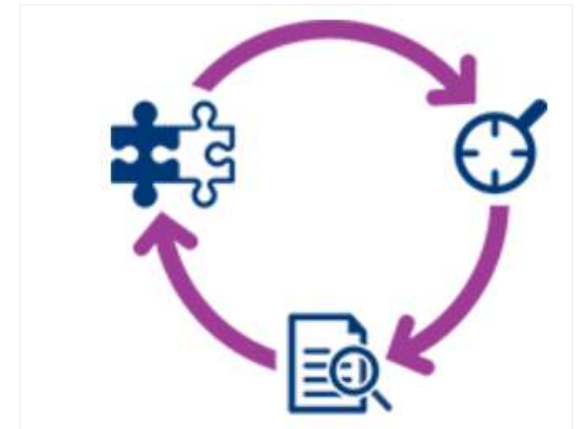
Lack of capacity to engage in effective problem solving



Lack of understanding of investment rules and their implications



Absence of systematic tools to collect information on investor issues and their impact on investors



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Why does investor-State dispute prevention matter?



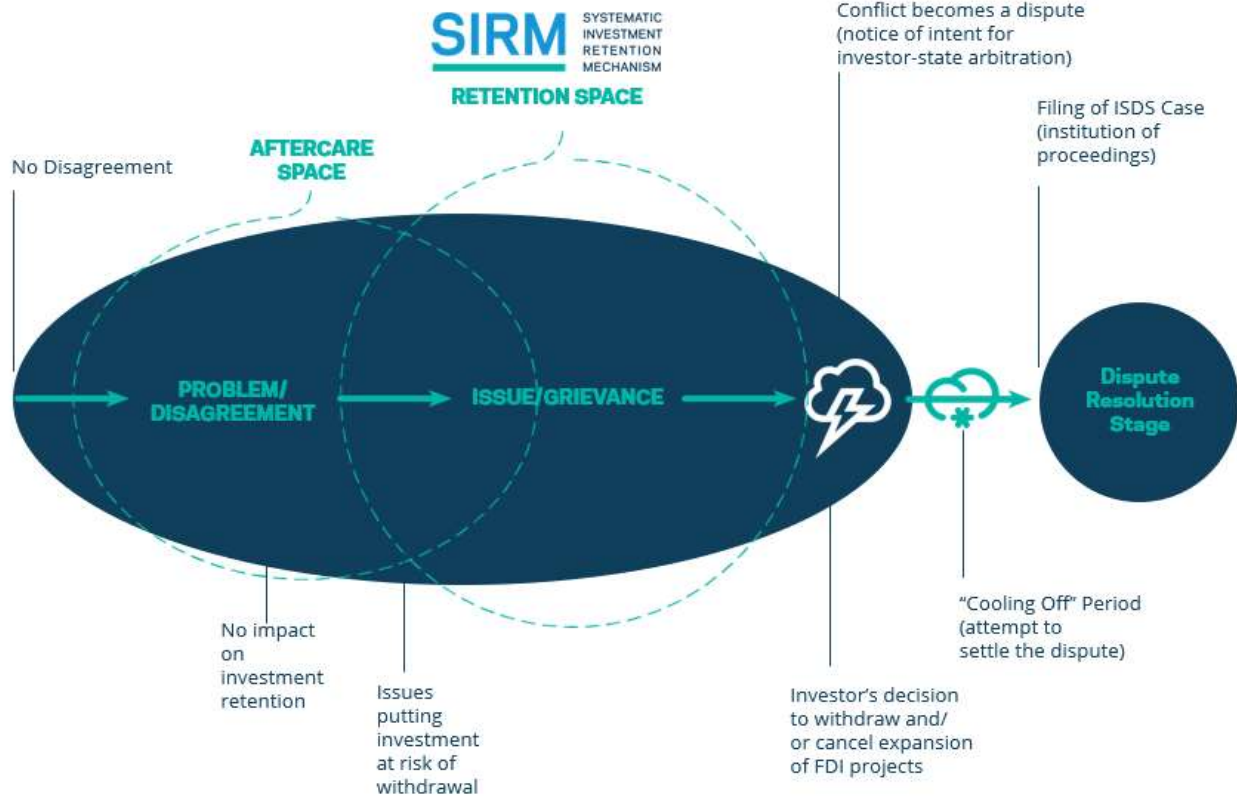
What are the challenges governments face in minimizing disputes?



What are some tools to prevent investor-State disputes?

What are tools to strengthen government capacity to prevent disputes and retain investment?

- **Investor State Conflict Continuum**
- Countries have typically focused on two ends of the spectrum – Aftercare and Dispute Settlement
- Tools also need to focus on addressing the missing middle



Strategy 1: Systemic Measures to Improve Regulatory Frameworks

Institutional clarity and defined reform process

- Single lead agency in charge of the regulatory reform at hand – coordinating across institutions as needed.
- Develop a consolidated program document, implementation roadmap, and decision-making schedule, with public meetings to report progress.

Consultation

- Consultation should be timely and transparent and provide stakeholders with sufficient time to submit their position.
- Report back on the result of such consultation, explaining how the stakeholder input has been assessed and considered

Better informed rule making

- Consider regulatory developments from other countries

Stocktaking, analysis and monitoring

- Early in the reform process, review all existing international obligations of the state, analyze the potential impact/ risks stemming from the envisaged regulatory reform.
- Study the problems, conflicts, and disputes the host country experienced in the past in the sector; analysis of problems faced by other countries that had introduced similar reforms. This study should be part of the impact assessment of the proposed regulatory/policy changes.

Strategy 2: Institutional measures to handle investor issues caused by regulatory risks - before their escalation to legal disputes



Institutional setup

Lead Agency

- Identifies, tracks, manages projects at risk and investor issues

Legal Instrument, Clear Mandate

- Clarifies role of lead agency
- Ensures coordination

Escalation Mechanism / Advocacy

- Addresses highly political issues and enforces implementation
- Addresses systemic issues – push for reforms



Operating procedures

Steps to Define Standard Operating Procedures

1. Defining and executing plan to reach out to investors (having a strategy)
2. Recording issues / filtering by risk
3. Assessing impacts (legal and economic)
4. Problem-solving
5. Escalating and Advocacy (if needed)
6. Following up



Monitoring & evaluation

Impact Indicator

1. Investment retained

Main Outcomes

1. Number of projects retained
2. Number of issues / grievances solved

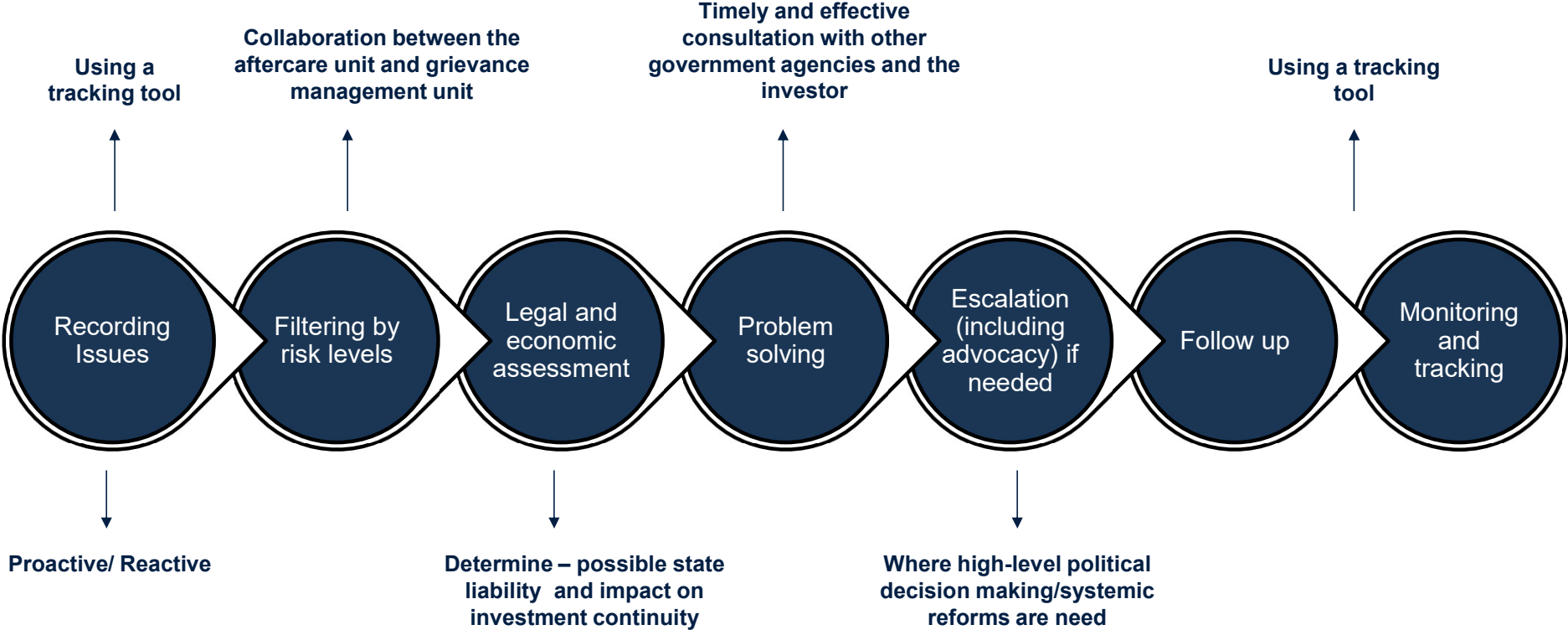
Tracking Tool

- For the Lead Agency to easily calculate those indicators it is important to have a tracking tool to capture the necessary data.

Options for establishing a lead agency

	Model 1 - New Agency	Model 2- Within Investment Promotion Agency (IPA)
Type	<ul style="list-style-type: none"> Independent / new lead agency (for example, a Business Ombudsman) 	<ul style="list-style-type: none"> Lead agency within an Investment Promotion Agency (for example, a grievance management unit)
Escalation Mechanism	Independent platform <ul style="list-style-type: none"> Prime Ministerial or Inter-Ministerial Meeting 	Discussion in IPA units <ul style="list-style-type: none"> High level management of the IPA Prime Ministerial or Inter-Ministerial Meeting
Pros	<ul style="list-style-type: none"> Strong authority (including on issues outside the scope of the IPA) Focus on high-risk cases 	<ul style="list-style-type: none"> Easy access to investors Easy issue collection process
Cons	<ul style="list-style-type: none"> New institution: new resources Slow progress Low capacity 	<ul style="list-style-type: none"> Mandate can be limited Confusion between the high-risk grievance management and broader aftercare Difficulties in focusing on high-risk cases
Conditions for success	<ul style="list-style-type: none"> No IPA or a weak IPA Strong political support from the top to create a new agency 	<ul style="list-style-type: none"> Strong empowerment of the IPA for coordination Need for an efficient filtering and escalation mechanism

Standard Process to Resolve Issues



Type of information recorded in registering investor issues and grievances

Investor Details	Project Involved in Issue	Issue Details and Impacts	Issue Resolution	Status of Issue
<ul style="list-style-type: none"> • Name • Contact • Sector • Country of Origin • Size of Company (revenue/turnover) • Year of Incorporation 	<ul style="list-style-type: none"> • Name • Sector • Size of Project (i.e., investment) • Sponsors/Lenders/Partners • Location • Project Benefit (Jobs, Tax) • Exports • Imports 	<ul style="list-style-type: none"> • Description of Issue • Classification • Parties Involved • Action taken in past by investor (consultation, legal action (cases filed-when, forum, result)) • Costs incurred so far (in taking action) • Investment action that investor considers/may consider (withdrawal, no expansion, on hold) • Amount of Investment, jobs at risk 	<ul style="list-style-type: none"> • Action by Lead Agency (date of filing, case assignment) • Follow up actions with Involved Agency (date of communication and outcome) 	<ul style="list-style-type: none"> • Closed (resolved, escalated to legal dispute, withdrawn) • Open

International Developments

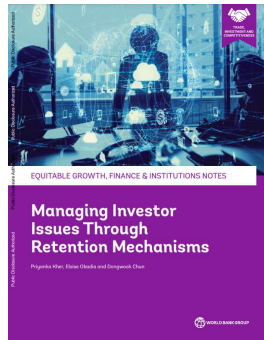
1. Investment Facilitation negotiations at the WTO
2. UNCITRAL Working Group III- ISDS Reform Discussions
3. Complementary tool: Treaty specific mechanisms; for example Korea-China FTA article 12.19 (appointing China's IPA and KOTRA as contact points for receiving complaints from investors of other party regarding administrative actions)
4. Africa Continental Free Trade Agreement – Investment Negotiations

Background – Resources

Enabling Renewable Energy FDI: Reducing Regulatory Risk



Managing Investor Issues through Retention Mechanisms



World Bank-EU Report: Retention and Expansion of FDI



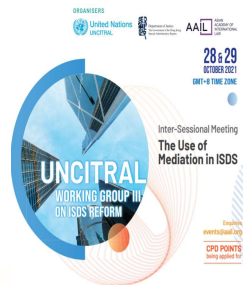
Policy Options to Mitigate Political Risk and Attract FDI



Regulatory Risk and FDI



UNCITRAL-World Bank Legislative Guide /Compendium



Strengthening Service Delivery of IPAs



Institutions for Investment



ITC-WEF Commentary Group on Investment Facilitation for Development

INVITATION: 18 February 2021, 6th VIRTUAL MEETING OF THE COMMENTARY GROUP ON INVESTMENT FACILITATION FOR DEVELOPMENT

Dear Colleagues,

We would like to invite you to participate in the 6th meeting of the Investment Facilitation Commentary Group, to take place virtually on 18 February 2021, from 09:00 to 16:00 Eastern Daylight Time (EDT), 15:00 to 14:30 Central European Time (CET).

As a reminder, the Commentary Group's mandate is to provide input on the content of the Handbook, being developed in the WTO to facilitate cross-border investment and increase its development impact.

The 6th meeting will focus on how to structure effective mechanisms to identify and resolve investment-related issues early, before they become a risk to the investment climate or even a legal dispute.

As background documents, please find the following attached:

- a) The updated Secretary of Concrete Measures to Facilitate the Flow of Sustainable FDI, available at <https://www.itsaforum.org/investment-facilitation-for-development>;
- b) The outcomes of the 1st, 2nd, 3rd, 4th and 5th Commentary Group meetings which were shared with WTO registars, available at <https://www.itsaforum.org/investment-facilitation-for-development>;
- c) The Internal Consolidated Text of the WTO Structural Discussion on Investment Facilitation for Development (February 6, 2021), available here. For the meeting you might want to go over Section IV.16. Contact focal points/Outsiders types and mechanisms.

THANK YOU

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