

**LEGAL TREATMENT
OF FOREIGN INVESTMENT:
THE WORLD BANK GUIDELINES**

IBRAHIM F.I. SHIHATA

*Vice President and General Counsel,
The World Bank*

*Secretary-General,
International Centre for Settlement
of Investment Disputes*

Legal Treatment of Foreign Investment:

“The World Bank Guidelines”



1993

MARTINUS NIJHOFF PUBLISHERS

DORDRECHT / BOSTON / LONDON

A C.I.P. Catalogue record for this book is available from the Library of Congress.

ISBN 0-7923-2525-7

Published by Martinus Nijhoff Publishers,
P.O. Box 163, 3300 AD Dordrecht, The Netherlands.

Sold and distributed in the U.S.A. and Canada
by Kluwer Academic Publishers,
101 Philip Drive, Norwell, MA 02061, U.S.A.

In all other countries, sold and distributed
by Kluwer Academic Publishers Group,
P.O. Box 322, 3300 AH Dordrecht, The Netherlands.

Printed on acid-free paper

All Rights Reserved
© 1993 Ibrahim F.I. Shihata
Kluwer Academic Publishers incorporates the publishing programmes of
Martinus Nijhoff Publishers.

No part of the material protected by this copyright notice may be reproduced or
utilized in any form or by any means, electronic or mechanical,
including photocopying, recording, or by any information storage and
retrieval system, without written permission from the copyright owner.

Printed in the Netherlands

**To Anne Le Lorier and her colleagues at the French Treasury
who initiated the request which led to the development
of the guidelines discussed in this book;**

**and to Gillian Kettaneh for her assistance,
without which this book would not have been
produced in such a short time.**

FOREWORD

On September 12, 1985, following extensive deliberations by the World Bank's¹ Executive Directors sitting in twenty sessions of their Committee of the Whole, the draft Convention Establishing the Multilateral Investment Guarantee Agency (MIGA) and the documents related to it were approved by the Board of Executive Directors without objection. Nonetheless, two Executive Directors abstained because the issue of the standards applicable to foreign investment, that is the general legal principles that should govern the treatment of such investment by host governments, had not been resolved in the convention, as previously requested by their authorities.

Following this decision of the World Bank's Executive Directors, the Dutch Executive Director, Ferdinand Van Dam, while congratulating me on the difficult chairmanship of the deliberations of the Committee of the Whole and the successful completion of the text of the MIGA Convention, urged me to continue to pursue the issue of applicable standards. "I believe," he said with confidence, "you can succeed in obtaining an international consensus on this question." However, I was convinced at the time that reaching an international consensus on such a controversial issue was an elusive goal. The United Nations' efforts in this field, initiated in 1977, like many earlier attempts in other fora, suggested that the gap between the traditional attitudes of developed and developing countries, hardened by years of unsuccessful negotiations, was too wide to allow for realistic compromises.

Exactly seven years later, on September 21, 1992, the Development Committee (a joint ministerial committee of the World Bank and the International Monetary Fund), without any reservations, issued a set of

¹ The terms "World Bank" and "Bank" refer to the International Bank for Reconstruction and Development and the International Development Association together, unless the context suggests otherwise. The World Bank Group consists of the International Bank for Reconstruction and Development (IBRD), the International Development Association (IDA), the International Finance Corporation (IFC), the Multilateral Investment Guarantee Agency (MIGA) and the International Centre for Settlement of Investment Disputes (ICSID).

universal guidelines on the legal treatment of foreign investment. The text of the guidelines was prepared by a small working group which I had the honor to chair. The successful outcome, however, was not so much a personal achievement as the product of changing realities and perceptions about foreign investment and the benefits it can bring to the global economy and the economies of developing countries in particular. In a broader sense, the great transformations of the late eighties and early nineties created a new environment which made possible agreement on many issues thought earlier to defy common solutions.

The purpose of this book is to provide a personal account of the steps which led to the issue by the Development Committee of the Guidelines on the Treatment of Foreign Direct Investment (the Guidelines) and a first hand explanation of the text of the Guidelines. The book places the Guidelines in the broader context of continuing international efforts to improve investment climates. It includes not only the text of the Guidelines (in three languages) but also the studies which preceded the preparation of that text and the official reports which explain its rationale and contents. This book may therefore be read as a complement to my earlier book on MIGA and foreign investment.² Together, the two books provide detailed accounts of the continued efforts by the World Bank to encourage the flow of international investments through specific mechanisms which complement its financing, catalytic and advisory roles, in pursuance of one of its main purposes, which is "to promote foreign private investment."³

Ibrahim F.I. Shihata

June 30, 1993
Washington, D.C.

² IBRAHIM F.I. SHIHATA, *MIGA AND FOREIGN INVESTMENT* (1988).

³ *See* Articles of Agreement of the International Bank for Reconstruction and Development, Article I.

ACKNOWLEDGEMENTS

This book was written with the able assistance of Gillian Kettaneh, Counsel at the World Bank. Her qualifications in the fields of law, economics and government and her dedication made it possible to complete the research and writing of this book in record time. The contribution of Ms. Kettaneh is all the more appreciated as she joined the Bank's service on August 31, 1992, after the work on the Guidelines had been completed and, for that reason, did not have the advantage of prior involvement in the subject. I am also grateful to Antonio R. Parra, Legal Adviser of the International Centre for Settlement of Investment Disputes (ICSID), for having reviewed the manuscript in full in a very short time and for his useful remarks. Without Miss Cleone Hoover's efficient management of my office, this book could not have been prepared. Ms. Kerry Smyth's patient work in typing the manuscript and in managing parts of the production process are also acknowledged with appreciation.

My gratitude goes to D.C. Rao, Acting Vice President and Chief Economist, World Bank and Kwang W. Jun, Senior Financial Economist, for their review and useful comments on the Introductory Chapter, the first section of which is based mainly on the work of their department.

As the book explains in detail, the preparation of the Guidelines was a joint effort of José E. Camacho, Vice President and General Counsel of the International Finance Corporation (IFC), Luis Doderó, Vice President and General Counsel of the Multilateral Investment Guarantee Agency (MIGA), Daoud L. Khairallah, Deputy General Counsel of the IFC, and myself, with the assistance of Antonio R. Parra and his staff at the ICSID Secretariat and Bertrand P. Marchais, Senior Counsel in MIGA. It is therefore with great appreciation that I wish to acknowledge the contribution and support of these able colleagues.

The suggestions and criticisms received from many sources during the preparation of the Guidelines which are detailed in the book have helped in shaping the final product. While each of the sources, be they individuals or organizations, shares in the credit for the outcome, the responsibility for the shortcomings rests only with the Working Group which prepared the Guidelines and explanatory report, and with me in particular.

My great appreciation and thanks go to Barber B. Conable, former President of the World Bank Group, for having entrusted me with the primary responsibility for undertaking the work requested by the Development Committee and to Lewis T. Preston, the current President of the World Bank Group, for his unswerving support throughout the process.

I.S.

The views expressed in this book are those of its author and do not necessarily represent the views of the World Bank, its member governments, Executive Directors or Management.

TABLE OF CONTENTS

Foreword	vii
Acknowledgments	ix
Table of Contents	xi
INTRODUCTORY CHAPTER: THE ENABLING ENVIRONMENT FOR INCREASED FOREIGN DIRECT INVESTMENT FLOWS	1
I. An Overview of the Increasing Role of Foreign Direct Investment in Developing Countries	1
A. Recent Trends in Foreign Direct Investment Flows	1
B. Possible Benefits of Foreign Direct Investment to Developing Countries	9
II. Elements of a Favorable Investment Climate	12
A. Source Country Policies	13
1. Policy Framework in the Source Country	13
2. Source Country Promotional Instruments .	17
3. Source Country Regulations	18
B. Host Country Policies	20
1. Economic and Financial Framework	20
2. Political and Cultural Conditions	22
3. Legal and Regulatory Regime	24

PART ONE — PREPARATION OF THE GUIDELINES

CHAPTER TWO: THE ORIGINS OF THE WORLD BANK'S INVOLVEMENT 29

- I. The MIGA Convention and the Standards
Applicable to Foreign Investment 29
- II. The Treatment of Standards under the MIGA
Regulations 34
- III. The French Initiative at the April 1991
Development Committee Meeting 37
- IV. The Decision of the Bank's President on
the Process 39
- V. The Work Plan 40

CHAPTER THREE: PHASE ONE — SURVEY OF EXISTING INSTRUMENTS 47

- I. Preparation of the Background Studies 47
- II. The April 1992 Development
Committee Meeting 57

CHAPTER FOUR: EVOLUTION OF THE GUIDELINES 61

- I. Preparation of the Initial Working
Group Draft 61

II.	Text and Analysis of the Initial Working Group Draft	65
A.	The Preamble	65
B.	Draft Guideline I: Scope of Application . . .	67
C.	Draft Guideline II: Admission	73
D.	Draft Guideline III: Treatment	77
E.	Draft Guideline IV: Expropriation and Breach of Contracts	85
F.	Draft Guideline V: Settlement of Disputes . .	95

CHAPTER FIVE: CONSULTATION ON THE GUIDELINES 99

I.	Internal Bank Consultations Regarding the Initial Working Group Draft	99
A.	IFC Comments	100
B.	MIGA Comments	101
C.	FIAS Comments	102
D.	Bank-wide Consultations	104
II.	Discussions of the May 6, 1992 Draft	106
A.	Preliminary Discussion of the Draft Guidelines by the Executive Directors	107
B.	United States Comments	107
C.	Comments by Other Developed Countries . .	114
D.	Comments by Developing Countries	117
E.	Early Comments by National Business Groups	118

III.	Consultation with International Organizations and International Business Groups — The Paris Conference, July 1, 1992	119
IV.	Draft of July 6, 1992	124
	A. Amendments to the Draft Guidelines	124
	B. Further Comments of Business Groups	126
	1. U.S. Council for International Business	126
	2. International Chamber of Commerce	128
V.	July 1992 Meeting of the Committee of the Whole	131
VI.	Final Draft of the Working Group: Draft of August 7, 1992	135
CHAPTER SIX: FINALIZATION OF THE GUIDELINES AND THEIR PROSPECTIVE IMPACT		139
I.	The Last Amendments Proposed by the U.S.	139
II.	Adoption of the Guidelines: The September 1992 Meeting of the Development Committee	143
III.	Future of the Guidelines	146
IV.	Concluding Remarks	150

PART TWO — THE GUIDELINES

I.	Final text of the Guidelines	155
	A. Original English Text	155
	B. French Translation	165
	C. Spanish Translation	179
II.	Report to the Development Committee on the Legal Framework for the Treatment of Foreign Investment, submitted to the Fall meeting of the Development Committee, September 21, 1992	193

PART THREE — SURVEYS AND DOCUMENTS

A. SURVEYS:

I.	Treatment of Foreign Investment in Bilateral Investment Treaties	221
II.	Multilateral Approaches to the Treatment of Foreign Investment	267
III.	Principles Governing Foreign Investment, as Reflected in National Investment Codes	311
IV.	General Principles Governing Foreign Investment as Articulated in Recent International Tribunal Awards and Writings of Publicists	337

B. DOCUMENTS:

- I. Excerpt from the Communiqué of the 41st Meeting of the Development Committee, Washington, D.C., April 30, 1991 383
- II. Draft Outline of the Legal Framework Prepared by the Staff of the French Treasury . . 385
- III. Text of Author's Presentation to a Meeting of the MIGA Committee of the Whole, dated March 6, 1992 on the Progress Report 389
- IV. Progress Report on the "Legal Framework" for the Treatment of Foreign Investment submitted to the Spring meeting of the Development Committee, April 18, 1992 393
- V. May 6, 1992 Draft of the Guidelines on the Treatment of Foreign Direct Investment 401
- VI. Memoranda Outlining U.S. Concerns Relating to the Legal Framework for the Treatment of Foreign Investment
 - (a) Memorandum dated May 28, 1992 413
 - (b) Memorandum dated July 22, 1992 419
- VII. Comments from the Office of The Netherlands Executive Director 423
- VIII. Comments from the Office of the United Kingdom Executive Director 427

IX.	Documents Relating to the Consultative Meeting convened in Paris on July 1, 1992	431
	(a) List of Invitees	431
	(b) List of Attendees	432
	(c) Text of Address of French Finance Minister	434
X.	Text of Author's Presentation of the Draft Guidelines to a joint meeting of the World Bank and MIGA Committee of the Whole, dated July 27, 1992	439
XI.	Comparison of the Final Text of the Guidelines with the Initial Working Group Draft of the Guidelines	443
INDEX		459
BOOKS BY THE AUTHOR		467