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CENTRE FOR CO-OPERATION WITH NON-MEMBERS
ENVIRONMENT POLICY COMMITTEE

Emerging Market Economy Forum

CONFERENCE ON FOREIGN DIRECT INVESTMENT AND THE
ENVIRONMENT

DRAFT ANNOTATED AGENDA AND SUGGESTED ISSUES FOR DISCUSSION

The Hague, The Netherlands, 28-29 January 1999

72980

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CONFERENCE ON FOREIGN DIRECT INVESTMENT AND THE ENVIRONMENT

*To be held at the Steigenberger Kurhaus Hotel, The Hague, The Netherlands
Thursday, 28th and Friday, 29th January 1999*

DRAFT ANNOTATED AGENDA

Thursday, 28 January 1999

- 9.00 a.m. **Opening of the conference**
- 9.30 a.m. to 12.30 p.m. **Plenary Session 1**
- *Context and key issues*
- 2.30 p.m. to 6.00 p.m. **Parallel workshop 1**
- *The environmental impact of FDI: Policy and institutional responses*
- Parallel workshop 2**
- *The role of voluntary commitments*
- Parallel workshop 3**
- *The impact of FDI on environmental standards: Pollution havens and pollution halos*

Friday, 29 January 1998

- 9.30 a.m. - 12.30 p.m. **Continuation of the parallel workshops**
- 2.30 p.m. - 5.00 p.m. **Plenary session 2**
- *Conclusions*

SPEAKERS

Thursday 28 January 1999

**9.00 a.m.
to 9.30 a.m.** **Opening of the conference**

Mr. Gerrit Ybema
Minister for Foreign Trade
The Netherlands

Mr. Donald Johnston (to be confirmed)
Secretary-General
OECD

**9.30 a.m.
to 12.30 p.m.** **Plenary session 1: Context and key issues**

Chair: Ms. Joke Waller-Hunter
Environment Directorate
OECD

Rapporteur: Ms. Frances Seymour
World Resources Institute
United States

Lead Speaker: Mr. Brad Gentry
Yale Centre for Environmental Law and Policy
United States

Panel: Ms. Anne Weir (to be confirmed)
Unilever

Mr. Charles Arden-Clarke
Trade and Investment Unit
World-Wide Fund for Nature International
Switzerland

Mr. Fabio Feldmann
Member of the House of Representatives
Former Secretary of the Environment of São Paulo State
Brazil

Open discussion.

Documentation: Background paper no. 1; CCNM/EMEF/EPOC/CIME(98)2

**2.30 p.m.
to 6.00 p.m.
and continuing
on 29 January
from 9.30 a.m.
to 12.30 p.m.**

Parallel workshop 1: The environmental impact of FDI: Policy and Institutional responses

Chair: Mr. David Runnalls
International Institute for Sustainable Development
Canada

Rapporteur: Mr. Jernej Stritih
Regional Environmental Centre
Hungary

Lead speaker: Ms. Gretta Goldenman
Milieu Environmental Law Consultancy
Belgium

Panel: Mr. Kim Salkeld
Planning, Environment and Lands Bureau
Government of the Hong Kong Special Administrative Region
Hong Kong, China

Ms. Vivianne Blanlot
GTA Ingeneria Ltda
Chile

Mr. Hans Opschoor
Institute of Social Studies
The Netherlands

Mr. Gary Nash
The International Council on Metals and the Environment
Canada

Open discussion.

Documentation: Background paper no. 2: *The environmental implications of FDI: policy and institutional responses*;
CCNM/EMEF/EPOC/CIME(98)3

**2.30 p.m.
to 6.00
and continuing
on 29 January
from 9.30 a.m.
to 12.30 p.m.**

Parallel workshop 2: The role of voluntary commitments

- Chair: Mr. Manfred Schekulin
Ministry of Economic Affairs
Austria
- Rapporteur: Mr. Jan Schuijjer
Directorate for Fiscal, Financial and Enterprise Affairs
OECD
- Lead speaker: Ms. Jan Adams
Environmental Policy Consultant
Australia
- Panel: Mr. Michael Brandt
Shell International
The Netherlands
- Ms. Sigrid Shreeve
Consultant
United Kingdom
- Mr. Pieter van der Gaag
ANPED, the Northern Alliance for Sustainability
The Netherlands
- Mr. William Witherell
Directorate for Financial, Fiscal and Enterprise Affairs
OECD

Open discussion.

Documentation: Background paper No. 3: *FDI and the environment: the role of voluntary corporate environmental management*
CCNM/EMEF/EPOC/CIME(98)4

**2.30pm
to 6.00pm
and continuing
on 29 January
from 9.30 a.m.
to 12.30 p.m.**

**Parallel workshop 3: The impact of FDI on environmental standards:
“Pollution havens” and “pollution halos”**

Chair: Mr. Duncan Brack
Royal Institute of International Affairs
United Kingdom

Rapporteur: Mr. Sitanon Jesdapipat
Thailand Environment Institute
Thailand

Lead speaker: Ms. Lyuba Zarsky
Nautilus Institute
United States

Panel: Mr. Elmer S. Mercado (to be confirmed)
Undersecretary for Environment and Programme Development
The Philippines

NGO participant, to be confirmed

Ms. Nancy Olewiler
Department of Economics
Simon Fraser University
Canada

Other participant, to be confirmed

Open discussion.

Documentation: Background paper no. 4: *Pollution ‘havens’ and pollution ‘halos’*, CCNM/EMEF/EPOC/CIME(98)5

Friday 29 January 1999

**2.30 p.m.
to 5.00 p.m.**

Plenary session 2: Conclusions

Chair: Mr. Frans Engering
Director-General of Foreign Economic Relations
The Netherlands

Reports by the workshop rapporteurs

Open discussion.

SUGGESTED ISSUES FOR DISCUSSION

1. The objectives of the conference are two-fold:
 - to deepen the analysis of the key policy issues in the relationship between foreign direct investment (FDI) and the environment, within the context of a globalising economy; and
 - to examine ways in which this relationship might be improved to reinforce environmental and FDI policy goals mutually.
2. Drawing on the experience of the public and private sectors and non-governmental organisations, both in OECD Member and non-member economies, the conference will examine in particular:
 - the policy and institutional frameworks for managing the environmental impacts of FDI, including the role of environmental impact assessment;
 - private and governmental initiatives to promote “best environmental practices” in FDI, including the role of corporate and industry codes of conduct, environmental reporting, information disclosure and investment standards;
 - empirical evidence of the raising or lowering of environmental standards to attract FDI, the influence of environmental standards on FDI, and the economic and environmental policy implications.
3. The remainder of this paper provides background information to support each segment of the conference and suggests issues to help focusing the discussion.

Plenary session 1: Context and key issues

4. Foreign direct investment has been one of the main driving forces of globalisation. It has engendered economic growth and it has a proven potential to further the broader goal of sustainable development in both developed and developing countries¹.
5. World-wide foreign direct investment flows have expanded more than seven-fold² over the past two decades. Current data over 1997 estimate global FDI outflows at US\$400 billion (compared to US\$338 billion in 1996), and inflows at US\$424 billion (compared to US\$333 billion the year before)³. Most FDI continues to flow between OECD countries. Investors from OECD Member countries invested

1 FDI is only one component of private international capital flows. The other two major components are portfolio capital and commercial bank loans. Each one of these can have implications for the environment, although most research to date has focused on the FDI-environment relationship. In addition, official development assistance (ODA) remains an important source of finance for developing countries, even though its total volume has gone down, and by 1995 it was less than half of private capital flows to developing countries..

2 In constant US dollars.

3 UNCTAD, 1998: *World Investment Report 1998: Trends and Determinants*. UNCTAD. Geneva.

over US\$382 billion abroad over 1997, while these countries received US\$256 billion⁴. Seen over the current decade, six OECD countries and one non-Member economy (Hong Kong, China) each invested over US\$100 billion abroad over 1990-1997 (see table 1, in the annex).

6. Flows to non-OECD countries have accelerated, but most of these have a small number of countries as their destination, located in three regions: Asia-Pacific, Latin America and, to a lesser extent, central and eastern Europe. Among the 25 principal destinations of FDI over 1990-1997, there were five Asian and four Latin American non-Members (see table 2).

7. Despite the impact of the recent financial crisis on these trends, several issues concerning the FDI-environment relationship have been receiving increased attention⁵:

- *The positive and negative environmental effects of FDI.* On the one hand, FDI promotes economic growth and may foster resource-efficient production methods, as well as investment in environmental protection. On the other hand, it could encourage the production and consumption of polluting goods and/or expanded industrial activity with higher emissions.
- *The environmental effects of technology development and diffusion.* Foreign investors often introduce newer technologies that are cleaner and more resource-efficient than the existing stock. On the other hand, it has been argued that some investors off-load out-of-date or hazardous technologies to less developed countries which lack an appropriate regulatory infrastructure to prevent abusive practices.
- *The impact of environmental standards on investor decision-making.* The effects of high environmental standards on industrial location has been the subject of debate. Do “high standard” countries stimulate companies to relocate to those with “lower” (or less well enforced) environmental standards (the “pollution haven” hypothesis) ? On the other hand, investors frequently argue that uncertain environmental requirements, particularly concerning liabilities for past environmental damage, impede investments. In some instances, investors have lobbied for stricter or clearer environmental standards in the host country, and better enforcement. Do MNEs tend to observe stricter home country standards if the host country standards are lower ?
- *The environmental effects of international competition for FDI.* A related fear is that some countries will use lower standards (or weak enforcement) as a way of attracting new FDI. Countries could either lower their standards intentionally, or they could resist change as international standards rise, in order to gain a competitive advantage.

4 Updates of the data contained in: OECD, *Financial Market Trends* No. 70, June 1998.

5 See OECD, 1997: “Foreign Direct Investment and the Environment: An Overview of the Literature” for a fuller discussion. Available at website <http://www.oecd.org/daf/env/index.htm>.

Issues for discussion

- *Participants are invited to present empirical evidence of the impact of FDI on environmental quality. Is there evidence that the impact of FDI on the environment is less beneficial, or even detrimental, in less developed countries ?*
- *Is there evidence that low standards, or lax enforcement, have been effectively used as investment incentives ? Conversely, is there evidence that foreign investors voluntarily apply home country standards, even if these are stricter than those imposed by law in the host countries ?*
- *Could the objectives of investment and environment policy be integrated? How could FDI be made to contribute to environmental protection ? What could be the contribution of government policy (e.g. in the form of legally binding rules, financial incentives, promoting good corporate conduct), of voluntary commitments taken on by the industry, and of society at large ?*

Workshop 1: The Environmental impact of FDI: Policy and institutional responses

8. Environmental impact assessment (EIA) is one of the principal policy instruments used in OECD Member countries, but also among many non-Members, to evaluate the environmental implications of domestic and foreign investment projects. EIA procedures require project proponents to evaluate the environmental consequences of a proposed project. Public authorities can block projects whose impacts are judged unacceptable, or they can require modifications to the project or specify environmental requirements which must be met. EIA procedures in most OECD countries provide for public participation in decision-making.

9. A country's policy on environmental liability can also be a major factor in investment decisions. Uncertainty about liability for future environmental damage or for the clean-up of past environmental damage can deter potential investors and creditors. For example, potential liability from past environmental practices was cited as the most important environmental issue among a survey of the 1001 largest mining, construction and manufacturing companies in North America and western Europe that had made or considered investment in central and eastern Europe. This was followed by concern about liability for present and future practices and uncertainty about environmental standards⁶. Environmental auditing and due diligence procedures have been developed to generate the information required to manage past environmental damage in investment decisions.

10. The level of environmental standards is important, but it is also crucial that the institutional arrangements are in place to ensure their effective implementation⁷. This, in turn, will depend on the capacities which exist in the public authorities to develop and implement environmental measures. Joint development of policies, and institutional mechanisms involving both environmental and investment authorities, can help balance the two sets of policy goals.

6 Klavins, J. and Zamparutti, A., 1995: Foreign Direct Investment and Environment in Central and Eastern Europe. A Survey. A Report for the Environmental Action Programme for Central and Eastern Europe. World Bank. Washington D.C. See also Goldenman, G. et al., 1994: *Environmental Liability and Privatization in Central and Eastern Europe*. A Report for the Environmental Action Programme for Central and Eastern Europe. Graham and Trotman/Martinus Nijhoff. London/Dordrecht/Boston.

7 Esty, D.C. and Gentry, B.S., 1997: "Foreign Investment, Globalisation, and Environment" in OECD, 1997: *Globalisation and Environment. Preliminary Perspectives*. OECD Proceedings Series. OECD. Paris.

Issues for discussion

- *What are the key policy and institutional requirements to ensure an effective management of the environmental impact of investment ?*
- *How do participants judge the effectiveness of Environmental Impact Assessment and other tools for managing investment-related environmental problems ? Could they make suggestions for improvement, if needed ?*
- *What types of policies, policy instruments and institutional arrangements have been implemented to improve the coherence of investment and environmental goals, and what lessons can be drawn from their implementation ?*

Workshop 2: The Role of voluntary commitments

11. Enterprises, individually and collectively, are committed to a variety of “voluntary”, or non-binding initiatives, concerning the environmental consequences of their activities. Examples include the “Responsible Care” initiative of the chemicals industry and the Business Charter for Sustainable Development developed under the aegis of the International Chamber of Commerce. The Coalition for Environmentally Responsible Economies (CERES) has adopted ten principles that emphasise environmental indicators and management approaches⁸. Companies endorsing the principles undertake voluntarily to go beyond formalistic compliance with prevailing legal requirements. Participants commit themselves annually to complete the CERES report on progress in implementing the principles and to make it public.

12. Guidelines for enterprises have also been developed in consultations involving intergovernmental organisations, business and other stakeholders. For example, the non-binding OECD Guidelines for Multinational Enterprises have an environment chapter⁹. These Guidelines are currently under review. This review will address both the operating procedures and the text with the aim of making the Guidelines more effective in promoting good corporate conduct. The UNEP, responding to the growing awareness in the financial community of the linkages between environmental and corporate performance, has developed a Financial Institutions Initiative on the Environment, including a Statement by Financial Institutions on the Environment and Sustainable Development.

13. At the enterprise level, more and more companies are reporting on their environmental performance, often accredited under the European Union’s EMAS system or ISO 14000. The reduction of waste and emissions, and continuous improvement in environmental performance, are key features in such reports.

14. Implementation, monitoring and evaluation are of critical importance in determining the effectiveness of voluntary initiatives. An UNCTAD survey in the early 1990s showed that multinational

8 The principles cover protection of the biosphere, sustainable use of natural resources, waste reduction and disposal, energy conservation, risk reduction, safe products and services, informing the public, management commitment and audits/reports. Among the companies that have endorsed the principles are General Motors, Polaroid and the Body Shop.

9 The text of, and additional information on, the OECD Guidelines for Multinational Enterprises are available on the Internet, at <http://www.oecd.org/daf>.

enterprises do not use the guidelines developed by public institutions as much as they use sector and industry-based codes.¹⁰ Yet involving other stakeholders (government, trade unions, employees, NGOs, consumer groups, the finance industry) in the development of voluntary agreements, and the monitoring of their implementation, can significantly strengthen their credibility.

15. Enterprises may be called upon to heed the often heard demands for greater consistency in, and standardisation of, their reporting on environmental performance, including in their investments. This would facilitate benchmarking and the assessment of the environmental component of company performance.

Issues for discussion

- *What should be the role of non-legally binding standards in the field of FDI and environment, in addition to legal requirements ?*
- *Could participants provide evidence of effective voluntary standards in the aforementioned field ? Could these experiences be generalised, or are they specific for the sector or countries concerned ?*
- *What are the requirements to ensure that voluntary commitments, on the level of individual companies or sectors, as well as on national or international level, are effective ?*
- *What types of information are most needed in environmental performance reporting by companies, particularly where their investment is concerned ? What criteria or indicators would be most useful to assess performance over time ?*
- *How might business strengthen its dialogue with the above-mentioned stakeholders in developing, implementing and monitoring the performance of voluntary commitments ?*

Workshop 3: The Impact of FDI on environmental standards: Pollution havens and pollution halos

16. There has been considerable debate about whether or not FDI is directed to countries with lower environmental standards in order to benefit from reduced compliance costs: the so-called “pollution haven” hypothesis. Research suggests that, in general, companies do not invest abroad with the primary goal of reducing their environmental compliance costs; other costs appear to be more significant in influencing investment location decisions¹¹. However, this research is rather oriented towards western enterprises and it cannot be taken for granted that the outcome would be different in other parts of the world. Furthermore, there is some evidence that, for some firms in some industries, migration to jurisdictions with lower environmental standards, and accordingly lower compliance costs, may occur. For example, industries that face higher than average pollution control costs, or industries whose products are relatively undifferentiated and whose market share is sensitive to small cost differences.

17. Most large investors researched argue that they would prefer clear, stable environmental regulations that are consistently enforced without discrimination between foreign and domestic investors,

10 UNCTAD, 1993: *Environmental Management in Transnational Corporations: Report on the Benchmark Corporate Environmental Survey*. UNCTAD. Geneva.

11 Esty, D.C. and Gentry, B.S., 1997: see Footnote 8.

rather than unclear standards and inconsistent enforcement. Minimising regulatory risks generally helps to attract industries that want reliable overseas bases of operation¹².

18. Foreign investors can also act to raise environmental performance and standards. Large multinational companies often apply a single set of corporate standards to their operations in all countries, and they have sometimes lobbied for the adoption of similar standards in the host country. While this may improve environmental standards and help establish a level playing-field in the host country, it may also provide the investor with a short-term competitive advantage *vis-à-vis* local producers. The potentially adverse consequences of world-wide bad publicity on environmental performance provides an extra incentive for investors to apply high environmental standards. However, smaller investors in countries where environment does not feature high on the political agenda may be influenced by different considerations.

19. Some commentators have argued that “pollution halos”, *i.e.* countries or regions which attract FDI by implementing high environmental standards, are more likely to develop in some circumstances than “pollution havens”. For example, some governments may implement high environmental standards as part of a broader economic development objective that aims to move a country further up the development ladder. Some countries have made clear policy choices to shift away from first generation, pollution-intensive industries and to increase the share of light industry, and promote investments by high technology, knowledge-intensive industries and services. These sectors generally provide higher value-added, cause less pollution and are more resource-efficient.

Issues for discussion

- *What empirical evidence exists concerning the pollution haven and pollution halo hypotheses ? What is the evidence from different industrial sectors, from countries at different stages of economic development and from countries of different economic structures (e.g. economies based primarily on natural resources or manufacturing or services) ?*
- *Are there cases where foreign investors have contributed to raising environmental standards in host countries ? What have been the key drivers behind this ? Has this resulted in improved environmental conditions and progress in meeting national and international environmental policy commitments ?*
- *What types of research and analysis would be most useful to shed further light on the pollution haven and pollution halo hypotheses ?*

12 Esty, D.C. and Gentry, B.S., 1997: see Footnote 8.

ANNEX

Table 1

FDI outflows by country, 1990-97 (\$ mln)

<i>US</i>	539,993
<i>UK</i>	244,742
<i>France</i>	217,640
<i>Japan</i>	199,662
<i>Germany</i>	199,237
<i>Netherlands</i>	131,257
<i>Hong Kong</i>	130,073
<i>Switzerland</i>	81,038
<i>Canada</i>	61,717
<i>Italy</i>	57,587
<i>Sweden</i>	57,329
<i>Belg.-Lux.</i>	55,770
<i>Spain</i>	33,209
<i>Australia</i>	26,109
<i>Chinese Taipei</i>	25,925
<i>Singapore</i>	24,111
<i>Denmark</i>	20,912
<i>Finland</i>	20,347
<i>Korea</i>	20,013
<i>Norway</i>	18,861
<i>China</i>	18,820
<i>Malaysia</i>	12,158
<i>Austria</i>	11,388
<i>Kuwait</i>	6,814
<i>Chile</i>	5,720

Source: OECD, IMF, UNCTAD

Table 2

Total FDI inflows by country, 1990-97 (\$ million)

<i>US</i>	414,074
<i>China</i>	200,578
<i>UK</i>	176,889
<i>France</i>	149,587
<i>BLEU</i>	84,008
<i>Netherlands</i>	70,743
<i>Spain</i>	68,068
<i>Mexico</i>	58,850
<i>Canada</i>	53,818
<i>Australia</i>	52,212
<i>Singapore</i>	49,173
<i>Sweden</i>	47,546
<i>Brazil</i>	44,228
<i>Malaysia</i>	35,177
<i>Italy</i>	30,394
<i>Argentina</i>	30,120
<i>Indonesia</i>	23,684
<i>Germany</i>	21,475
<i>Switzerland</i>	20,188
<i>Chile</i>	19,085
<i>Denmark</i>	18,177
<i>Thailand</i>	17,177
<i>New Zealand</i>	17,083
<i>Poland</i>	15,882
<i>Colombia</i>	15,798

Source: OECD, IMF, UNCTAD