Incentivising sustainable FDI

SUSTAINABILITY

CREATING A SPECIAL RSI CATEGORY WOULD INCREASE THE DEVELOPMENTAL IMPACT OF FDI, WRITE **KARL P. SAUVANT** AND **EVAN GABOR**

Illustration by John Holcroft

Foreign direct investment (FDI) can contribute significantly to development. But how can its positive impact be increased by attracting FDI that is more purposefully aligned with each individual country's development goals? Or, to put it differently, how does a country determine what sorts of FDI ought to be considered sustainable — a commercially viable investment that makes a reasonable contribution to the economic, social and environmental development of host countries and takes place in the context of fair governance mechanisms.

One way for a country to increase the level of sustainable FDI and, therefore, the developmental impact of FDI, could be creating a special category of 'Recognised Sustainable Investor' (RSI). This would help governments to influence investors' decisions to align with the tenets of sustainable FDI, and to observe corporate social responsibility (CSR) guidelines and international standards of responsible business conduct.

Setting this up could consist of three main parts:

1. Establishing basic criteria that all investors must meet to qualify as an RSI;
2. Allowing for country-specific FDI sustainability characteristics, established by the host country, that investors would commit to meeting;
3. Granting special benefits to RSIs beyond those generally available to all foreign investors.

Basic criteria

The first part would set basic criteria to be met by any investor wishing to qualify as an RSI within a given jurisdiction. The first basic criterion would require that investors commit to observe certain recognised and widely accepted intergovernmental guidelines — especially the UN Guiding Principles on Business and Human Rights, the International Labour Organization's MNE Declaration, the OECD Guidelines for Multinational Enterprises — and, if applicable, certain industry-specific codes.

In addition to this criterion, investors would need to meet any two or three of the following additional requirements:

- Making their CSR statements and progress reports widely available;
- Having a record of compliance with local laws and regulations;
- Maintaining a system of records to allow for necessary internal controls;
- Having a history of access to loans based on environmental, social and governance performance;
- Maintaining an appropriate due diligence and supply-chain risk-management system.

These basis requirements will contribute to increase investment with certain sustainability characteristics into the host countries. They will also help ensure that the investors who receive RSI benefits accept internationally recognised norms on responsible business conduct directly relevant to sustainable FDI and to show a history of responsible behaviour in their operations.

Country-specific FDI sustainability characteristics

In addition to meeting the basic criteria, investors would have to make reasonable best efforts to ensure that their investments contribute as much as possible to certain country-specific FDI sustainability characteristics, in order to qualify as an RSI.

Each country would provide its own list of sustainability characteristics. For example, a country could specify that investors would qualify as an RSI within its jurisdiction if they made commitments to use reasonable best efforts to do any two of the following across all investment entities they control within a jurisdiction:

- Creating a given number of jobs;
- Creating backward linkages;
- Engaging in community development;
- Reducing their carbon footprint;
- Following proper resource-management practices;
- Using non-discriminatory hiring practices;
- Providing specific skill-based training;
- Maintaining a high level of supply chain standards;
- Engaging with stakeholders.

Allowing countries to indicate the characteristics that qualify investors as 'sustainable' ensures that the RSI benefits target the investors who directly support each specific country's development goals. Additionally, providing a list of sustainability characteristics from which to choose, rather than specific ones, gives investors the flexibility to elect those characteristics most appropriate for their projects.

Special benefits

Why would an investor commit to potential costs associated with complying with the basic and country specific criteria? The answer lies in the incentive structure that creates a business case for becoming an RSI by providing special benefits. An investor that meets the criteria would:

- Qualify for additional special RSI benefits beyond those generally available to all investors.
- Benefit from the positive publicity of the country's RSI label.

The additional RSI benefits would be chosen and publicised by each country; these could include:

- Assigning individual case officers to qualifying investors who would assist them in all matters related to the establishment and operation of their projects throughout their investment lifecycles, to help them resolve any difficulties they might experience;
- Assisting qualifying investors on a priority basis (and at reduced fees and/or charges), in obtaining licenses, meeting other requirements and procedures (including the processing of applications), and by granting simplified investment document approval and shortened timeframes for approvals;
- Establishing a 'green channel' that would allow a qualifying investor's employees expedited entry into the host country;
- Helping qualifying investors in establishing local backward and forward linkages through, for example, programs that upgrade local suppliers;
- Aiding efforts to secure land for production purposes;
- Creating specialised employee training programs geared specifically toward investments by qualifying investors;
- Offering targeted fiscal, financial or other incentives to qualifying investors, including, for example, access to lower interest loans, special grants or subsidised infrastructure and services.

Countries attract FDI to advance their sustainable development. Accordingly, they seek to benefit as much as possible from the investment they obtain. Creating the special category of the RSI provides governments with a tool to incentivise sustainable FDI for sustainable development. Countries should utilise this tool.

Special benefits could also include various 'soft' recognitions. To begin with, the label '[Country A] RSI' would constitute, in and of itself, valuable recognition for any firm. Beyond that, for example, recognition could be given to RSIs through award ceremonies or special events attended by high-ranking officials. ■

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CASE STUDY

THE RSI MECHANISM IN PRACTICE: GHANA'S EXPERIENCE

The 'Recognised Sustainable Investor' (RSI) category is a mechanism that allows governments and firms to work together in a way that brings benefits to both, writes Matthew Stephenson. Governments want to ensure that foreign direct investment (FDI) is aligned with their development goals; firms want to be credited and recognised for good stewardship in their business operations, and also will gladly accept additional support, whether financial or non-financial.

The beauty of the mechanism lies in the fact that governments can work with firms to identify the specific development contribution that FDI is asked to make — for instance jobs, training or environmental protection — and so there is flexibility to tailor the RSI to the capacity of different firms to contribute in different ways.

The World Economic Forum (WEF) has worked with the Ghana Investment Promotion Centre on pioneering the RSI as part of a pilot project on facilitating sustainable FDI. As a result, the RSI was recently included in tax legislation. Ghana felt that it could better tailor and target its investment incentives this way. And now, there is a general shift across the world to what investment promotion agencies are calling 'smart incentives'; the RSI represents a mechanism to deliver these.

There is an opportunity to work with both the public and private sectors to scale measures that facilitate sustainable investment. The aim is to address the mismatch in global capital flows: sustainability-focused finance increased by 80% in 2020 to $3.2tn; yet, over the same period, FDI fell by 35% globally.

To this end, the WEF is inviting governments, international organisations and firms to launch public–private projects that Enable Action on Sustainable Investment (Easi). Easi projects will create a mechanism to combine finance mobilisation and policy reform, thereby helping get capital flowing to where it is most needed in developing countries and emerging markets.

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