SOUTH AFRICA, AFRICA, AND INTERNATIONAL INVESTMENT AGREEMENTS

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Introduction

The Centre for Conflict Resolution (CCR), Cape Town, South Africa, and the South African Department of Trade and Industry (DTI) hosted a policy advisory group seminar in Stellenbosch, South Africa, from 17 to 18 February 2014, on “South Africa, Africa, and International Investment Agreements”.

The meeting brought together about 30 policymakers, scholars, and civil society actors from Africa, Asia, Europe, North America, and South America, to assess and broaden the debate on the implications of international investment agreements (IIAs) – including bilateral investment treaties (BITs) – for development efforts in Africa. The meeting also assessed the principles that underpin these agreements, which were conceived in the immediate post-colonial era during the Cold War, and are increasingly seen by critics as being at odds with emerging economic challenges confronting developing countries.

Particular attention was paid to six key areas: the global context and changing perspectives on international investment agreements; the benefits that can accrue from foreign direct investment (FDI) and the relationship between investment agreements and foreign direct investment flows; the structure and impact of investment treaties; the core provisions of international investment agreements; the international arbitration system that provides for investor claims against states; and the implications of all this for Africa’s structural transformation and economic development.

1. Global Change and the International Investment Agreements Landscape

Foreign direct investment is important for economic development, helping host countries to generate inflows of capital and finance; technological innovation; managerial best practices; and access to global markets. However, structural changes to the world economy following the global financial crisis of 2008/2009 have strengthened the view that the benefits of such investment to the development of host countries are not automatic. Proponents of international investment agreements acknowledge that governments sacrifice some measure of regulatory autonomy when they sign these treaties. Nevertheless, they argue that the system of international investment agreements can be reformed – particularly by redrafting legal texts and through reform of arbitration mechanisms – to strike an appropriate balance between state sovereignty and investor rights. Other economists and policymakers take different views. Some advocate termination of international investment agreements and their replacement by a new model, while others oppose subjecting investor claims to international arbitration. All these approaches have aimed, to a greater or lesser extent, at ensuring that the right of sovereign governments to regulate foreign investors is not unduly impeded.

Over the past decade, reviews of investment treaties have been undertaken in Australia, Canada, Brazil, India, Norway, South Africa, the United States (US), and the European Union (EU). Actions taken by countries to address the
2. Determinants of Foreign Direct Investment and the Role of International Investment Treaties

International and bilateral investment agreements are often promoted as means of attracting foreign direct investment. In pursuit of such investment, some governments are prepared to offer strong protections to foreign investors and to liberalise investment regimes. However, there is little evidence of any direct link between foreign investment inflows and signing investment agreements. Increased foreign investment following the adoption of international and bilateral investment treaties is often more the result of other factors such as the promise of returns on investments and business strategies, as well as national economic reforms and domestic investment and trade regimes. Although international investment agreements have been promoted as instruments that encourage multinational corporations (MNCs) to invest in politically volatile jurisdictions, such firms often make their investment decisions regardless of the existence of such treaties. Investors are instead often guided by profit and ease of access to resources, labour, and regional markets. Foreign investment in mining, oil, and gas in volatile areas in countries such as Angola, Nigeria, and Libya is overwhelmingly driven by the prospect of high returns. Although foreign direct investment can produce economic benefits, it has also sometimes contributed to environmental damage; resulted in economic development in enclaves that has not contributed to broader national economic growth; and negatively affected the balance of payments in some countries.

In order to promote more effective management of international and bilateral investment agreements to foster sustainable development, the Paris-based Organisation for Economic Cooperation and Development (OECD) and the Geneva-based United Nations Conference on Trade and Development (UNCTAD) should work to forge a set of common principles that can guide the future development and practical application of international treaties, while also promoting a shared understanding of their potential impacts on host economies.

3. The Policy Impact of International Investment Agreements in Africa

By December 2013, 793 bilateral investment treaties had been concluded by African countries, representing 27 percent of the total number of such agreements. Most of these treaties employ expansive definitions and standards of protection to address state regulatory activity and standards, and provide for international investor-state dispute settlement (ISDS) mechanisms that generally favour the enforcement of the rights of foreign
investors. International investment agreements in Africa consist of bilateral treaties or provisions in preferential trade agreements (PTAs).

These investment treaties have sometimes constrained the capacity of African governments to fulfil their regulatory mandates to advance the public interest, while placing few obligations on the activities and conduct of foreign investors. Foreign firms are rarely required to integrate their operations into domestic value chains or to promote broader national industrialisation efforts. These agreements have also sometimes inhibited the imposition of developmental conditions of entry or operation on foreign investors such as the establishment of joint ventures, the transfer of technology, the purchase of domestic inputs; or undertakings to support research and development.

Most external investments in Africa seek to exploit the continent’s oil, gas, and mineral wealth. Conceding economic control over the terms on which foreign investors extract these natural resources can often undermine national and regional beneficiation policies and legislation to promote sustainable socio-economic development. For example, foreign investors may use international investment treaties to challenge tax regimes that seek to impose levies on mineral exports in support of industrialisation efforts. Investment agreements further impose differential treatment of foreign and domestic investors that often favours the former, and can abrogate beneficial terms of trade enjoyed by a country as a most favoured nation (MFN). Arbitration resulting from international investment agreements can further drain national bureaucratic, legal, and financial resources, leading to unwillingness on the part of African and other governments to contest cases, or to introduce legislation in the public interest for fear of legal repercussions.


The expansive scope and content of international investment agreements exacerbates their capacity to undermine the policy autonomy of governments in developing countries. Investment treaties typically include a preamble stating the goals of the parties; umbrella clauses that place blanket obligations on host states; and broad definitions of “investor” and “investment”. They also include substantive provisions that oblige host states to accord foreign investors “fair and equitable treatment”; to compensate them for any direct or indirect expropriation of their property; to allow the transfer of capital in and out of the host country by foreign investors; and to enable claims to be brought against host states through international arbitration.

Key definitions in these treaties have been contested in court, leading to contradictory arbitration awards. For example, the definition of “investment” can cover a wide range of “assets” beyond productive enterprises. Similarly, the definition of “expropriation” can extend to “regulatory takings” which cover any new policy measures that affect potential revenues and profits. “Fair and equitable treatment” has been controversially interpreted as granting foreign investors the right to challenge any government measure that could be interpreted as affecting a “predictable regulatory environment”. Most seriously, these investment treaties also contain provisions for an investor-state dispute settlement system which allow foreign investors to sue host governments in an international tribunal – a legal recourse that domestic firms do not enjoy.
and one that can undermine the national judicial sovereignty of host countries. International investment arbitration is also beset by inconsistent outcomes, many of which do not meet the standard of legal correctness. This compounds the uncertainty embedded in the agreements themselves.

Between 2007 and 2010, South Africa reviewed its 19 bilateral accords. Tshwane (Pretoria) concluded that the link between these treaties and increased foreign direct investment was uncertain, and that the ambiguity inherent in many of the standard provisions of these agreements created uncertainty for both investors and governments. As a result, South Africa decided to terminate its existing investment treaties, and only to enter into new ones if there were compelling economic or political reasons to do so. All partners were informed in advance about the decision to terminate these agreements. Tshwane has further introduced national legislation clarifying typical treaty provisions which can be adjudicated by domestic courts.

Meanwhile, the US and Canada have revised their model investment treaties, redrafting key provisions to clarify the rights of investors and to limit the scope of interpretation for arbitration panels. The EU has proposed new approaches to enhance the transparency of the process for negotiating these accords; the independence of arbitrators; and the predictability of the agreements, including through the possibility of binding interpretation by the parties involved. Brussels has also suggested the establishment of an appellate mechanism to ensure greater consistency in arbitration processes.

5. Assessing the Investor-State Dispute Settlement System

The investor-state dispute settlement system included in most international investment agreements enables foreign investors to sue host governments at an international tribunal – usually the Washington-based International Centre for the Settlement of Investment Disputes (ICSID) or the Vienna-based United Nations Commission on International Trade Law (UNCITRAL). If such a claim succeeds, the tribunal could award the investor financial compensation, which may be enforced through seizing government assets. Since its creation in 1966, the International Centre for the Settlement of Investment Disputes has concluded 282 cases, with 188 disputes still pending. In Africa, 25 percent of reported arbitrations involve mining, oil, and gas investments. Most international investment agreements also provide for State-to-State Dispute Settlement (SSDS), which allows cases to be brought between countries in relation to the application of investment treaties.

The investor-state dispute settlement system has become a multi-billion-dollar industry dominated by a small group of 20 law firms from Western countries. On average, each investor-state dispute costs $8 million in legal and arbitration fees, with some cases costing more than $30 million. Despite the large sums at stake, the system remains fragmented: a range of venues, each with its own history, culture, and rules of procedure, offer arbitration by panellists chosen in a relatively ad hoc manner. The same small group of lawyers rotates between representing claimants and respondents, and sitting on arbitration panels, raising serious concerns over conflicts of interest.
The system lacks an institutional framework that enshrines the principles of judicial accountability and independence. Arbitrators can award damages without having to apply the limitations on state liability that have evolved in domestic legal systems. Furthermore, in the absence of an appellate process, the system is prone to diverging interpretations in cases addressing the same provisions and similar facts, which has exacerbated uncertainty about the meaning of key obligations under these treaties. Concerns have also been raised over the secrecy of many aspects of these arbitration hearings. Unless and until this dispute system is reformed, consideration should be given to a moratorium on using it. State-to-state dispute settlement may provide a useful alternative avenue.

6. Regional Regulation of Investments in Africa

Africa’s governments, its regional economic communities (RECs), and the African Union (AU) have increasingly sought to address how international investment agreements can be managed at the sub-regional and continental levels. They have also examined the role of these treaties in Africa’s efforts to promote industrialisation and sustainable economic development. Fourteen of the 15 countries in the Southern African Development Community (SADC) have ratified a 2006 Finance and Investment Protocol (FIP), which came into force in 2010. However, regional norms on investment frameworks are often out of step with national policies, and are further undermined by competition for investment among African states. The African Union Commission has identified a need to align the investment protocols adopted by Africa’s sub-regional organisations such as SADC, the Economic Community of West African States (ECOWAS), the Common Market for Eastern and Southern Africa (COMESA), and the East African Community (EAC) with frameworks being proposed by the continental body. The AU Commission is seeking to harness investment flows to strategic economic objectives for Africa which include: enhancing the continent’s share of global markets; boosting intra-African trade; fast-tracking the establishment of a continental free trade area; accelerating Africa’s industrial development; and implementing the Africa Mining Vision and Action Plan, which was adopted by the AU in February 2009. The forging of such policies may entail a comprehensive review of all African international investment agreements, particularly if these treaties threaten national socio-economic plans and Africa’s wider development and integration objectives.

Policy Recommendations

The following ten policy recommendations emerged from the Stellenbosch policy advisory group seminar:

1. African governments should include properly researched and tested policies on international investment in their development strategies in order to support national economic diversification and industrialisation priorities;

2. African governments must draft investment laws that mobilise and harness domestic savings and funds, thereby decreasing dependence on foreign direct investment. Governments should also encourage international investors to look beyond international investment agreements for other means of creating an enabling environment to attract foreign direct investment.
3. African governments must review their international investment agreements to determine whether these treaties contribute to inclusive and socially equitable economic development. They should seek to amend or renegotiate these treaties, as necessary, in order to create a fair balance between the rights of investors and those of governments and their citizens;

4. African governments must retain their right to regulate investments in the public interest and minimise their exposure to damaging litigation in all negotiations related to aid, trade, and international investment agreements;

5. African civil society and private sector bodies; governments; and sub-regional and continental organisations should coordinate their efforts in order to harmonise protocols and legal frameworks regulating foreign investment. African governments must also ensure that commitments agreed under investment treaties do not undermine the continent’s integration efforts;

6. The oversight role of African parliaments over international investment agreements should be strengthened through greater coordination between national legislatures and the sub-regional and continental committees responsible for promoting investment legislation in support of Africa’s economic development;

7. The existing institutional architecture for investor-state dispute settlement must be reviewed to ensure fairer and more equitable outcomes; measures to ensure the transparency of the system, particularly in respect of investor-state disputes, should be integrated into investment treaties; the processes for nominating and selecting arbitrators in investment disputes must also be revised to enlarge the pool and ensure representation of a broader spectrum of interests. Consideration should be given to employing tenured judges as arbitrators. A code of conduct for arbitrators must also be introduced, and an effective appeals process should be established;

8. African governments must explore alternative models for the investor-state dispute settlement process, such as promulgating national legislation that prioritises the domestic adjudication of disputes; establishes independent trade courts; and promotes African dispute settlement systems. State-to-state dispute settlement should be promoted as an effective alternative to investor-state dispute settlement;

9. The African Union Commission must facilitate a dialogue among African trade ministers and sub-regional bodies on the impact of international investment agreements on the continent’s development agenda, at which lessons learned in international investment agreement negotiations should be shared and implemented; and

10. Africa’s regional organisations must coordinate with the continent’s think-tanks to develop common benchmarks for evaluating the quantitative and qualitative impact of investment policies - including those that promote international investment agreements - on sustainable development in Africa.