AfCFTA investment negotiations

Notes on concepts

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Contents

Acronyms

AfCFTA	African Continental Free Trade
AfDB	African Development Bank
ARIA	Assessing Regional Integration in Africa
AU	African Union
AUC	African Union Commission
BIT	bilateral investment treaty
CCSI	Columbia Center on Sustainable Investment
CFIA	cooperation and facilitation investment agreement
COMAI	Conference of African Ministers in Charge of Integration
COMESA	Common Market for Eastern and Southern Africa
CDIS	Coordinated Direct Investment Survey
ECA	United Nations Economic Commission for Africa
EPA	Economic Partnership Agreement
EU	European Union
FDI	foreign direct investment
FET	Fair and Equitable Treatment
FTA	Free Trade Agreement
GATS	General Agreement on Trade in Services
GVC	global value chain
IIA	international investment agreement
IISD	International Institute for Sustainable Development
IMF	International Monetary Fund
ISDS	investor–state dispute settlement
M&A	mergers and acquisitions
MFN	most-favoured nation
MIA	multilateral investment agreement
MNC	multinational corporation
ODI	Overseas Development Institute
OECD	Organisation for Economic Co-operation and Development
PAIC	Pan-African Investment Code
SADC	Southern African Development Community
SDG	Sustainable Development Goal
TIP	treaty/agreement with investment provisions
UK	United Kingdom
UNCTAD	United Nations Conference on Trade and Development
UNCITRAL	United Nations Commission on International Trade Law
UNGPs	United Nations Guiding Principles on Business and Human Rights
US	United States
USMCA	US–Mexico–Canada Agreement

1 Introduction

The African Continental Free Trade Area (AfCFTA) aims to increase intra-African trade and transform the economies on the African continent. These are critical objectives set in the African Union's Agenda 2063, aiming to reduce external dependence on commodity exports and increase value addition on the continent.

Implementation of Phase I of the AfCFTA, to start in January 2021, will gradually bring down barriers to trade between its members. Although it will not address the physical and infrastructure barriers that limit trade between African countries, or institutional and legal barriers, the AfCFTA could create opportunities to work towards dealing with them.

In Phase II, the AfCFTA aims to deepen economic relationships between African countries by negotiating provisions aimed at increasing bilateral investment.[1] Accomplishment of Agenda 2063 requires the design and implementation of tools that, in addition to eliminating trade barriers, can also contribute to developing productive capabilities across the continent. In this sense, increasing investment across Africa will contribute simultaneously to transforming economies and increasing bilateral trade flows.

Most African countries have negotiated bilateral investment treaties (BITs) among themselves and with non-African countries. In general, these aim to liberalise flows and eliminate investment restrictions between countries; and to provide a space and/or procedure to resolve investment-related disputes that may arise between entities in the signatory countries. In this sense, non-discriminatory treatment of partners with respect to domestic investors and the protection of concessions and property rights in the signatory country appear as key provisions in these types of agreements.

However, investment has effects that go beyond strictly private business and trade relations. It has significant impacts in wider social, environmental and human rights dimensions. Investments not only produce profits for their shareholders but also affect in many ways the lives of the people in the host country. There is an investor responsibility that exceeds the legal boundaries of the investment and that means that actions will be required to mitigate any negative impact.

BITs, by their design, have not been able to address these issues and, in many cases, have actually problematised government policies in these areas. Provisions on investment protection have complicated the implementation of policies in a wide range of areas whenever investors' profits or investments have been affected.

Moreover, the evidence on the effectiveness of traditional BITs in terms of increasing investment is particularly weak. Non-discriminatory provisions appear to be insufficient in terms of attracting the investment necessary to develop productive capacities. In this sense, the facilitation of investment should be part of the strategy to increase investment.

This suggests that a modern and effective investment agreement should provide for a balanced allocation of rights and responsibilities between actors. Investors need guarantees and securities to ensure that their investments are safe and that they will be treated fairly with respect to domestic competitors. They are also responsible for conducting their business in the host country in a manner

[1] Phase II will also include negotiations on competition policy and intellectual property rights.

that is respectful of legislation, as well as assuming their role in the economic development of the host country.

Governments, on the other hand, have the obligation to maximise social well-being for the whole of society. Investment agreements should not prevent governments implementing their policies whenever they have a genuine ultimate goal. In addition, governments have the responsibility for creating a space that facilitates investment, making transparent and clear any requirements.

Negotiations on investment on Phase II aim to bring all these elements together. They aim to create a common environment on the continent for flows of intra-African investment, to facilitate and protect this without giving up wider policy space. Phase II also aims to create a common platform for negotiations on investment that African countries could undertake with third countries. The objective is to ensure that these negotiations contribute to the continental effort rather than undermining it.

This collection of pieces has the goal of facilitating and assisting negotiators in each African country to navigate the complexity of the negotiation topics under discussion. It aims to provide some basic information, concepts, discussions and additional references to contribute to an understanding and formation of the respective negotiation position in each country. The notes are not intended to guide negotiations towards a particular outcome but rather to explain the options available.

This collection begins with a discussion of very simple definitions of investment and of its economic effects, provided by Dirk Willem te Velde from ODI. This section should provide negotiators with insights on how investment can affect economic transformation in their country.

Thierry Mutombo highlights the architecture of BITs with the aim of explaining how the AfCFTA may be structured, as well as discussing typical provisions. This will provide an initial insight into the main components the AfCFTA may have.

Jamie MacLeod presents an overview of the Pan-African Investment Code (PAIC) and its relationship with the current phase II negotiations of the AfCFTA, specifically in relation with the draft investment protocol.

Sarah Brewin from IISD discusses investment protection and dispute settlement. Her section describes the scope and limits of different provisions that aim to protect investment as well as resolve controversies. These include state–state and investor–state dispute resolution mechanisms.

Brooke Güven of CCSI looks at investment promotion and facilitation, by presenting typical provisions to pull and facilitate investment. In another section, she discusses modern provisions in BITs associated with social, environmental, labour and health outcomes.

Finally, Stephen Gelb from ODI describes the main characteristics of investment in Africa, highlighting differences between intra- and extra-continent investment. In particular, this discussion aims to show how both types of investment contribute to economic transformation.

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Max Mendez-Parra is a Senior Research Fellow at ODI. He is an economist with more than 20 years of experience in analysing trade and investment policy in developing countries. He was a trade official at the Ministry of Agriculture in Argentina where he provided analytical support in the multilateral and bilateral negotiations. He worked for the Inter-American Development Bank in the impact analysis of multilateral and bilateral negotiations in Latin America. He has an extensive knowledge of the WTO and bilateral agreements involving developed and developing countries.He has provided research and analytical support in the EU GSP Mid-term review, including the assessment of the use of preferences by beneficiaries. He has worked in multiple assignments involving assessing the impact of trade and investment policies on economic growth in Africa. Recently, he has been involved in assessing the AfCFTA implementation capabilities in Ghana as well as assessing investment opportunities and barriers in Nigeria.. He has obtained his Phd from the University of Sussex.

3 Investment: definitions and economic effects

Dirk Willem te Velde

This note looks at definitions of investment commonly used in investment negotiations and presents a general discussion of the main economic effects of investment.

3.1 What is investment?

Investment often refers to gross fixed capital formation in the National Accounts, but in the context of trade and investment agreements it tends to refer to **foreign (direct) investment** (FDI), a category in the country's Balance of Payments (Box 3.1). Investment is different from other cross-border engagements such as global value chains, where a buyer places orders with manufacturers (often) without investing in them.

International investment agreements (IIAs) can cover investment as a separate chapter or as part of services, as one of the modes of supply. The definition of investment within such IIAs is significant, since it defines their scope and reach. The primary question when defining investment is **whether investment other than FDI should be incorporated**, such as portfolio investment, both equity and debt components, other capital flows and various investment assets, both tangible and intangible, including intellectual property rights.

If the definition is broad, and provisions on national treatment are general and binding, this may also mean that protection covers sovereign bond issuances and so-called vulture funds. It is important to assess whether this is what is intended, especially in times of crises.

Box 3.1: What is foreign direct investment?

'Direct investment is a category of cross-border investment made by a resident in one economy (the direct investor) with the objective of establishing a lasting interest in an enterprise (the direct investment enterprise) that is resident in an economy other than that of the direct investor. The motivation of the direct investor is a strategic long-term relationship with the direct investment enterprise to ensure a significant degree of influence by the direct investor in the management of the direct investment enterprise. The "lasting interest" is evidenced when the direct investor owns at least 10% of the voting power of the direct investment enterprise. Direct investment may also allow the direct investor to gain access to the economy of the direct investment enterprise which it might otherwise be unable to do. The objectives of direct investment are different from those of portfolio investment whereby investors do not generally expect to influence the management of the enterprise.'

Source: OECD (2008)

There is no universal definition of investment, and not all agreements incorporate a precise definition. At the multilateral level, for example, the Agreement on Trade-related Investment Measures does not define investment, and the General Agreement on Trade in Services (GATS) defines it simply as a 'commercial presence'. Broadly, where IIAs define 'investment', they employ three types of definitions: asset-based, transaction-based and enterprise-based.

1. **Asset-based definition:** This is common in investment protection agreements (e.g. bilateral investment treaties) and includes assets and capital flows, moveable and immovable property, interests in companies, claims to money, intellectual property rights and concessions. While the definition is broad enough to include both direct and portfolio investment, it tends to exclude assets that are not related to long-term investment. The scope of the definition is often

restricted (e.g. to exclude portfolio investments or to limit the minimum size of an investment).

2. **Transaction-based definition:** This type of definition is typically found in IIAs that concern the liberalisation of cross-border financial flows through which an investment is made. An example of this approach is the definition used in Annex A of the Organisation for Economic Co-operation and Development (OECD) Code of Liberalisation of Capital Movements. The Code does not define investment but lists a number of capital transactions between residents and non-residents that are the subject of liberalisation commitments.
3. **Enterprise-based definition:** This confines investment provisions to enterprises established by foreign investors within a host country. The GATS' definition of investment as a 'commercial presence' is in effect an example of this type of definition. Another example of this approach is the Free Trade Agreement between Canada and the US 1988 (Chapter 16, Investment).

Investment negotiators often think about attracting FDI (Box 3.1) when designing investment provisions. However, not all FDI is the same. The international business school literature defines **four categories of motivations for FDI**: natural resource-seeking, efficiency-seeking, strategic asset-seeking and market-seeking FDI. The dominant **entry of foreign firms** is through cross-border mergers and acquisitions rather than through greenfield operations. **Financial instruments** related to FDI include equity, deposits, debt securities, loans, trade credit and other accounts. **Data on FDI** often distinguish between equity capital, reinvested earnings and other capital, including debt. Much of the FDI in Africa, for example, includes profits reinvested by multinationals. Further, as subsidiaries can provide loans to their parents for tax reasons, data FDI flows can be negative in a given year.

3.2 The economic impact of investment

Investment protocols usually contain development objectives such as sustainable development or economic transformation. The promotion, facilitation and protection of investment aims to contribute to these. Much has been written about the relationship between FDI and development over the past decades and whether regional integration can facilitate (quality) FDI. The main lessons are that (i) FDI has great potential to spur development but the effects are not automatic and require complementary policies and institutions; and (ii) regional integration tends to lead to increased FDI, including through the role of investment provisions, but a whole range of other factors are crucial and probably much more important. This means that investment protocols should always be seen in conjunction with other policies and factors in a country.

The United Nations Conference on Trade and Development (UNCTAD) (1999) reviews several areas through which FDI affects economic development (see table in the Appendix ; for additional reviews, see OECD, 2002; Farole and Winkler, 2013):

1. employment and incomes
2. capital formation and market access
3. structure of markets
4. technology and skills
5. fiscal revenues and
6. political economy.

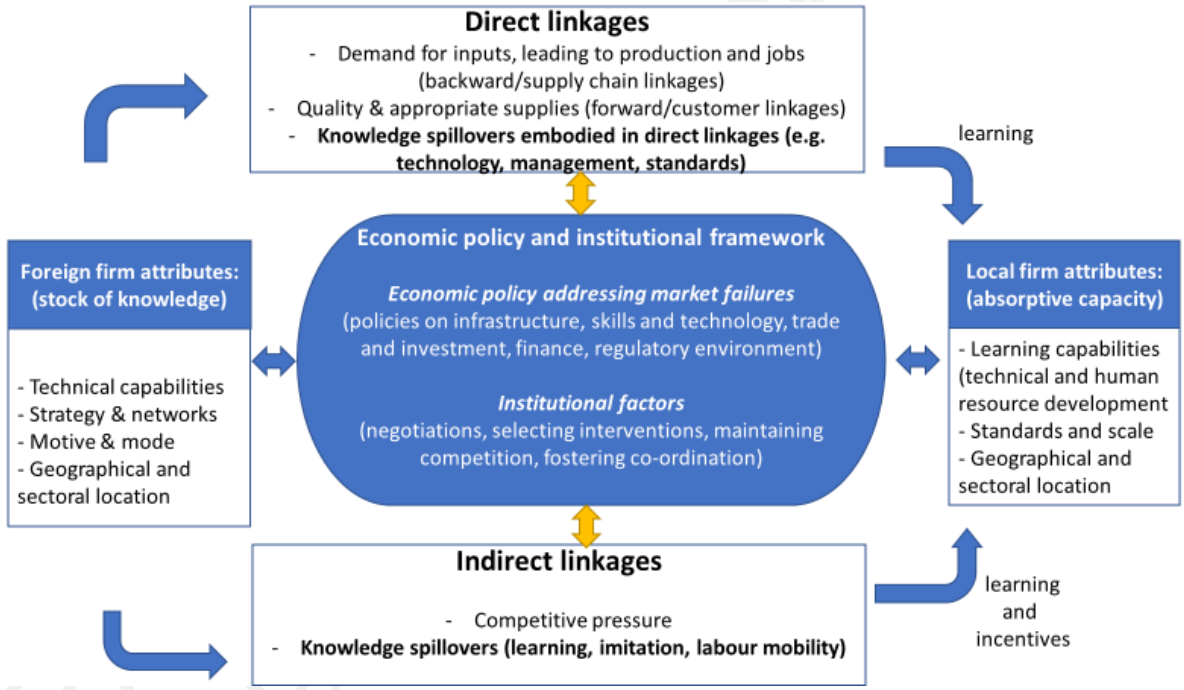
FDI leads to economic growth by increasing the amounts of factors of production (by increasing capital or employment directly, or indirectly in local suppliers and competitors), in the growth accounting context, or by increasing the efficiency with which these factors are used (by using superior technology or locating in high-productivity sectors, or through productivity spillovers to local firms), as expressed in the endogenous growth literature, with FDI being the port through which a country can access new ideas.

A crucial factor behind whether FDI affects the local economy temporarily or permanently is the extent of productivity spillovers. FDI-induced building-up of factors of production without

productivity effects can lead to a one-off shift in productive capabilities. This will lead to a one-off shift in incomes but a temporary shift in economic growth. In the long run, FDI-induced productivity change is important for long-lasting economic growth. This can happen through knowledge spillovers that enhance capabilities in local firms.

Figure 3.1 conceptualises the impact of FDI through linkages and spillovers, and the roles policy plays in this process (only some of which are included in investment protocols). Foreign firms bring with them a stock of knowledge and a set of strategies, standards and other attributes. They affect local firms through direct linkages (local firms selling to or buying from foreign firms) and indirect linkages. Spillovers refer to knowledge spillovers in the form of technological knowledge (including, e.g., on exporting) or knowledge on new management techniques that is being transferred from foreign to local firms. Such spillovers can occur through direct linkages, for example as part of a supplier relationship, or indirect linkages, such as when local firms imitate what foreign firms are doing (e.g. exporting, or developing and adapting new technology). Direct linkages refer to backward and forward vertical linkages; indirect linkages go beyond horizontal linkages and cover linkages between firms at the same or different levels in the value chain as the foreign firm, as long as they are not directly buying or selling to each other.

Figure 3.1: FDI, linkages, spillovers and the role of policy



Source: te Velde (2019)

Depending on the definition used in the investment protocol, investment can also include bank lending and portfolio debt and equity investment. Portfolio flows are often more volatile than FDI and can contribute to credit and consumer booms and busts. The impact of portfolio flows and bank lending is less positive compared with FDI (Hou et al., 2013), though as usual it depends on how flows are used.

UNCTAD data suggest that most FDI is either natural resource-seeking (e.g. UK or US FDI in oil and gas; FDI in Zambian copper; Tanzanian and Ghanaian gold) or market-seeking (South African supermarkets, major banks, telecommunications). This also relates to intra-African FDI. There is much less efficiency-seeking (and export-intensive) FDI, which countries (including the Asian Tigers and Costa Rica) around the world have used to upgrade their production structures and transform their economies. There are a few exceptions in Africa, such as Ethiopian garments and footwear and South African automobiles. There is also intra-Africa FDI in manufacturing, such as among East African Community countries.

There may also be differential effects of FDI depending on the mode of entry. In the short run, mergers and acquisitions (M&A) lead to a financial transfer, whereas greenfield investment will also lead to increased fixed capital formation, though this distinction is less strong in the long run. In the long run, the main difference seems to be that M&A tends to lead to increased concentration, whereas greenfield investment does the opposite (UNCTAD, 1999).

3.3 How does regional integration fit in?

As countries integrate as part of the AfCFTA, they are expected to increase efficiency-seeking as well as market-seeking FDI. The range of factors that attract FDI can be divided into:

1. general and specific host country economic conditions, which include market size and market growth; good-quality and appropriate infrastructure and skills; and natural resources
2. general and specific host country policies, institutions, administrative procedures and governance (e.g. the ease of doing business) and
3. international rules and activities (multilateral, bilateral and regional); and home country policies (e.g. directed credit, investment guarantees, etc.).

Te Velde (2006b), te Velde and Bezemer (2006), te Velde (2011) and te Velde and Munakula (2015) synthesise how different types of provisions in regional integration can support FDI and productivity change. Theory suggests that regional trade agreements are expected to lead to increased extra-regional FDI, but there are more ambiguous results for intra-regional FDI. An important reason for the ambiguity of the effects of trade rules is that multinational enterprises are motivated by exploiting firm-specific assets (e.g. firm-specific fixed costs) and hence want to enjoy economies of scale and scope, in addition to simply jumping trade barriers.

However, the *scope* of regional provisions is crucial. Dee and Gali (2003) and te Velde and Bezemer (2006) provide more details on the relevance of different types of regional investment provisions. Dee and Gali (2003) suggest that FDI responds significantly to the non-trade provisions of regional trade agreements (including investment provisions). Te Velde and Bezemer (2006) find that membership of a region as such is not significantly related to inward FDI, but, crucially, when a country is a member of a region with a sufficient number and level of trade and investment provisions (e.g. describing treatment of foreign firms, significant trade preferences), this will help attract more inward FDI to the region.

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Appendix: Inward FDI and economic development

Impact area	**Static effects**		**Dynamic effects**	
	Indicators	**Differences between foreign and local firms**	**Impact processes**	**Indicators**
Employment and income	Employment generation inside foreign firms Wage levels for staff with given characteristics	Foreign firms are larger and pay higher wages (especially for skilled employees) than local firms	Provides employment and incomes directly. Also indirectly through procuring from local firms, which can grow as a result. Wage labour may induce spending and further effects. May also indirectly crowd out other employment by replacing existing employment or pushing up factor prices; may lead to increased wage inequality by raising relative demand for skills	Long-run employment generation in firm and in suppliers and buyers Long-run wage development in foreign firms and spillover effects on wage levels in other firms
Physical capital	Fixed capital formation Financial transfers	Foreign firms tend to be more capital-intensive	Stable source of external finance, improving the Balance of Payments and potentially raising fixed capital formation May crowd out and compete with investment and opportunities of domestic firms Financial sector deepening raises availability and lowers cost of finance	Long-run relationship between FDI and domestic capital formation
Market access and exports	Share of inputs imported Share of output exported	Foreign firms tend to be more trade-intensive	Firms can gain access to export markets by using global networks of foreign firms Foreign firms can maintain tight controls of export channels	Long-run relationship between exports and FDI, and between imports and FDI
Structure of factor and product markets	Concentration in product and factor markets Profit margins	Foreign firms can often be found in sectors with 'barriers to entry'	Entry by foreign firm may lead to more competition. This may reduce product prices by offering consumers more choice The entry of foreign firms may also lead to further concentration and market power. This may raise prices of own and other products	Long-run relationship between FDI and profitability
Technology, skills and management techniques	Skill level of employees Training budgets Output per employee Research and development budgets Types of technologies	Foreign firms are more skills-intensive, and tend to use more up-to-date technologies and train more	Provides up-to-date techniques, skilled personnel and advanced management techniques, raising the return to skills offering additional incentives for education. Positive spillover effects on domestic firms through backward and forward linkages, learning, demonstration effects and human resource development. Spillovers are not automatic or free. Reliance on foreign technology and skills may inhibit development of local capabilities. Increased linkages raise dependency of domestic firms on foreign firms	Vertical (intra-sectoral) and horizontal (extra-sectoral) spillover effects on local productivity; share of inputs sourced locally Supplier development Upgrading and long-run development of technology, training

Impact area	Static effects		Dynamic effects	
	Indicators	**Differences between foreign and local firms**	**Impact processes**	**Indicators**
	used			and skill levels in foreign and local firms
Fiscal revenues	Fiscal payments Grants to foreign firms	Tax holidays or outright grants are sometimes offered to foreign firms	Foreign firms can raise fiscal revenues for domestic government through payment of taxes in case of new economic activities with more value-added. If foreign firms crowd out domestic firms, fiscal revenues may be lower through use of special tax concessions, leading to an erosion of the tax base. Special tax concessions are an implicit subsidy, which may lead to rent-seeking behaviour	Long-run fiscal payments through foreign firms and through a change in economic activity more generally
Political economy	Agreed deals between state and business	More competition for foreign firms State–business relations	Foreign firms can expose host country to other norms and values, e.g. environmental management, corporate governance, ethics, but foreign firms may lead to political, social and cultural problems, by imposing unacceptable values interfering with political regime, and are said to exacerbate existing problems of corruption. Deals between firms and government may have governance benefits	

Source: te Velde (2019)

4 Intra- and extra-African investment – what difference does the investor's home country make?

Stephen Gelb

The AfCFTA is concerned with promoting facilitating and regulating intra-African investment to support Africa's transformation and sustainable development, as expressed in Agenda 2063. Foreign direct investment (FDI) can support sustainable development through three channels, though it is of course not inevitable that FDI has a net positive impact on development. On the demand side of the economy, FDI may boost total savings and foreign exchange reserves in the short run, as well as fixed investment and employment if it is 'greenfield'. Perhaps more important for long-run development is the potential supply-side contribution to technology and capabilities, or productive knowledge. FDI may also have positive impacts on sustainable development through a third channel, by raising standards in environmental, social (including labour and gender) and governance practices.

4.1 Intra-African investment – how much is there?

The AfCFTA's focus on investment facilitation promises to boost intra-African investment over the long run. But at present, a very large share of inward FDI into Africa comes from outside the continent, and a similarly large proportion of outward FDI from Africa is outside the continent, so the AfCFTA's direct remit will be quite limited in the medium term, insofar as investment is concerned.

It is very difficult to be precise about the extent of intra-African investment, but a rough estimate is possible by examining the International Monetary Fund's (IMF's) Coordinated Direct Investment Survey (CDIS) database on bilateral investment, in conjunction with the United Nations Conference on Trade and Development's (UNCTAD's) country data on total inward and outward FDI.[2] The CDIS to date includes only 24 African countries, but in UNCTAD's database, which covers all African countries, these 24 contribute 85.8% of Africa's total outward investment stock (as well as 58.7% of Africa's total inward investment stock). South Africa alone provides 74.8% of outward FDI from Africa, according to UNCTAD, with Morocco and Algeria – also in CDIS – contributing a further 2.7%. On the inward side, these countries plus Nigeria receive 36.7% of inward FDI to Africa from the rest of the world, according to UNCTAD. Significant African outward investors that do not participate in CDIS are Liberia, Egypt, Libya, Democratic Republic of Congo and Angola, plus Nigeria for outward investment. Together, these countries account for 17.8% of Africa's outward FDI stock in the UNCTAD data.

[2] UNCTAD provides bilateral country data for most countries but only up to 2012, and data appear to be incomplete for most African countries.

The inter-regional investment totals indicate that the 24 African countries included in the CDIS had total outward FDI stock of $551.4 billion at end-2018, of which only $84.7 billion (15.4%) was invested in Africa, mostly from South Africa ($35.4 billion, or 41.8%) and Mauritius ($36.97 billion, or 43.6%). If we exclude Mauritius as a special case (discussed below), this falls to $47.75 billion (8.67%). Of South Africa's total outward FDI stock, 14.4% was into the rest of Africa, though this falls to 6.1% if Mauritius is excluded.[3] Excluding Mauritius entirely, Africa's share of total inward FDI into Africa probably ranges from 3.06% to 6.05%. The lower and upper bounds assume that 16.5% and 50%, respectively, of African outward FDI (aside from South Africa) goes elsewhere in Africa. The lower assumption is based on the CDIS average of 8.67%, whereas the higher assumption of 50% is the share of Morocco's outward FDI going into Africa.

Mauritius is a special case, illustrating an important point – the investing country is not always the investor's *de facto* home country. The bulk of Mauritius' inward and outward FDI stocks is non-Mauritian investment routed through Mauritius to third countries.[4] Meanwhile, according to the CDIS, Mauritius has very large inward and outward investment stocks, larger than South Africa's, though only about 5% of Mauritian inward stock is from Africa, and 8–9% of Mauritian outward investment stock is in Africa. By contrast, UNCTAD reports Mauritius stocks as very small, of the same order as those of Botswana. The difference between the two is that the UNCTAD data report only FDI stocks relating to Mauritian residents, whereas the CDIS data include the Global Business Licence Holders category. Mauritian authorities use this category to classify non-residents investing in Mauritius in order to do business outside Mauritius. Such third-country routing is common as investors seek to take advantage of double taxation treaties and/or protection from favourable international investment agreements.

But, though small in volume, direct investments from African countries into Africa do comprise a broad network: for example, South Africa and Nigeria both have investments in more than 20 other African countries, whereas Togo has direct investment assets in more than 30 other African countries.[5]

Also worthy of mention is that foreign investment may not be registered as such in official data, because local citizens are used to 'front' the investment to avoid host country restrictions or because funds are brought in through informal financial channels. Evidently, this is largely applicable to small operations, and, even included in the official data, is unlikely to increase the aggregate value of investment significantly. But this unofficial FDI – which is more likely to come from other developing economies in Africa and elsewhere – may be important in terms of the *numbers* of firms engaged in intra-African investment.

4.2 South–South versus North–South investment

However, with only 3–6% of African inward investment coming from Africa itself, it is clearly important to consider non-African investment as well. We can distinguish between 'North–South' (N–S) investment and 'South–South' (S–S) investment – that is, investment by a developed in a developing economy versus investment by one developing economy in another. Intra-African investment is part of the latter category, together with investment from China, India, other Asian countries such as Malaysia and Indonesia, Brazil and Turkey, as arguably also from Hong Kong and Singapore.

The significance of the distinction between North and South home (sending) countries[6] lies both in the willingness of foreign investors to enter host (receiving) countries in the South and in their impact once they have invested (see UNCTAD, 2006; also Gelb, 2005). All foreign investors face challenges when entering a new market, owing to their lack of familiarity with the market, its operating

[3] Based on South African Reserve Bank data: www.resbank.co.za
[4] See Bank of Mauritius, International investment position: external assets and liabilities at end-December 2018:, https://www.bom.mu/sites/default/files/iip_2018_provisional.pdf
[5] The investments from Togo are probably Ecobank operations.
[6] The home or sending country is taken here to mean the *de facto* home country from which the investor originates, not a third country through which investment is routed for tax or treaty protection reasons.

environment and business practices, as well as their lack of networks. Investors use various strategies to address this 'liability of foreignness', such as first exporting to the market to build their understanding of it. But the liability of foreignness may be smaller for investors from South economies compared with those from North economies, because South investors are likely to be more familiar with challenges in the host operating environment – regulations, infrastructure, skills availability, access to finance – which may be similar to those in their home country. As a result, South investors may be less risk averse than North investors when considering entry to other South economies, and so may enter in larger numbers.

The development impact of FDI in South economies may also differ between investors from South and from North home economies. The former may produce goods or services whose quality or sales price are more appropriate for South customers – firms buying equipment and production inputs, households buying consumer goods. South investors may also catalyse more significant inflows of productive knowledge to, and capability development in, domestic firms in South economies than will North investors, because the technological 'gap' is smaller between the foreign investor and domestic firms, an important consideration given the limited absorptive capacity for technology in South economies. Both forward and backward linkages may be more effective as mechanisms for knowledge transfer and productivity upgrading by domestic firms, while 'horizontal' spillovers in the same market as a result of increased competition may be more likely to lead to productivity improvements in domestic firms than to contraction or closure.

'Unofficial' FDI may have significant welfare impacts in African economies by expanding the scope or lowering the price of consumer goods or services, or by providing a boost to efficiency through effective competitive pressure on domestic firms.

Investors' risk perceptions, and their consequent willingness to enter, as well as the impact of their investments post-entry, will depend not only on the whether their home country is a developing economy or not but also on the industrial sector in which their investment is located, and, related to this, whether their motive for investment is market- or resource-seeking.[7] Market-seeking South investments are of course more likely to expand the scope of goods available to consumers and firms in the host economy, and to lower their cost, while also potentially leveraging greater productive knowledge gains through backward and forward linkages. Resource-seeking investments – motivated by natural resources, such as mineral deposits, agricultural land or tourist attractions, or by labour resources, including low-wage labour – may offer larger gains in employment and exports, but may also impose greater costs on the host country in terms of environmental and social standards.

Focusing on *sustainable* FDI by taking account of these standards underlines two important points. First, development impacts include both benefits and costs, and whether the net impact is positive may depend significantly on host country investment facilitation policies. Second, the *a priori* assumption would be that South FDI will have lower environmental and social standards than North FDI, so that, in these significant arenas, the development impact of South FDI may be less beneficial to South hosts.

However, it is important to remind ourselves that North investors only raised their standards on environment and social issues relatively recently, and largely as a result of regulatory demands by home country governments. The question therefore is whether South governments are able to similarly raise their standards. The recent shift of emphasis in investment regulation from investor protection to investment facilitation for sustainable development – see contribution by Brooke Güven (Section 9) – will improve the prospects for higher standards through joint action by governments, in multilateral, regional, plurilateral and bilateral contexts. Collaborative action to raise standards by Southern states may be both more likely (as a result of peer pressure) and more effectual than action by Southern states acting alone.

[7] Other commonly mentioned motives for FDI are efficiency-seeking and strategic asset-seeking, but these are perhaps less frequent reasons for FDI in African economies.

Environmental and social standards are being raised in many activities in South countries as a result of intervention by North investors as part of their 'lead firm' role in global value chains (GVCs). In many contexts, GVCs combine South–South and North–South FDI as complements, rather than posing them as alternatives, for example in the labour-intensive export-oriented clothing industries that have emerged in many African and South-East Asian countries in response to trade preferences in European and North American markets. Here, very small investments in South producer countries by large multinational brands and buying companies (largely from the North) are accompanied by FDI in manufacturing operations, often also relatively small in value terms, largely from the South.[8] In these GVCs, the brands and buyers have a crucial role not only in ensuring the raising of environmental and social standards but also in encouraging stronger backward linkages with local firms and support for enterprise development. Cooperation between foreign brands and buyers and the host government is essential but may be hampered by suboptimal political economy dynamics, mitigating the benefits of South–South FDI.

4.3 Intra-African investment and home economy considerations

It is important to consider intra-African investment also from the perspective of the home economy. Beyond China and perhaps India, the home country impact of outward FDI from the South has been little analysed.

An overriding concern of policy-makers in considering outward investment, whether from the North or from the South, has been whether it is a complement or substitute for domestic investment, with contrasting effects on domestic output and employment. But it is important to emphasise that the potential impact of FDI, through both the productive knowledge and the sustainability channels, may be positive not just for the host country but also for the home country. Firm internationalisation – operating across borders in multiple country markets with different regulatory and operating environments – may improve a firm's overall business capabilities, with 'reverse spillovers' increasing its own efficiency in its home market and that of its competitors. Efficiency gains from economies of scale and scope may also result from internationalisation, while regulatory and market pressures in a firm's foreign markets may lead to improvement of its sustainability practices not only in those markets but also in its home market.

The capacity to operate internationally itself needs to be learned. In Europe and Asia, most firms initially developed this capability through small investments into their own region. By encouraging intra-African FDI, the AfCFTA offers some promise of a much-needed boost to the capabilities of African firms.

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[8] Most FDI in these manufacturing activities is from Asia and Africa, though some is European.

5 Architecture of bilateral investment treaties

Thierry Mutombo

5.1 The universe of international investment agreements

The United Nations Conference on Trade and Development (UNCTAD) has recorded 3,317 international investment agreements (IIAs) at the end 2018, out of which 2,932 are bilateral investment treaties (BITs) and 385 treaties/agreements with investment provisions (TIPs).

A BIT is an agreement establishing the terms and conditions for private investment by nationals and companies of one state in another state. This type of investment is called foreign direct investment (FDI).

At the regional level, investment provisions can be contained in a dedicated framework or in an annex, protocol or a chapter of a comprehensive legal framework like a Free Trade Agreement. For Africa, its Investment Protocol, the AfCFTA, will be one of the mega-regional trade agreements, alongside the Transatlantic Trade and Investment Partnership, the Trans-Pacific Partnership agreement and the Canada–EU Comprehensive Economic and Trade Agreement.

5.2 Older-generation IIA architecture and concerns

Most older-generation IIAs grant investments made by an investor of one contracting state in the territory of the other a number of guarantees, which typically include substantive standards for FDI protection. For some, they even include 'full protection and security', free transfer of means and an alternative dispute resolution mechanism, whereby an investor whose rights under the BIT have been violated could have recourse to international arbitration, often under the auspices of the International Center for the Settlement of Investment Disputes. Capital-exporting states usually negotiate BITs on the basis of their own 'model' texts, aiming to protect and facilitate their nationals and companies.

Since 1996, the year in which the highest number of signed IIAs – more than 230 – was recorded, a permanent decline in the number of IIAs has been noticed. This owes to the number of terminations, which continues to rise: in 2018, at least 24 terminations entered into effect ('effective terminations'), of which 20 were unilateral and 4 were replacements (through the entry into force of a newer treaty). This prompted IIA reform and investment policies at country level. In this context, it is observed that the architecture in the newly concluded IIAs has changed, mainly in response to the challenges facing developing countries, mostly as a result of limited regulatory space, investment disputes resulting from investors' claims and the need to reflect the Sustainable Development Goals in the IIAs.

Typically, there are five common and interconnected concerns across different treaty reform narratives, raised by host states, international organisations and other stakeholders:

- extensive substance on investment and investor protection
- too little policy flexibility
- wide-ranging definitions of investment and investor
- language perceived as lacking in precision and
- investor–state dispute settlement (ISDS) clauses affording high levels of discretion or legal delegation to arbitrators.

5.3 Modern architecture of IIAs

The architecture of the new generation of IIAs is diverse and is based on guiding principles set out in UNCTAD's Investment Policy Framework for Sustainable Development (WIR12, updated in 2015), or follows UNCTAD's Road Map for IIA Reform as included in UNCTAD's Reform Package for the International Investment Regime. It is also informed by analytic work and advocacy conducted by the International Institute for Sustainable Development (IISD) and others international institutions. The following approaches have been identified to guide the modern architecture of BITs:

Approaches in designing key provisions	Key provision focus
Treaty coverage	✓ investment and investor protection ✓ investment promotion and facilitation ✓ pre-establishment and admission ✓ investment liberalisation ✓ provision scope (definitions of investment and investor, exclusions for policy areas or economic sectors) ✓ Fair and Equitable Treatment (FET) – customary international law, specific state obligations, no FET
Inclusion of sustainable development-oriented provisions	✓ flag overall importance of sustainable development (e.g. preamble, clause on objectives) ✓ preserve policy flexibility (e.g. exceptions for health, environment, social policies) ✓ guide government behaviour and investor expectations (e.g. clauses on not lowering standards, corporate social responsibility, impact assessments) ✓ support local small and medium-sized enterprises in supply chains, as well as protecting national security ✓ supporting and protecting critical local industries ✓ public health through foreign investment screening
Balance between investor protections and investor obligations	✓ comply with host state domestic laws and regulations ✓ abstain from corruption ✓ uphold labour rights ✓ undertake impact assessments ✓ meet corporate social responsibilitystandards ✓ encourage responsible investment ✓ uphold human rights and core labour standards
Clarification of the scope and meaning of standards of treatment of investment and investors' clauses	✓ coverage (investor or investment) to be protected ✓ indirect expropriation, national and most-favoured nation treatment, ✓ full protection and security, free transfers
Right for the host state to regulate	✓ exceptions (e.g. for general public policy objectives, national security, prudential measures) ✓ exclusions (e.g. from treaty scope, specific obligations, ISDS)
Balance between powers of arbitrators and those of state parties	✓ jointly determine certain issues under consideration by a tribunal ✓ issue joint interpretations binding on tribunals awards ✓ preview and comment on draft arbitral awards ✓ launch counterclaims
Different approaches to investment dispute settlement	✓ no ISDS ✓ standing ISDS tribunal ✓ limited ISDS ✓ improved ISDS procedures
Plans for adjustments over time of the treaty	✓ programmes for future work or negotiations ✓ periodic reviews of the treaty

5.4 Multilateral investment agreements

The current global economic architecture is characterised by the absence of a multilateral agreement on FDI. A multilateral investment agreement (MIA) was discussed extensively from 1970 to 1998 but never concluded.

However, the need for such an agreement has increased in the past decade. FDI has grown substantially and now flows in both directions, between developed and developing countries, with multinational corporations (MNCs) hailing from all parts of the world. The numerous BITs warrant an international standardised set of rules for FDI. With investment now clearly identified with MNCs and integrated with trade, the World Trade Organization has emerged as a natural home for an MIA. Discussions are being held at this specialised UN institution.

5.5 AfCFTA Investment Protocol and BITs among African Union Member States

The AfCFTA Investment Protocol is a continental set of provisions meant to regulate the investment relationship within the AU Member States. The rationale is that there will not be a need for these Member States to conclude among themselves new BITs; and once those in force come to an end, they are supposed not to renew them.

The investment relationship between African Member States and third parties can continue to be guided by existing or new BITs unless they comply with the key standards set in the AfCFTA Investment Protocol.

6 An overview of PAIC in relation to the AfCFTA Investment Protocol

Jamie MacLeod

6.1 Background to the PAIC and the AfCFTA Investment Protocol

The third Conference of African Ministers in Charge of Integration (COMAI III, Abidjan, 2008) mandated the AU and its development partners (including the United Nations Economic Commission for Africa, ECA) to 'develop a comprehensive investment Code for Africa with a view of promoting private sector participation'.

The Specialised Technical Committee on Finance, Monetary Affairs, Economic Planning and Integration (October 2017, Addis Ababa) adopted the Pan-African Investment Code (PAIC) as a 'non-binding instrument'.

In July 2018, the AUC, along with ECA, the United Nations Conference on Trade and Development (UNCTAD) and the African Development Bank (AfDB) commenced research on the 10th edition of the Assessing Regional Integration in Africa (ARIA) flagship report, which would consider the Phase II topics of the AfCFTA and contribute to providing a situational analysis of investment in Africa. The ARIA IX report, including its chapter on an AfCFTA Investment Protocol, was published in July 2019.

Negotiations on the Investment Protocol are scheduled to start in 2020 for conclusion by mid-2021, though the coronavirus outbreak could disrupt this envisaged schedule.

6.2 Context to an Investment Protocol: rebalancing of the investment regime

Traditionally, international investment agreements have been oriented around investment protection. Investment protection obligations are intended to lessen political risks arising from policy changes with detrimental effects for investors, including nationalisation or conduct of the state authorities. Investor protection obligations provided international investors with an additional layer of investor protection standing above national law (Salacuse and Sullivan, 2005; Sprenger and Boesma, 2014).

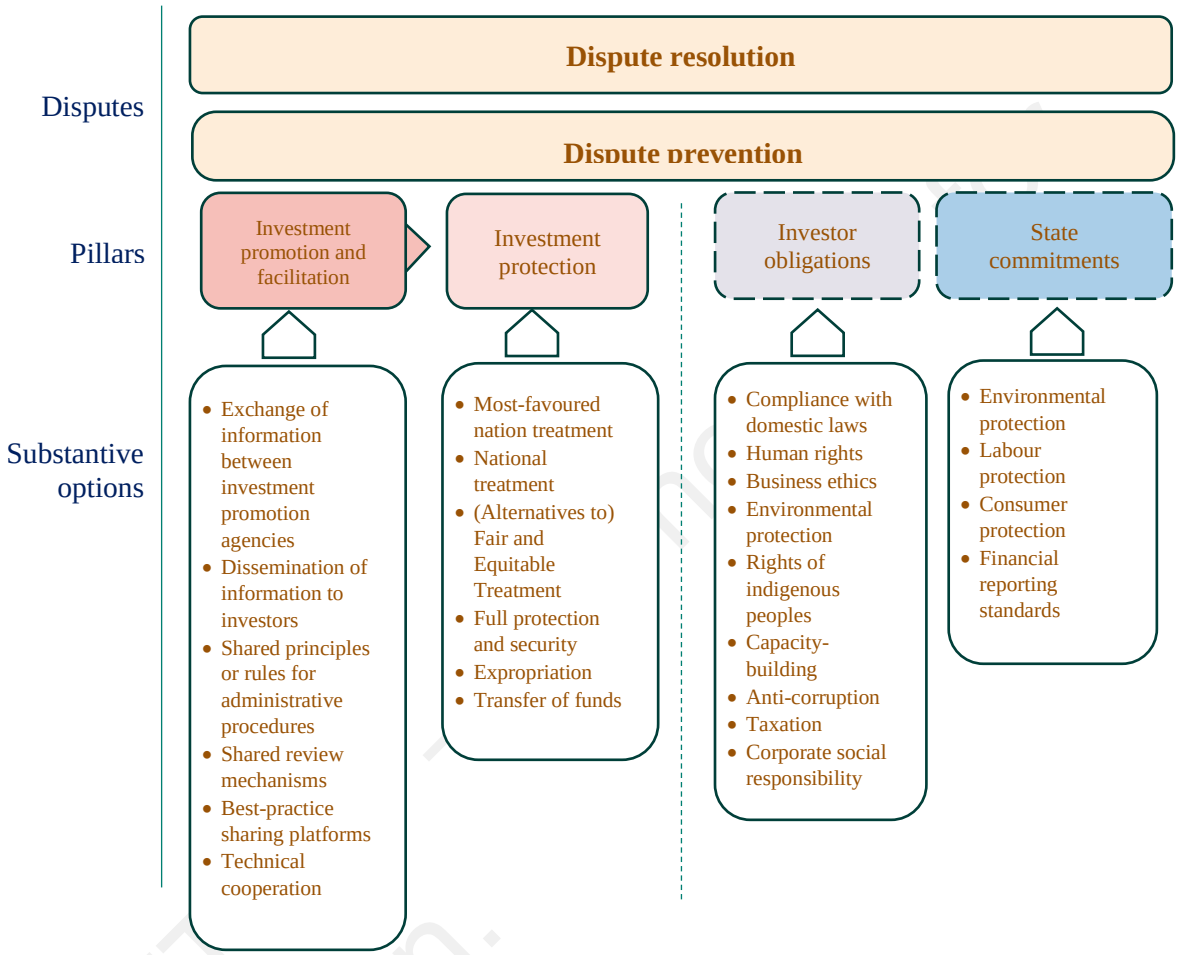
However, traditional international investment agreements faced a backlash, particularly because of their impact with regard to limiting policy space, which was compounded by uncertainty and inconsistency. Since then, more recently designed investment agreements have looked to provide more balance. These include the agreements of the Southern African Development Community (SADC), the Common Market for Eastern and Southern Africa (COMESA) and UNCTAD's Reform Package; the revised domestic investment treaty laws of South Africa, Ecuador and Indonesia; and the formulated model treaties of Brazil, Nigeria, India and the Netherlands, as well as the replacement of investor–state dispute settlement (ISDS) with a standing court (promoted by the EU).

The new approaches being included in investment regimes have included:

- protection of policy and administrative space, transparency and misuse and abuse of treaties
- A growing focus on investment promotion and facilitation (though the second term is somewhat amorphous) in recent years

- investor obligations, which have to be met for investors to be accorded the benefits of protection and
- state commitments, to reduce 'race-to-the-bottom' regulatory issues on topics such as taxation or labour rights.

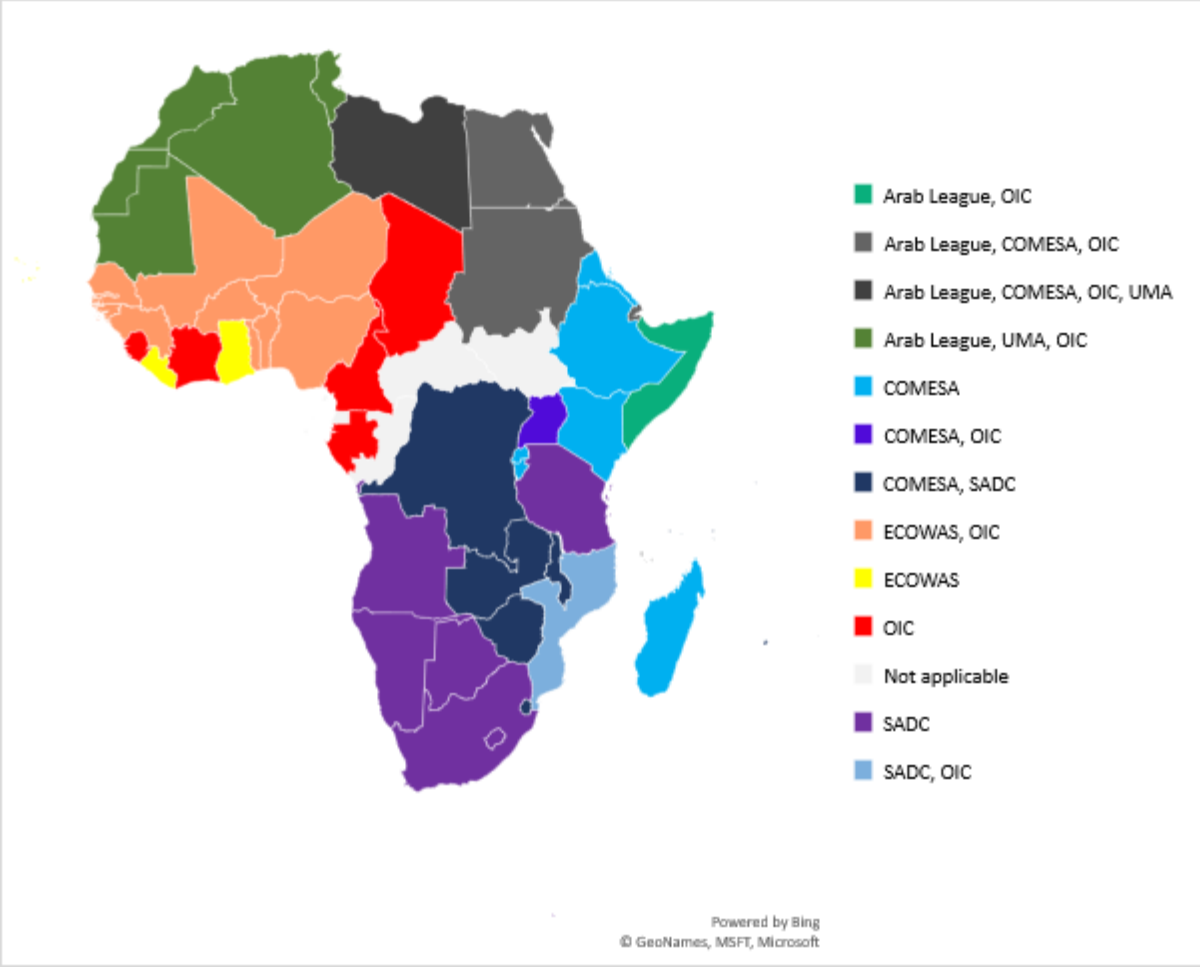
Figure 6.1: Schematic overview of AfCFTA Investment Protocol options



Sources: ECA et al. (2019)

A second important development in investment agreements in Africa has been the proliferation of often overlapping bilateral and regional treaties, between Member States and with external partners. Some countries are increasing their number of treaties with African partners and these treaties do not always include all the necessary safeguards.

Figure 6.2: Membership of African countries of regional investment agreement



Source: UNCTAD Investment Policy Hub

The Investment Protocol needs to sufficiently address these issues. It also offers Africa an opportunity to articulate and put forward an alternative vision of the investment regime and guide future negotiations (ECA et al., 2019).

6.3 PAIC: a model for rebalancing the investment regime in Africa

The PAIC was widely celebrated for its innovations and novel approaches to topics within international investment agreements (Chidede, 2019). In particular, sustainable development considerations take centre stage, including in the preamble, objectives, scope and substantive provisions (Mbengue and Schacherer, 2017). Investment is clearly articulated as a means to a sustainable development end, rather than a goal in itself.

Substantively, the PAIC integrates and puts emphasis on investor obligations related to human rights, child labour, environmental protection, respect for domestic laws and corruption and corporate social responsibility, among others. The PAIC also contains provisions on investment promotion and facilitation (Mbengue, 2018).

The PAIC critically reappraises traditional investment protection rules. For instance, a Fair and Equitable Treatment provision was dropped. The most-favoured nation (MFN) provision was redesigned to prevent treaty shopping. Together with national treatment, it was anchored on ‘like circumstances’ and included a list of exceptions. In doing so, the PAIC was constructed to protect policy space for African governments to continue to regulate and innovate in the investment policy sphere.

The PAIC was an ambitious undertaking, spanning a large number of investment-related issues, including intellectual property rights, competition, transfer of technology and taxation.

6.4 From the PAIC to the Investment Protocol

The PAIC was adopted as a non-binding 'code' to help inform the design of future African investment agreements. Several steps are required to transpose and review the ideas of the PAIC for an AfCFTA Investment Protocol.

Alignment with AfCFTA architecture

The Investment Protocol needs to be aligned with the overall AfCFTA architecture on both legal and institutional dimensions.

A key issue here is the relationship between the Investment Protocol and the Phase I and Phase II Protocols, such as in investment disputes bordering trade, competition or intellectual property. These issues always need to be present (e.g. definition of assets, potentially problematic reference to the Agreement on Trade-Related Aspects of Intellectual Property Rights and exceptions thereto when taking the Investment Protocol into account).

Development of provisions within the PAIC

Several areas of investment treaty-making have developed in recent years, and this could lead to review and potential updating. These include investment promotion and facilitation, which could be strengthened to drive integration (but preferably remain separate from investment protection to not create additional obligations of host states *vis-à-vis* foreign investors).

Choices about the operative part of the treaty need to be conscientious, as these will shape the way of the future path of regional integration. For instance, sustainable development and policy space need to remain fundamental to a new predictable, clear and forward-looking investment environment. Concerns also need to be addressed with regard to putting African companies at a relative disadvantage under stronger protections for, for instance, European or Asian companies under parallel investment agreements (Kidane, 2017–2018) and at risk of treaty-shopping.

Substantive provisions on investment protection, drawing on best practices on the continent (or inspired by approaches beyond) include:

- investment and excluded assets need to be defined
- MFN and national treatment are well developed in the PAIC but could nevertheless be reviewed
- Fair and Equitable Treatment can be left out (such as is the approach in the PAIC) or an African alternative advanced (such as in SADC) could be proposed
- full protection and security could be circumscribed to physical security
- right to regulate to could limited or expanded
- prevention of race-to-the-bottom provisions could be powerful in a pan-African context.

Technical and administrative provisions

Decisions must be made over how the Investment Protocol will be administered. Key decisions here are related to:

- the operationalisation of investor obligations through claims and counterclaims (i.e. procedure, technical, institutional – see e.g. Amado et al., 2017; Krajewski, 2020)
- methods for dispute prevention (part of investment facilitation)
- choice of dispute settlement provisions, as these embody the underlying relationship with investment and investors.

In particular, the PAIC allows countries to offer ISDS 'subject to the applicable laws of the host State and/or the mutual agreement of the disputing parties' (a 'middle ground solution to African states that

are either pro-ISDS or anti-ISDS') (Kane, 2018). Such an approach could be reviewed in the AfCFTA, with other options including a Pan-African Investment Court or a hybrid court–ISDS. Care must also be taken over alignment with the existing (state-to-state) dispute settlement mechanisms in the AfCFTA Protocol on the Settlement of Disputes, which was not designed with investors and investment issues in mind.

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7 Investor–state dispute settlement

Sarah Brewin

Most international investment treaties allow foreign investors to enforce the rights owed to them by states under those treaties with investor–state dispute settlement (ISDS). The term ISDS refers to the settlement of treaty-based disputes through arbitration where (i) the claimant-investor may bring a claim directly against a host state; (ii) the dispute is resolved by a tribunal set up on an *ad hoc* basis for the dispute; and (iii) both disputing parties, including the claimant-investor and the respondent-state, play an important role in selecting the arbitral tribunal. The issues set out below are those raised by states for consideration by the United Nations Commission on International Trade Law (UNCITRAL) Working Group III on Investment Reform.

This note first sets out some of the widely acknowledged concerns and issues with ISDS under international investment agreements and then looks at modern approaches to ISDS.

7.1 Concerns related to investor–state dispute settlement

UNCITRAL Working Group III is considering three sets of concerns.

1. **Concerns about the lack of consistency, coherence, predictability and correctness of arbitral decisions by ISDS tribunals**
   - Because there is no system of binding precedent in ISDS, arbitrators interpret substantive standards (like the level of protection states owe investors) in **conflicting, inconsistent and unpredictable** ways. The same is true for procedural and jurisdictional issues (a tribunal deciding whether or not it has the competence to hear a case).
   - States can face multiple proceedings brought by different investors challenging the same measure, or multiple proceedings brought by the same investor in different forums. But there is **no framework to address multiple proceedings**, worsening the issues of inconsistent outcomes and increased costs for states.
   - States have **limited opportunity to challenge or appeal** incorrect or inconsistent decisions, except the current annulment procedures, which are very narrow in scope.
2. **Concerns about arbitrators and decision-makers**
   - Because parties appoint and pay their own arbitrators, they are more likely to appoint arbitrators whom they know and whom they expect to be most sympathetic to their case, and who are **not necessarily the most impartial, competent and well qualified.**
   - There is **little diversity** in terms of gender, ethnicity, geography, language, age and legal tradition in the small pool of people who tend to be appointed as arbitrators. This is concerning for the representation of different opinions and perspectives and can **increase the cost and length of proceedings** where individual arbitrators have busy schedules and large caseloads.
   - The issue of 'double-hatting' raises concerns **that arbitrators may not be impartial or may have prejudged the issues in a case**. Double-hatting refers to one individual being able to play multiple different roles within the ISDS process at the same time, such as being arbitrator, counsel, expert witness and adviser to a third-party funder.
   - There is no **consistent, clear and universal set of standards** for arbitrators' independence and impartiality, to guide issues like double-hatting.

- There is a **limited and inefficient challenge mechanism** for states to dispute the appointment of an arbitrator because of issues of lack of independence and impartiality.

3. **Concerns about the cost and duration of ISDS cases**
   - ISDS proceedings tend to be **lengthy and expensive**. The average estimated cost to defend a claim is $8 million, but it sometimes greatly exceeds that. For example, the Philippines spent $58 million to defend two cases brought by a German investor, and Australia spent $39 million defending a case brought by tobacco company Philip Morris.
   - There is no **clear, consistent approach to the allocation of costs** by arbitral tribunals.
   - There is no mechanism for states to ask tribunals to **address or strike out frivolous or unmeritorious claims** at an early stage in the proceedings, which would help reduce costs.

In addition to the issues above, states and commentators have for many years voiced broader concerns about ISDS. These include concerns about ISDS:

- operating under conditions of strict confidentiality, preventing oversight and participation by other stakeholders
- displacing domestic adjudicatory decisions and domestic law and institutions
- operating against the interests of developing states
- creating conditions for 'regulatory chill'
- creating an exclusive category of dispute settlement for foreign investors
- permitting monetary awards of very large size to investors (in this respect, multibillion dollar awards are now not uncommon).

Others forms of disputes settlement are available and deserve consideration. Many of the concerns above are more fundamental and inherent to the concept of ISDS. They may not be easily addressed by the procedural safeguards set out in the next section of this note. They may instead require a broader reconsideration of the inclusion of ISDS in international investment agreements, especially in the context of a regional instrument such as the AfCFTA Investment Protocol. Other forms of dispute settlement include state–state arbitration, domestic or regional court-based options and dispute prevention mechanisms, explored further in the next section. Such options can be approached as alternative mechanisms to ISDS, or in combination with it.

Further reading

- UNCITRAL and reform of investment dispute settlement
- Phase 2 of the UNCITRAL ISDS review: why 'other matters' really matter
- International Centre for the Settlement of Investment Disputes rule amendment: an attempt to remedy some of the concerns regarding ISDS identified by UNCITRAL WG III

7.2 Modern approaches to investor–state dispute settlement

Modern investment treaty language includes safeguards and limitations on ISDS to try and address the issues and minimise the risks with ISDS set out in the previous section.

Requirements for submission of a dispute

Modern treaties set requirements or hurdles that claimant investors must clear before they can initiate an ISDS claim. For example, claimants must usually **to attempt to resolve the dispute amicably**[9] for a period (e.g. six months), and to **waive their right to pursue the claim in other ways.**[10] Claimants

[9] See, for instance, Art. 9(3) of the Cabo Verde–Hungary BIT (2019).
[10] See, for instance, Art. 16(6)(c) of the Morocco–Japan BIT (2020).

can also be required to **exhaust local remedies**[11] (i.e. submit their claim for resolution by the domestic courts or administrative processes), usually for a period of three years, before being allowed to resort to ISDS. Many new treaties also impose a **limitations period**[12] requiring the investor to bring their claim within a certain time from the alleged treaty breach (usually three years).

Newer treaties may also require **prior written consent of the disputing parties** to submit a dispute to arbitration.[13] This can help avoid a situation whereby arbitrators rule on important public interest laws and policies, or other delicate public policy issues that cannot be appropriately resolved through arbitration. Some treaties also **carve out certain measures** from the scope of ISDS, or specify a limited list of obligations to which ISDS can be applied.[14] Modern drafting may also contain provisions that **strengthen state–state processes in relation to ISDS**, particularly in sensitive or technical policy areas. This allow the parties, rather than arbitrators, to decide whether certain measures meet the test of the exceptions they intended to create.[15]

Finally, some new treaties **make access to ISDS conditional on the investor's behaviour.**[16] This means, for example, that an investor that has established its investment through corruption or fraud, or has committed serious human rights violations, environmental damage, grave labour law violations or similar, can be barred from using ISDS.

Procedural safeguards

Many modern treaties contain procedural safeguards to try and address the issues outlined in the previous note and mitigate the risks to states' interests posed by ISDS. Newer treaties may set standards for the **impartiality and independence of arbitrators**,[17] or refer to **codes of conduct**[18] for arbitrators. Some treaties address this issue by requiring the parties to establish a **roster of arbitrators**[19] who are selected ahead of time by the parties to the treaty, rather than being selected by the disputing parties when a case is initiated.

Modern treaty drafting is increasingly addressing concerns around **transparency and participation** of broader stakeholders in ISDS proceedings. Some treaties refer to the UNCITRAL Rules on Transparency in Investor–State Arbitration. The Southern African Development Community model bilateral investment treaty (BIT) and the Investment Agreement for the Common Market for Eastern and Southern Africa Common Investment Area have extensive provisions on transparency in investor–state arbitration proceedings. Modern treaties may also contain provisions expressly permitting submissions from an **amicus curiae**, or 'friend of the court'.[20] This is someone who is not a party and is not engaged by a party or the tribunal but who assists the tribunal by offering information that is relevant to the case.[21]

Many newer treaties now provide guidance to a tribunal in **the sources of applicable law**[22] it must consider when interpreting and applying the treaty. This prevents the tribunal from focusing only on the investor protection provisions of the treaty when deciding a matter, and will usually specify that

[11] See, for instance, the 2006 SADC Protocol on Finance and Investment, Annex 1, Art. 28, Para. 1. NB the current text no longer includes it as the treaty was amended to remove ISDS.
[12] See, for instance, Art. 13(1)(f) of the Rwanda–UAE BIT (2017).
[13] See, for instance, Art. 10. of the Mauritius–Egypt BIT (2014).
[14] Many older BITs signed by China limit ISDS to disputes involving the amount of compensation for expropriation. See, for instance, Art. 9.3 of the China–Syria BIT (1996).
[15] For example, 'Where an investor submits a claim to arbitration under this Article, and the disputing Contracting Party invokes (the general exception related to prudential measures), the investor-State tribunal… may not decide whether and to what extent (the general exception related to prudential measures) is a valid defence to the claim of the investor. It shall seek a report in writing from the Contracting Parties on this issue. The investor-State tribunal may not proceed pending receipt of such a report or of a decision of a State-State arbitral tribunal, should such a State-State arbitral tribunal be established' (Canada–China BIT, Art, 20.2(a)).
[16] See, for instance, Vietnam–EU FTA, Chapter 8, Section 3, Sub-section 1, Art. 1.
[17] See, for instance, Art.18 of the Rwanda–UAE BIT (2017).
[18] See, for instance, Annex II to the India–Brazil BIT (2020), which sets out a code of conduct for arbitrators.
[19] See, for instance, Art. 29.8 of the CETA.
[20] See, for instance, Art. 26(2) of the Hong Kong–Chile BIT (2016).
[21] See, for instance, Art. 8 of the COMESA CCIA, and in the SADC Model BIT Art. 29(15).
[22] See, for instance, Art. 27(2)(c) of the Morocco–Nigeria BIT (2016).

the **domestic law of the host state is the governing law**, along with general principles of international law. This type of provision can also require the tribunal to consider (and be bound by) any **joint interpretive statements**[23] regarding the interpretation of any part of the treaty. A joint interpretative statement can allow the state parties to agree to clarify or restrict how any part of the treaty is interpreted, as a 'safety valve' to stop unintended interpretations binding the parties. This can be simpler and more direct than amending the treaty.

It is becoming more common for states to face several treaty claims at the same time, all arising from the same measure and from similar investment treaty provisions. To address this, newer treaties contain provisions setting out how to **consolidate multiple claims into one process**.[24] This can greatly reduce the burden for the state in trying to defend multiple cases at the same time. It also reduces the risk of getting conflicting decisions on the same issue.[25]

To address concerns around the high costs to taxpayers of defending ISDS claims, modern treaties are starting to include provisions on **security for costs**.[26] An order for security for costs is when an investor is required to post a certain amount of money as security for the state's costs in defending the claim if the investor loses the case. It is a safeguard that can prevent a state from being significantly out of pocket for defending an unsuccessful case brought by an investor who later becomes insolvent or unable or unwilling to pay. This can also filter out claims that are speculative.

For similar reasons, the latest treaties also require disclosure of **third-party funding.**[27] Third-party funding, where a company that has a stake in the final award pays for an investor's cases, is now commonplace in ISDS. Many consider that third-party funding has the potential to alter the dynamics of ISDS; for instance, it may encourage investors to exit a country and seek a cash award through ISDS, rather than staying and trying to negotiate a mutually agreeable settlement. It may enable more weak or marginal cases to be brought and incentivise investors to seek larger claims.

Investors may bring a weak or marginal case simply to pressure a state into a financial settlement or into withdrawing a new law or measure ('regulatory chill'). Newer treaties address this by providing what is known as a **'strike out' process**[28] – an expedited procedure to dispose of unmeritorious claims at the preliminary stage of a proceeding.[29] This makes it possible to dismiss claims that 'manifestly lack legal merit' or that are 'unfounded as a matter of law'[30] early, before they needlessly consume state resources. To prevent 'mailbox' investors using shell companies to launch ISDS claims, many treaties include a '**denial of benefits**' clause that allows the host state to challenge the investor's use of the treaty's ISDS mechanism where it is not a genuine investor in its claimed home state.[31] To a similar end, some older treaties require an investor to be **approved or registered** ahead of time to be able to use ISDS under a treaty.[32]

Many newer treaties **limit the types of awards**[33] that tribunals can order. In the context of an investment dispute, the measure complained of may be a perfectly legitimate exercise of state sovereignty or public interest regulation. As such, modern treaty language provides that awards be limited to damages, and not extend to allowing the tribunal to order reversal of the measure. Finally, select recent treaties include explicit provisions on a possible **appellate mechanism**,[34] or intent to

[23] See, for instance, Art. 34 of the Canada–Burkina Faso BIT (2015).
[24] See, for instance, art.28 of the Canada–Guinea BIT (2015).
[25] For example, a consolidation provision in NAFTA was successfully used by the US to secure the consolidation of three separate investor-state arbitrations that had been initiated against the US by different Canadian forestry companies for the same type of measure.
[26] See, for instance, Art. 26(6) of the Iran–Slovakia BIT (2016).
[27] See, for instance, Art. 8.26 of CETA (2016).
[28] See, for instance, Art. 26(3) of the Hong Kong–Chile BIT (2016).
[29] See, for example, ICSID Arbitration Rule 41(5), and CETA Art. 8.32.
[30] Often referred to in common law jurisdictions as 'frivolous or vexatious' claims that are not brought in good faith.
[31] See, for instance, Art .22 of the Morocco–Nigeria BIT (2016).
[32] See, for instance, Art. 3 of the UK–Thailand BIT (1979).
[33] See, for instance, Art. 35(2) of the Canada–Guinea BIT (2015).
[34] See, for instance, EU–Vietnam FTA, Chapter 8, Section 3, Art. 13: 'A permanent Appeal Tribunal is hereby established to hear appeals from the awards issued by the Tribunal…'

negotiate an appellate mechanism.[35] An appellate mechanism could improve predictability and accountability, consistency and coherence in investor–state jurisprudence.

Counterclaims and investor obligations

Modern investment treaties, such as the Pan-African Investment Code or the Morocco–Nigeria BIT of 2016, try to balance the rights afforded to investors by states with obligations on investors, for instance to respect domestic laws and ensure their operations do not violate human rights or labour protections or damage the environment. Where investor obligations are present in a treaty, they can be made self-enforcing by being linked to the ISDS provisions contained in that treaty.

This can be done in two ways. A treaty can provide that, if a State Party to a dispute brought by an investor alleges that the investor is in breach of its investor obligations, the tribunal must take this into consideration as **a factor in mitigation**. This includes considering whether the investor's breach weakens its case or reduces the amount of damages to which it is entitled. The treaty can also allow the respondent state to make a **counterclaim** for an investor's breach of its obligations or of the domestic law.[36]

Dispute prevention, conciliation and mediation

States, investors and local communities all hope to have long-term and positive relationships. As such, modern treaties now create mechanisms to prevent minor conflicts from escalating to contentious proceedings that will likely damage the relationships among the stakeholders. This requires putting into place institutions (e.g. contact points, joint committees, ombudsmen) and processes. This can include:

- establishing effective **cooperation and information-sharing mechanisms** between state and non-state actors, as well as focal points, joint committees and other tools to foster dispute prevention.[37] This may prevent disputes from escalating and engaging the ISDS
- requiring **conciliation, mediation or other alternative dispute resolution** mechanism as a mandatory precondition to the more formal settlement of disputes, such as arbitration and adjudication[38]
- putting in place a **cooling-off period** between an initial notice of a dispute and initiation of a formal arbitration process. This allows more time for the parties to seek to settle amicably or through alternative dispute resolution mechanisms.[39]

State–state arbitration and domestic or regional court-based options

States can also consider other options for investment dispute settlement mechanisms. One option entails conferring investment dispute settlement to the national and regional courts, as the sole mechanism available. This is the approach currently taken by South Africa, for example. A regional or continental court-based system would lead to more consistent outcomes and interpretations, avoiding a situation whereby the interpretation of a provision differs based on who initiates the claim or who sits in the tribunal. Institutionalised options at regional or continental level may resolve many of the procedural and cost problems identified in the context of investor–state arbitration.

[35] 'If a separate, multilateral agreement enters into force between the Parties that establishes an appellate body for purposes of reviewing awards rendered by tribunals constituted pursuant to international trade or investment arrangements to hear investment disputes, the Parties shall strive to reach an agreement that would have such appellate body review awards rendered under [Dispute Settlement Provisions] in arbitrations commenced after the multilateral agreement enters into force between the Parties' (Peru–US FTA Art, 10.20.10).
[36] For example, 'When the claimant submits a claim pursuant to [Investment chapter provisions], the respondent may make a counterclaim in connection with the factual and legal basis of the claim or rely on a claim for the purpose of a set off against the claimant' (CPTPP Art. 9.18(2)).
[37] See, for, instance Art. 5 of the Brazil–Angola Agreement on Cooperation and Facilitation of Investment.
[38] See, for, instance, Art. 12(1) of the Egypt–Swiss BIT.
[39] See, for, instance, Art.8.3 of the Germany–UAE BIT.

Another option is providing only for state–state arbitration mechanisms, which allow countries to submit claims against another state on behalf of national investor. State–state mechanisms already exist in most investment treaties but usually as an option alongside ISDS.

Further reading

- Sustainability toolkit for trade negotiators (investment provisions)
- IISD's Best Practice series on Security for costs, Exhaustion of local remedies, State–state dispute settlement, Registration and approval requirements in investment treaties and Transparency in the dispute settlement process

8 Investment promotion and facilitation

Brooke Güven

8.1 What are investment promotion and investment facilitation?

Investment is a critical component of sustainable development. In particular, under the right conditions, foreign direct investment (FDI) can improve economic growth and living standards, create jobs, transfer technology and know-how and result in supply chain upgrading. However, its benefits are not automatic, and, if not carefully governed, investment can result in harm to the environment, labour standards and lead to tax evasion or other undesirable outcomes.

Investment promotion and investment facilitation, in turn, can help states attract, expand and retain FDI. These two concepts are mutually supportive but in practice entail very different activities: investment promotion is about promoting a country (or location within a country) as an investment destination, and investment facilitation means ensuring that investors do not face undue hurdles in establishing or expanding investments or in conducting their business, including opaque, confusing, or burdensome regulatory requirements; complicated or delayed administrative procedures; difficulties in understanding or assessing investment opportunities; corruption; or a lack of critical infrastructure or services.

Even though in many countries investment promotion agencies are tasked with both promoting and facilitating investment, the legal and policy frameworks required to effectively facilitate and retain investment require broader governance and government approaches.

Key takeaways:

- *Investment promotion is about promoting a country (or location within a country) as an investment destination.*
- *Investment facilitation is ensuring investors do not face undue hurdles in establishing or expanding investments or in conducting their business.*

8.2 What is investment facilitation for sustainable development?

Traditional concepts of investment facilitation, and even many of today's discussions of this topic (even those purporting to incorporate sustainable development objectives), tend to be investor-centric, focusing on speeding up approvals, removing hurdles or regulatory barriers and stabilising the legal and regulatory environment.

However, as the United Nations Conference for Trade and Development (UNCTAD) Global Action Menu for Investment Facilitation (2016) states:

> *[A]ny facilitation initiative cannot be considered in isolation from the broader investment for development agenda. Effective investment facilitation efforts should support the mobilization and channeling of investment towards sustainable development, including the build-up of productive capacities and critical infrastructure. It should be an integral part of the overall investment policy framework, aimed at maximizing the benefits of investment and minimizing negative side effects.*

Similarly, the Organisation for Economic Co-operation and Development (OECD), as reflected in its Policy Framework for Investment, conceptualises investment facilitation as a part of a broader policy

context in which governments should aim to support an enabling environment for investment, but one that enhances its development benefits to society (Novik and de Crombrugghe, 2018).

Thus, factors that are now recognised as critical to advance, alongside investor-oriented policies, are environmental protection, local economic and social development (including with respect to female entrepreneurship), industrial upgrading, employment and skills training, human rights, health, climate and other elements of national, regional, continental and international development plans and agendas.

Investment facilitation for sustainable development, then, may be understood as a combination of tools, policies and processes that foster a regulatory and administrative framework to facilitate investment that maximises and does not undermine sustainable development objectives. However, there is not sufficient empirical evidence or common agreement as to precisely what tools, policies and processes are necessary or desirable for countries to facilitate investment for sustainable development, and whether these tools are best implemented at the:

- national
- regional
- continental or
- international level

and whether by:

- the home state of the investor
- the host state of the investment
- the investor
- bilateral or multilateral networks (e.g. economic organisations or treaty-based networks) or
- international institutions (Novik and de Crombrugghe, 2018).

Key takeaways:

- *Investment facilitation for sustainable development is a combination of tools, policies and processes that foster a regulatory and administrative framework to facilitate investment that maximises and does not undermine sustainable development objectives.*
- *Each tool may be best implemented at the national, regional, continental or international level, and/or by the home state, host state, investor, bilateral or multilateral networks or international institutions.*

8.3 National, regional, continental or international governance and tools

Decisions as to how a country will admit, approve and govern investment are complex and require weighing (competing) costs and benefits in areas as wide-ranging as environment, health, labour, competition, tax and sector-specific considerations that may vary by industry (e.g. financial institutions, extractives, water and sanitation, health care, manufacturing, telecommunications, agriculture, etc.) and indeed by economy.

Regulatory issues relating to the accessibility and transparency of investment regulations and procedures, the administrative procedures applicable to an investment and the ways in which linkages with the broader economy can be facilitated are all focused at the national level. Similarly, AU governments have individually set forth development agendas and plans that can be significantly advanced through investment facilitation measures. Thus, national legal and regulatory frameworks are in many ways most directly relevant to advancing sustainable development outcomes (Brauch et al., 2019).

AU governments have also established regional and continental development objectives that incorporate investment facilitation measures. For example, the Southern African Development Community, the Common Market for Eastern and Southern Africa and other regional organisations

have model agreements and other initiatives to advance certain investment objectives to and within the region. Similarly, the Pan-African Investment Code represents a continental initiative to promote, facilitate and protect investments, including their processes and outcomes, to foster the sustainable development of member states. These established regional and continental platforms are also important for advancing agreed outcomes and facilitating investment for sustainable development purposes.

The role for investment facilitation is broader than just the policies of capital importing states, or among regions; the circumstances under which home states should be, and are, regulating, facilitating or subsidising (e.g. via political risk insurance, guarantees, investment treaty protection) outward investment vary by economy, but are also part of the larger question of how and under what circumstances capital is, and should be, moving from one economy into another.

Similarly, investor-focused norms relating to responsible business conduct and responsibilities to respect human rights are quickly evolving, placing more responsibility, and liability, on corporate actors to comply with these frameworks.

As such, there may also be an important role for supra-national-level cooperation that may help coordinate facilitation efforts, promote learning and address certain collective action challenges. (Novik and de Crombrugghe, 2018).

Key takeaway: *Many of the regulatory issues related to investment facilitation for sustainable development may be best implemented at the national level, but there may also be a role for regional, continental and international cooperation to address certain governance issues.*

8.4 Using international agreements to promote and facilitate sustainable investment

In a world of global value chains and mobile capital, countries face various collective action problems relating to investment facilitation for sustainable development. For example, many countries are competing for FDI, and regulatory races to the bottom, in terms of environmental, labour and social standards, can occur. From this perspective, 'investment facilitation' may mean excessively streamlining and expediting critical requirements, such as environmental, social or human rights impact assessments with the hope of easing FDI, despite evidence that these processes ultimately result in higher-quality and longer-term investments (Coleman et al., 2018). Crafting norms and platforms that will incorporate international cooperation on these issues may help balance the competing priorities of investment facilitation from a sustainable development perspective.

Similarly, bridging transnational governance gaps, in terms of drafting, monitoring and enforcing, laws regulating corporate conduct, can be difficult. Corporate structuring can result in eroding tax bases, externalised harms to societies and an inability for home or host economies to effectively obtain information about or regulate corporate conduct. International cooperation and information-sharing relating to corporate families and ways in which the investment chain can be effectively regulated for the social benefit of both home and host country could similarly be a useful basis for supra-national efforts.

Finally, platforms for information exchanges surrounding best practices and challenges may be underdeveloped. Investment promotion agencies and other government entities may wish to better understand and benefit from successful practices, or learn from challenges, of other countries, in establishing:

- tools to facilitate investments (one-stop shops, business registration systems, aftercare services)
- policies to improve investment (rules on transparency, anti-corruption practices, good governance mechanisms) and

- processes to make tools and policies useful (dialogues; interagency coordination; capacity-building) (Novik and de Crombrugghe, 2018; Brauch et al., 2019).

What will be important for governments to consider is, to the extent that regional, continental or international efforts on investment facilitation are advanced, the extent to which sustainable development objectives are achieved through more collaborative, 'soft' approaches, or though more commitment-based, 'hard' approaches. Examples of each are discussed below.

Key takeaways:

- *Solving collective action problems is necessary to facilitate investment for sustainable development, although at what level and with what tools this is best accomplished is complex and often unclear.*
- *Governments should consider whether 'soft', collaborative or 'hard', commitment-based approaches best solve these problems.*

8.5 The Brazilian model – using international investment agreements to promote investment cooperation and facilitation

In 2014 Brazil, a country that has never been a party to an investment agreement containing investor–state dispute settlement, proposed a new model of investment agreement – one that focused less on concepts of 'investor protection' and rather focused on attracting and retaining investment with a focus on 'cooperation and facilitation' (Brauch, 2020). Brazil has since concluded several cooperation and facilitation investment agreements (CFIAs).

The Brazilian model arose out of consultations with a wide variety of domestic stakeholders and foreign investors, trying to understand the ways in which investor attraction and retention could be better achieved, and how international agreements and cooperation could help facilitate these processes. As a result of these inquiries, Brazil's agreements now include contact points, and establish national ombudsperson offices as a focal point to manage concerns surrounding investment processes. Procedures are in place that facilitate visas and other procedural issues that are necessary for investment to occur. While Brazil had originally intended that the ombudsperson offices would be available only to investors from CFIA treaty partners, it has now opened these offices and the services that they offer to all foreign investors.

While relatively new, the Brazilian model represents a shift in thinking about international investment agreements, moving towards a focus on improved coordination and consultation with an aim of facilitating investment in the treaty parties. The aim is to prevent disputes, and, if and when disputes occur, and cannot be resolved by the contact point, ombudsperson or other mechanisms established by the treaty, to provide for state–state resolution of these issues, through dispute settlement if required, rather than granting to private companies the right to bring a claim against the host country.

Key takeaway: *Brazil's new model represents a shift in thinking about international investment agreements, moving towards a focus on improved coordination and consultation with an aim of facilitating investment into the treaty parties.*

8.6 World Trade Organization – structured discussions on investment facilitation

In December 2017, 70 World Trade Organization (WTO) Members issued a Joint Ministerial Statement on Investment Facilitation for Development calling for structured discussions with the aim of developing a multilateral framework on investment facilitation (which should not include market access, investment protection and investor–state dispute settlement). A total of 98 members are currently participating in discussions. These discussions have not yet resulted in agreement as to the

nature of the framework that should emerge, and whether it should include binding rules or focus to a greater extent on cooperation and softer obligations. Thus far, text has not been made public, although bracketed versions are significantly advanced and were intended to be progressed or finalised during the course of 2020 (Baliño et al., 2020).

While there is not yet agreement on what legal format or content the proposed framework would have, the current draft prepared contains a mix of binding and best-effort obligations, subject to capacity-building and special and differential treatment carve-outs for developing countries. Substantive areas included in the WTO discussions include non-discrimination and most-favoured nation treatment; transparency and predictability of investment measures; streamlining and speeding up administrative procedures; establishment of contact points; regulatory coordination and coherence; corporate social responsibility; and anti-corruption (Baliño et al., 2020).

Inclusion of investment facilitation within the WTO has been opposed by some countries not participating in the framework discussions, and other commentators for various reasons, including that WTO processes typically lead to binding disciplines, while investment facilitation measures may benefit from cooperative approaches and capacity-building, and that the WTO does not have a mandate to advance sustainable development approaches (Brauch, 2017; Mann and Brauch, 2018).

Key takeaway: *The WTO is addressing investment facilitation through an agreement, although the final framework, including whether or not it should include any binding obligations, is not yet agreed.*

8.7 Conclusion: how should governments approach these complex issues?

When considering how to approach the issue of investment facilitation, AU governments may wish to start with the following questions:

- What are national (and sub-national), regional, continental and international sustainable development objectives?
- What frameworks, national, regional, continental and international, are currently governing those objectives?
- What investment processes and outcomes are desirable to achieve those objectives?
- Are there regulatory or technical gaps that are putting up hurdles to desirable investment?
- Are those regulatory or technical gaps best addressed at national, regional, continental or international levels?
- What tools, policies and processes are best suited to address those gaps?
- Are such tools, policies and processes most effective as voluntary- or commitment-based measures, and what are the costs and benefits of each alternative?
- What type of assistance, if any, would AU governments need to implement these tools, policies and processes?
- What are the costs, benefits and potential consequences (intended or unintended, positive or negative) of taking these steps?

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9 Modern provisions in investment treaties

Brooke Güven

9.1 Why reform?

Governments are pursuing substantive and procedural reform of the international investment regime in recognition that there are fundamental, systemic and interrelated concerns about current approaches to investment governance,[40] and that current approaches have failed to meet their purported objectives.[41]

A vast majority of the 1,023 publicly known treaty-based claims have been brought under 'old-generation' treaties.[42] In 2018, for example, 60% of such claims were brought under treaties originally concluded in the 1990s or earlier, and all but one was filed under a pre-2011 treaty (UNCTAD, 2019). These old-generation agreements[43] include vague and far-reaching obligations for states, generally do not include any reference to investor responsibilities (even in non-binding terms) and rarely have provisions that seek to meaningfully preserve and protect the ability of states to regulate without having to pay compensation. Effective environmental, human rights, gender, health, labour and other public interest provisions are generally absent from these agreements.

Without provisions that effectively protect the ability of states to regulate, and meaningfully advance sustainable development objectives of states parties, respondent host states have been left exposed to costly investor–state dispute settlement (ISDS) proceedings and claims challenging public interest measures.[44] Investor claimants have also relied on investment treaties and ISDS provisions to make threats of claims in order to distort government measures or conduct in foreign investors' favour.[45] For example, in the context of COVID-19, law firms have already seized on the pandemic to advise multinationals on strategies for relying on investment treaties and ISDS to bring claims against governments on the basis of COVID-related measures.[46]

9.2 Options for approaching treaties

Beyond the specific substantive and procedural obligations enshrined in a treaty, some governments are carefully reconsidering the structure and form of agreements that govern international investment, and whether/ how to expand and contract different parts of these agreements in order to achieve the development objectives being pursued. States are stepping back and asking a series of questions, including:

[40] Governments are engaged in various processes to reform the system. These include multilateral reform efforts, including at UNCITRAL's Working Group III on ISDS Reform: https://uncitral.un.org/en/working_groups/3/investor-state

[41] For a discussion of the extent to which ISDS has not met its purported objectives, see Johnson et al. (2017). See also the following papers for discussions of the costs and benefits associated with investment treaties: Bonnitcha (2017); Pohl (2018); Johnson et al. (2018a); Borga et al. (2019).

[42] Known treaty-based ISDS cases per UNCTAD Navigator, updated as of 31 December 2019: https://investmentpolicy.unctad.org/investment-dispute-settlement

[43] UNCTAD (2017) refers to 'old-generation' treaties as those concluded before 2010, noting that these '[o]ld treaties "bite": as off end-2016, virtually all known investor-State dispute settlement (ISDS) cases were based on those treaties'. Phase 2 of UNCTAD's Road Map for IIA Reform proposes options for modernising these treaties. CCSI has also elaborated on some of these options (see Johnson et al., 2018b).

[44] Average awards are $120 million excluding outliers and $500 million including outliers (Behn and Daza, 2019). Proceedings cost on average $5 million per side, and tribunals often require respondent host states to pay their own fees even when the investor's claim is dismissed.

[45] On regulatory chill, see e.g. van Harten and Scott (2016); Kelsey (2017); Tienhaara (2018); Sachs et al. (2020).

[46] In light of the risk posed by ISDS to the ability of countries and the global community as a whole to confront the COVID-19 challenge, experts called (on 6 May 2020) for a moratorium on ISDS claims during the pandemic and a permanent restriction on ISDS claims for COVID-19-related measures: http://ccsi.columbia.edu/2020/05/05/isds-moratorium-during-covid-19/

1. What do we want from international investment? And what aspects/impacts of international investment do we want to avoid?
2. What are the policy tools available to help us get what we want?
3. What role can treaties usefully play, or play better, than other tools?
4. How can treaties be designed to help us achieve our aims?
5. How can treaties be designed to minimise our costs and risks?
6. What is the overall balance of costs and benefits struck by our 'model' approach, and how is that balance distributed (e.g. do foreign investors reap the benefits and domestic actors the costs?)
7. (How) can the state ensure the balance struck in the 'model' is secured in practice (i.e. in negotiations and resulting treaties)?

Questions 4, 5 and 6 go to the design of a 'model', while Question 7 relates to what a state will get in practice when negotiating based on that model. In each context, treaty designers can use a variety of different levers to shape the agreement – expanding or narrowing whom and what they are willing to protect, the scope of protections they are willing to provide and financial exposure they are willing to in turn assume (Coleman et al., 2018). These considerations require looking at the contents of provisions defining covered investors and covered investments; which substantive obligations are included and what they require of the state parties; whether there are exceptions to excuse breach; who can bring claims against whom; and what relief is available.

Key takeaway: *When identifying desired provisions, it is crucial to take a holistic view of the model (and any eventual treaties negotiated on the basis of a 'model' approach) and how its parts – substantive and procedural – work together.*

9.3 How are countries currently trying to address these provisions in modern treaties?

To address the cross-cutting issues flagged below, states are integrating provisions into models and treaties that affect who is protected, the scope of obligations benefiting investors (e.g. the scope of indirect expropriation), the scope of obligations towards treaty partners (e.g. in non-lowering of standards provisions), exceptions from breach, dispute settlement and investor obligations. This note does not focus on issues of scope of protections (e.g. definition of investor or investments) or the nature of investor protections (Fair and Equitable Treatment (FET), indirect expropriation, national treatment, most-favoured nation, etc.) *per se*, but looks at (i) how approaches to those obligations affect the issues of environmental protection, the realisation of human rights obligations, etc. and (ii) how certain treaty provisions have sought to specifically address the cross-cutting issues of environment, human rights, etc.

9.4 Cross-cutting issues

Environment

In newer-generation treaties and models, references to environmental obligations and protection of the ability to regulate can be found in the following types of provisions: preambles, reaffirmations of the sovereign right of states to regulate and commitments to non-lowering of environmental standards in order to attract investment. In some cases, they can also be found in provisions concerning investor responsibilities (to, e.g., conduct environmental impact assessments) and in general exception provisions. These references appear in newer treaties and models with varying frequency. The extent to which these provisions advance environmental objectives or effectively protect host state measures in practice remains unclear.

AU member states have been at the forefront of these innovations. The Southern African Development Community (SADC) Model, for example, requires that investors and their investments comply with

applicable environmental and social impact assessment processes.[47] The Morocco–Nigeria Bilateral Investment Treaty (BIT) contains a similar provision,[48] as does the draft Pan-African Investment Code (PAIC).[49] The SADC model also includes a more unique provision, requiring that investors not operate 'in a manner inconsistent with international environmental, labour, and human rights obligations binding on the Host State or the Home State, whichever obligations are higher'.[50] With respect to state obligations, the SADC model includes a non-lowering of standards provision,[51] and refers explicitly to environmental measures in its general exception.[52]

Other countries also have useful examples. Colombia's revised Model BIT, like the SADC model, refers explicitly to environmental measures in its general exception.[53] While Colombia's general exception is self-judging, meaning that the provision intends for states parties to determine whether a measure falls within the scope of the exception, it nevertheless requires the measures to be 'necessary' (often a high bar for a measure to meet).

Notably, even very recent treaties and models fail to specifically include explicit references to climate change, including, for example, how state's obligations under international investment law may interact with climate objectives or obligations.[54]

Key takeaway: *Despite clear and profound links between investment governance and realisation of climate objectives, even recent models fail to address this link, and therefore risk opening states up to ISDS claims challenging actions taken in good faith and consistent with climate mitigation and adaptation commitments and objectives. AU governments may wish to consider how investment treaties can be tailored to promote climate-friendly investment, deny protection to investments that undermine climate objectives and play a role in addressing climate mitigation and adaptation challenges that require global cooperation.*

Human rights

A 2014 study published by the Organisation for Economic Co-operation and Development (OECD) found that only 0.5% of the 2,107 treaties included in the study contained references to human rights, and a majority of those references were found in the preambles of the relevant agreements (Gordon et al., 2014: 18).[55] Developments in more recent drafting practice indicate some improvement, meaning that more recent treaties include some explicit references to (i) the human rights obligations of states in the context of investment governance and/or (ii) the human rights responsibilities of investors. However, these references remain rare and their effectiveness is generally untested and/or limited.

With respect to investor responsibilities, which can permit states to counterclaim for investor wrong-doing or to deny certain treaty protections in some cases, the draft PAIC includes a chapter on investor obligations.[56] Some of the provisions enshrined therein are mandatory, while others are enshrined in 'best efforts' terms. The PAIC includes a provision on counterclaims, which would enable a prospective respondent state to bring a counterclaim against an investor where they have failed to

[47] SADC Model Art 13.
[48] Morocco–Nigeria BIT Art. 14.
[49] Draft PAIC Art. 37.4.
[50] SADC Model Art. 15.
[51] SADC Model Art. 22.
[52] SADC Model Art. 25.
[53] Colombia revised Model BIT Art. [XX] General Exceptions.
[54] By comparison, some Free Trade Agreements (FTAs) and Economic Partnership Agreements (EPAs) without investor protections do contain such references. The EU's EPAs with Armenia and Japan, for example, include reaffirmations of the parties' commitments to implementation of the objectives of the United Nations Framework Convention on Climate Change, the Kyoto Protocol, and the Paris Agreement, and to further cooperation and implementation of international climate change frameworks. FTAs also frequently include provisions that recognising the links between trade and environmental obligations, and reaffirm commitments to implementing (in national laws and practices) multilateral environmental agreements to which states are party.
[55] Gordon et al. examined a sample of all investment treaties that 54 countries plus the European Commission had concluded with any other country 'provided that the full text was electronically available in early 2014', which meant that it covered 2,107 treaties and 'more than 70% of the global investment treaty population' (p. 10).
[56] Draft PAIC Ch. 4. Most treaties currently in force do not include any investor responsibilities or obligations, meaning that states are often unable to advance counterclaims against investors, or deny treaty protections, even in cases of investor wrongdoing.

comply with obligations under the Code or 'other relevant rules and principles of domestic and international law'.[57] Brazil's Model Cooperation and Facilitation Investment Agreement (CFIA) adopts a 'best efforts' approach to corporate social responsibility.[58] While the model represent a step forward as compared with old-generation agreements, it does not condition receipt of treaty benefits on compliance with those standards.

The Netherlands model (2019) includes ISDS, though it seeks to curtail access to the mechanism.[59] The model also includes some notable references to the human rights responsibilities of investors and obligations of states. For example, it requires prospective states parties to 'take appropriate steps' to ensure that those affected by business-related human rights abuse have access to effective remedy.[60] This mirrors the wording of Principle 25 of the United Nations Guiding Principles on Business and Human Rights (UNGPs),[61] seeking to reinforce that principle within the text of the model; however, its practical effects remain unclear. The model also provides that an ISDS tribunal determining a claim 'is expected to take into account non-compliance' by an investor claimant with commitments under the UNGPs and the OECD Guidelines for Multinational Enterprises.[62,63] This is unique among models, but it raises the question, for consideration by AU states, of whether non-compliance with human rights norms should be addressed by an ISDS tribunal through a reduction of damages (which still permits an investor to advance claims and a state to spend the time and cost of defending against them), or whether receipt of treaty benefits, and thus the ability to bring a claim in the first place, should be conditioned on the responsible business conduct of an investor.

A handful of recent agreements include specific exceptions or reservations that seek to address the ability of governments to take measures to preserve the rights of indigenous peoples concerning lands and natural resources. Examples include the Argentina–Japan BIT,[64] the Canada–Moldova BIT,[65] the US–Mexico–Canada Agreement (USMCA)[66] and the Comprehensive and Progressive Agreement for Trans-Pacific Partnership.[67]

These newer generation models represent a step forward as compared with the dearth of references to human rights obligations and responsibilities in texts reviewed by the OECD in its 2014 study. However, the examples referred to above remain the exception rather than the rule and, importantly, it is not yet clear that these new provisions will be effective in preserving the ability of states to comply with their human rights obligations and in conditioning receipt treaty benefits on responsible business conduct by investors.[68]

Key takeaway: *Consider whether human rights provisions will be effective in protecting the state's ability to regulate in practice, and how to condition treaty benefits on compliance by investors with investor obligations in order to promote responsible business conduct.*

Gender

While the intersection of gender and trade is more frequently addressed in more recent trade agreements, it is less frequently an issue area that is explicitly addressed in investment treaties and investment chapters within Free Trade Agreements (FTAs). The Brazil–Chile FTA, concluded in

[57] Draft PAIC Art. 43.
[58] Brazil Model CFIA Art. 14.
[59] The Netherlands Model BIT limits access to ISDS by, for example, specifying that arbitral tribunals 'shall decline jurisdiction' where an investor 'has changed its corporate structure with a main purpose to gain the protection of this Agreement at a point in time where a dispute had arisen or was foreseeable' (Art. 16.3).
[60] Netherlands Model BIT Art. 5.
[61] https://www.ohchr.org/documents/publications/guidingprinciplesbusinesshr_en.pdf>.
[62] Netherlands Model BIT Art. 23.
[63] https://www.oecd.org/corporate/mne/
[64] Annex II (Non-Conforming Measures, Schedule of the Argentine Republic).
[65] Annex I (Reservation for Future Measures, Schedule of Canada).
[66] Art. 32.5. For Canada, the 'legal obligations' referred to in this provision include the rights of indigenous peoples covered by Section 35 of the Constitution Act of 1982 and those set out in self-government agreements.
[67] Art. 29.6(1).
[68] For further discussion of the merits of various approaches, see Johnson (2019).

2018, includes a chapter on gender that reaffirms and incorporates a number of international human rights obligations relating to this issue area.[69] The chapter also provides for review, within two years, of implementation of the chapter, and national contact points are to be established to support cooperation regarding its implementation.[70]

Health

As with environmental provisions, references to the ability of states to regulate with respect to the health of their populations are found in some newer treaties and models. General exception provisions, where included, tend to provide that the treaty shall not preclude adoption or enforcement of measures relating to protection of human health. Such exceptions often require that measures be "necessary",[71] justified, proportionate to the objectives pursued, and/ or that that they not be discriminatory or arbitrary.[72] Where a treaty includes ISDS, a tribunal will have the discretion to assess the government's conduct.

Labour

Labour issues are dealt with in some recent treaties and models in provisions addressing (i) the state's ability to regulate and its obligations other international agreements; and (ii) investor obligations or (non-binding) responsibilities.

With respect to (i), these references appear in a similar manner to those concerning the environment and health, and could be strengthened accordingly. Regarding (ii), recent provisions vary considerably in terms of frequency and strength. Colombia's Model BIT, for example, provides that an investor may be denied the benefits of the treaty if 'an international court or a judicial or administrative authority of any State with which the Contracting Parties have diplomatic relations has proven that' the investor directly or indirectly violated the host state's labour laws, among other things.[73] The draft PAIC contains several labour-specific provisions, including that investors shall 'adhere to socio-political obligations' including those concerning 'respect for labor rights'.[74] Elimination of forced and compulsory labour is also listed as one of the principles listed as governing 'compliance by investors with business ethics and human rights' under the draft PAIC.[75]

In general, labour provisions in models and treaties could be strengthened by a minimum requirement to comply with the international labour standards adopted by the host and home state (whichever is higher), and by reference to existing reference to existing state obligations and investor standards under the International Labour Organization's framework.[76] Going beyond explicit references to labour obligations, provisions concerning performance requirements, compliance with domestic law, etc. are also closely connected to this issue area, and should be considered alongside those concerning labour obligations specifically (of both states parties and investors).

Sustainable development

Broader references to the sustainable development objectives of states parties are found in the preambles of some newer texts and (less frequently) in some operative provisions. The draft PAIC contains references to sustainable development and the Sustainable Development Goals (SDGs) in its preamble, and the Code's stated objective is 'to promote, facilitate and protect investments that foster the sustainable development of each Member State, and in particular, the Member State where the

[69] Ch. 8.
[70] Arts 18.4(9) and 18.5.
[71] A tribunal assessing whether a measure was 'necessary' will review the government's conduct and, among other things, whether less restrictive measures could have been adopted by the government. Necessity is a difficult test to satisfy.
[72] The draft PAIC (Art. 14), for example, does not require that measures be 'necessary' but it does require that measures 'are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between investors in like circumstances or a disguised restriction on investment flows'.
[73] Art. [xx] Denial of Benefits.
[74] Draft PAIC art Art. 20.
[75] Art. 24.
[76] For further discussion, see Bernasconi-Osterwalder et al. (2018: 11–13).

investment is located'.[77] The Code also provides that '[i]nvestors shall contribute to the economic, social and environmental progress with a view to achieving sustainable development of the host State'.[78] Similarly, the Mercosur Investment Protocol also recognises, in its preamble, the role of investment in the promotion of sustainable development and poverty reduction, and also provides that investors and their investments operate in a socially responsible manner.[79] The stated objective of the Protocol is to promote cooperation among states parties in order to facilitate investment that enables sustainable development.[80] Colombia's revised Model BIT conditions access to dispute settlement under the agreement on the '[i]nvestor's contribution to sustainable development and welfare of their [H]ost Party',[81] though the mechanism for assessing this is not outlined within the text of the model.

Beyond these references, more could be done to design agreements that *encourage and channel* investments that contribute to sustainable development, and to withhold treaty benefits from those investments that undermine or do not contribute to sustainable development.[82]

Key takeaway: *Recent models and treaties may contain noteworthy provisions when compared with 'old-generation' agreements. However, it is critical to investigate and assess whether these new provisions are sufficient to achieve the sustainable development objectives policy-makers are seeking to realise with the conclusion of investment agreements. Even 'new-generation' provisions continue to fall short.*

What steps are currently being proposed at multilateral levels?

The fundamental and systemic concerns about ISDS have prompted a number of reform processes at regional and multilateral levels. At the multilateral level, the United Nations Commission on International Trade Law's (UNCITRAL's) Working Group III on ISDS Reform has 'a broad mandate to work on possible reform of investor-State dispute settlement (ISDS)' (UNCITRAL, 2017), though this mandate has been interpreted to limit work to procedural aspects of ISDS rather than substantive treaty provisions. States have reiterated in their submissions and interventions that reform of ISDS will require addressing substantive provisions, including those concerning states' ability to regulate, in order to meaningfully reform ISDS. The International Centre for the Settlement of Investment Disputes is also undertaking a rule reform process, which is unlikely to directly address the substantive cross-cutting issues covered in this note.

The EU's proposed Investment Court System, also being discussed through UNCITRAL's Working Group III on ISDS Reform, similarly seeks to pursue procedural changes to dispute settlement. It does not directly address the cross-cutting matters raised in this note.

9.5 Dispute settlement

The meaning/ interpretation of treaty provisions is significantly shaped by dispute settlement, including, in particular, who has power to bring and frame claims. Excluding ISDS from models and treaties is an effective way of limiting direct exposure of states parties to future ISDS claims.[83] Other,

[77] Art. 1.
[78] Art. 22.3.
[79] Preamble.
[80] Art. 1.
[81] Section DD (dispute settlement) Art. X(3) (scope of application of ISDS).
[82] For further discussion, see Johnson et al. (2019).
[83] Brazil's Model CFIA, for example, excludes ISDS and focuses more on attracting and retaining investment, instead favouring establishment of ombudsperson mechanisms to address investor grievances if/when they arise. State–state dispute settlement is provided for as a last resort where disputes cannot be addressed through the domestic courts or through the ombudsperson mechanism. It also includes fewer traditional 'investor protection' standards. States have also reportedly chosen to exclude ISDS from the Regional Comprehensive Economic Partnership. ISDS was also limited in scope in USMCA: (i) as between the US and Mexico, ISDS was retained for certain breaches, after exhaustion of domestic remedies. Exceptions are made for a number of sectors (including oil, gas, power generation, transport services, telecoms and public infrastructure) where investors have covered government contracts – these claimants are not required to first exhaust local remedies; (ii) Canada and the US have removed ISDS from relations between those parties. Investors from these treaty parties will be able to bring ISDS claims against their host states for three years during a North American Free Trade Agreement/USMCA transition period, after which ISDS will no longer be available to them.

less effective, procedural mechanisms for limiting exposure to ISDS claims challenging environmental, human rights and other public interest measures include (i) state-state filters;[84] and (ii) not providing advance consent to ISDS.[85]

Consider also who has power to participate as a third party in dispute settlement processes. Affected third parties are currently excluded from meaningfully participating in ISDS; their ability to raise environmental, human rights and other public interest issues is therefore undermined. Where ISDS, ombudspersons or other dispute settlement mechanisms are provided for in a model or treaty, providing for meaningful participation of affected third parties enables relevant public interest matters to be heard and relevant rights and interests to be represented in the dispute/ process.[86]

Key takeaway: *When evaluating how to effectively preserve the ability to regulate, consider how environmental, human rights, gender, health, labour and other public interest provisions will interact with dispute settlement provisions and the broader nature and form of an investment agreement.*

9.6 How should countries be thinking about what is needed/desired?

Questions that may support evaluation of the effectiveness of environmental, human rights, gender, health, labour and other public interest provisions include:

- Are the provisions **aligned** with the objectives sought by treaty parties?
- Do the provisions **clarify** the interaction between state obligations under other areas of international, regional and national law (such as environmental and human rights law) and investment law?
- Do the provisions clearly and effectively **protect** host state measures adopted to comply with environmental, human rights, gender, labour, health and other public interest obligations or objectives?
- What **signals** do the provisions send to investors, states and other stakeholders? Do they promote or undermine responsible business conduct?
- Do they address **pressures** that can result in investment obligations taking precedence over public interest obligations in practice?

More broadly, existing treaties must be reformed and reimagined to achieve deeper alignment with Agenda 2063 and the SDGs. Most investment treaties continue to be far off this mark. The sustainable development objectives sought by policy-makers should be at the centre of any new negotiations, and of reviews of existing agreements. New and existing agreements could be assessed against their ability to:[87]

- encourage and channel investments that promote, rather than undermine, sustainable development
- foster, rather than constrain, SDG-advancing governance at the national level and
- promote international cooperation to overcome collective action challenges related to the governance of international investment.

[84] State–state filters help ensure that treaty parties have ongoing control over management of their treaties in ensuring that claims falling within the scope of protection are advanced, and that clear outliers cannot bring opportunistic or abusive claims (e.g. those challenging environmental and human rights measures) under the auspices of the treaty. These filters could be applied to a wide range of measures or, indeed, to all claims.

[85] In nearly all existing investment treaties, the state parties give consent in the treaty itself to be sued in arbitration by any investor who qualifies for treaty protections. In other words, the state gives 'advance consent' to any future claim at the time it ratifies the treaty. A different approach, and one that would give greater control to respondent states to limit claims for public interest measures, would be to provide treaty-based investor-protections, but not to grant consent in advance to arbitrate with the investor; rather, the state could give that consent on a case-by-case basis as claims arise.

[86] For approaches to consider, see CCSI et al. (2019).

[87] This framework is outlined in Johnson et al. (2019).

Creating space for reform also requires addressing the existing stock of treaties. Various options have been advanced to address the existing stock, including termination of treaties and withdrawal of consent to ISDS.[88] Most recently, in May 2020, 23 member states of the EU signed an agreement to terminate intra-EU BITs owing to the incompatibility of ISDS with EU law.[89] This most recent development further opens the door for much-needed creativity in addressing the large stock of old-generation treaties, and in further innovating the provisions enshrined in future agreements.

Key takeaway: *To align investment treaties with Agenda 2063 and the SDGs, evaluate new and existing agreements against the sustainable development objectives these agreements are seeking to realise. Various options exist for dealing with the existing stock of 'old-generation' treaties.*

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