Public interest, social and environmental policies under threat

Change EU investment policy – now is the time!

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Over the past decades EU member states have signed over 1200 "Bilateral Investment treaties" (BITs) designed to protect their investors abroad. BITs allow multinational corporations the right to challenge governments' social, environmental and economic regulations if they look like they might harm the profitability of their investment. The investment dispute settlement mechanisms that are typically an integral part of BITs allow foreign investors to by-pass domestic courts and sue sovereign states before international arbitration panels. BITs have cost taxpayers millions in legal expenses and compensations and are eroding the ability of governments to act in the best interests of their citizens. **Bilateral investment treaties are a threat to public policy, democratic governance and the public interest and should alert anybody concerned with environmental and social policies.**

There is now **a window of opportunity to break away from the current investment policies** and to put public interest before corporate profits. The Lisbon Treaty has moved the competence for foreign investments from the 27 European member states to the European Union level. The European Commission, Council and Parliament are at present discussing the content and directions of the future EU investment policy. **Social movements, human rights, development and environmental organisations as well as trade unions must speak out** and push for a balanced investment policy that is not merely concerned with investor rights, but holds investors accountable and promotes and protects public interests, human rights and environmental sustainability.

Why should EU citizens be concerned with investment treaties?

BITs are agreements between two countries that establish the terms and conditions for private investment in each other's territories. They typically contain clauses on non-discrimination, general treatment, compensation in the event of expropriation or damage to the investment and guarantees for the free transfer of capital. The terms in which these clauses are formulated tend to be legally very imprecise, which has enabled investors to greatly extend their privileges while making it very difficult for host states to predict the limits of their rights and obligations with any certainty whatsoever.

Environmental regulation and democracy under attack - the case of Vattenfall v. Germany

Investment treaties have typically had the hardest impact in the developing world, but a recent controversial case in the EU has revealed the potential financial and environmental cost for European taxpayers. In 2009, Vattenfall brought the German government to arbitration before an ICSID tribunal for allegedly violating the terms of the Energy Charter Treaty - a multilateral agreement governing investments in the energy sector. Vattenfall was demanding compensation over the introduction of environmental measures restricting the use and discharge of cooling water for the coal-fired power plant the company was constructing on the banks of the Elbe river. Vattenfall maintained the new regulations ran counter to earlier assurances given by the public authorities of the city of Hamburg and would hamper the economic viability of the project. However, the public authorities say the restrictions of Vattenfall's water permit are a result of an EU directive on water quality that affects all industries along Germany's rivers.

In August 2010, a settlement was reached between the contesting parties. The exact terms have not been made public, but Vattenfall's original arbitration request shows the company was seeking some 1.4 billion Euros in compensations for damages to their 2.6 billion Euro investment. German and international media reports have alluded to a possible dilution of local water-use restrictions which would otherwise have prevented the completed plant from operating at full capacity.[1]

[1] 'Parties announce settlement of dispute over German power plant 28.8.2010', Investment Treat News, Issue 1, Volume 1, September 2010.

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This legal uncertainty is aggravated by the fact that most BITs include mechanisms for dispute settlement that allow investors to bypass national legal systems and bring host states before international arbitration tribunals when they consider that their rights under the BIT have been violated.

BITs are mainly concerned with the protection of investors' rights. Investor obligations are largely excluded. BITs typically do not contain standards to protect the environment, labour rights, social provisions or natural resources. As a result these are rarely taken into consideration by arbitration tribunals, whose decisions are final and binding, even though cases are generally conducted behind closed doors, away from public scrutiny.

Arbitration cases have so far challenged a wide range of environmental regulations, including the bans of various chemicals for environmental reasons, a permit refusal for a hazardous waste landfill, an export ban on PCB waste and measures requiring open-pit metallic mines to backfill.[2] Social policies have been another target area.

Since the first cases in the 1990s, more than 300 arbitrations have been launched, mostly against developing countries, with disputes centring on public services, including water, electricity, telecoms and waste management and natural resources (oil, gas and mining).[3] These arbitration cases pose serious challenges to states' responsibility to promote social and environmental well-being. The costs involved can drain government budgets for social spending, health and education. A fear of being dragged into lawsuits and compensation obligations can even lead to a 'regulatory chill', where states abandon proposed social or environmental regulation.

As a 'market leader' in outward investment, the EU has thus far rarely been on the receiving end of such arbitration cases. But that may change rapidly, given the shifting global balance of economic power. Emerging economies like China and India are increasingly engaged in outward investment.

Soon the measures we take to combat the effects of the current economic crisis and regulate banking, to stop climate change, ensure public service provision and protect the environment could all become subject to litigation – with public authorities, and thus the ordinary tax payer, having to cough up millions of Euros in damages.

Foreign investors undermine South Africa's policies to redress apartheid

In 2007, a group of Italian/Luxembourg investors in South Africa's mining industry filed a claim for ICSID arbitration, arguing that the South African Black Economic Empowerment (BEE) programme violated the BITs signed with South Africa by both Luxembourg and Italy. The BEE programme is at the heart of policies to redress inequalities in South Africa. Under the Mineral and Petroleum Resources Development Act (the MPRD Act), which came into effect in 2004, South Africa required a re-licensing of all mining companies. The new licences came with conditions relating to the transfer of a greater proportion of shares into the hands of black investors and efforts to increase the percentage of 'historically disadvantaged' South Africans in management positions. The investors argued that the re-licensing conditions ran counter to South Africa's obligation to guarantee them 'fair and equitable' treatment 'no less favourable' than that awarded to domestic investors, as stipulated by the BITs. The case was settled in 2010, with South Africa granting significant concessions regarding the investors' BEE obligations.[4]

Questioning the human right to water

A group of European investors operating a 30-year concession to provide water and waste water services in and around Buenos Aires challenged various actions taken by Argentina to counter the financial crisis that hit the country in the late 1990s. These measures, they alleged, destroyed the value of their investment and thus violated Argentina's obligations to protect their interests as foreign investors under its BITs with Spain, the UK and France.

In its final ruling (30 July 2010), the ICSID Tribunal accepted that Argentina had experienced a severe economic crisis that could justify its defensive measures. However, it went on to rule that Argentina could have taken other measures to respond to the crisis that would not have violated the investors' rights.

Argentina had urged the Tribunal to take into account the fact that the concession dealt with water and impacted the human right to that resource. However, the Tribunal rejected the notion that a government's human rights obligations trump its obligations to investors under BITs. According to the Tribunal, states must respect both its human rights and treaty obligations equally. The amount of damages is yet to be decided.[5]

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[2] Nathalie Bernasconi, Background paper on Vattenfall v. Germany arbitration, International Institute for Sustainable Development, July 2009.

[3] ITUC Briefing note on Bilateral Investment Treaties, at: http://gurn.info/en/topics/bilateral-and-regional-trade-agreements/bilateral-investment-treaties/background/tils-briefing-note-on-bilateral-investment-treaties (accessed 22-11-2010).

[4] For more on this case, see: ITUC Briefing note on Bilateral Investment Treaties, at: http://gurn.info/en/topics/bilateral-and-regional-trade-agreements/bilaterl-investment-treaties/background/tils-briefing-note-on-bilateral-investment-treaties (accessed 22-11-2010). And: 'ICSID Tribunal awards South African Government 7.5 per cent of its Euro 5.33m costs claim', at: http://www.webberwentzel.com/wwb/view/wwb/en/page1873?oid=27715&sn=detail&pid=1873 (accessed 22-11-2010).

[5] 'Argentina on the hook for breach of Fair and Equitable Treatment', Investment Treaty News, Issue 1, Volume 1, September 2010.

Scope for change

The European policy context now offers a window of opportunity to redress the glaring imbalance between public and private interests within investment agreements.

The transfer of competence by the Lisbon Treaty requires both the development of an overarching EU investment policy and a way to deal with the 1200 existing Bilateral Investment Treaties of the member states. This offers a unique opportunity for an open and broad discussion on the substance of European international investment policy.

In July 2010, the Commission initiated the policy development process by publishing a Communication 'Towards a Comprehensive European Investment Policy', as well as a draft regulation on how to deal with existing BITs. These are now up for consideration by the Council and the European Parliament. Meanwhile, the European Commission is drafting mandates to add investment protection provisions to the free trade agreements it is negotiating with Canada, India, Singapore and the South American regional block Mercosur. Mandates for self-standing investment treaties with Russia and China may soon follow.

The Commission has indicated that under the Lisbon Treaty the EU's common investment policy needs to be guided by broader EU objectives such as human rights and sustainable development. It has also suggested to seek more transparency in the investor-to-state dispute settlement and to ensure a better balance between public and private interests with regard to expropriation.

But at the same time, the Commission will be looking to build on the 'best practices' of the Member States' existing BITs. It will likely hold on to the broadly phrased and open-ended investor protection provisions that have in practice led to corporations suing against all forms of regulation. The EU member states in any case are determined to make the EU policy reflect their own practice and to maintain their own BITs and investment policies for as long as possible.

Now is the time for civil society to voice its concerns and push for a radically new approach to foreign investments. Civil society organisations should:

– contact their national **members of the European Parliament** and in particular of the Trade Committee (INTA) which will vote in March-April on a resolution on the new EU investment policy and on amendments to the draft regulation dealing with the existing member states BITs;

– contact their **national members of parliament** to question the investment policies of their national governments and the positions they take in the Council;

– contact the **European Commission** to dissuade it from copying damaging member state BITs practices and launching investment negotiations before a thorough assessment and broad public discussion has taken place;

– pass this briefing onto others, organise events and stir a **public debate** about this issue!

BITs under fire from the global South

For many developing countries, foreign direct investment is an important source of capital needed for economic growth. However, it is clear that the EU's current BITs have not been designed to further sustainable development. Countries around the world are becoming increasingly aware of the possible negative consequences of BITs. Realising that BITs are only one of the many factors that impact on companies' decisions where to invest,[6] various countries have begun to evaluate and revise their investment policies. The South African government is currently critically reviewing all its BITs to better align them with development considerations,[7] putting forward the argument that: 'One of the most fundamental elements of state sovereignty is both the right and the duty of governments to regulate economic activities and actors in the broader public interest... Investment promotion and protection must not be pursued at the expense of other key policy objectives.'[8] As one of the largest receivers of FDI in Latin America, Brazil continues to hold off ratification of its BITs. And in 2007, Bolivia made the decision to withdraw from ICSID. The fact that ICSID allows multinationals to file charges against governments – including for the 'loss' of <u>future</u> earnings - , but does not permit governments to take action against multinationals is a key objection for Bolivia. Bolivia's president Evo Morales motivated his decision by saying: "(We) emphatically reject the legal, media and diplomatic pressure of some multinationals that ... resist the sovereign rulings of countries, making threats and initiating suits in international arbitration."[9]

[6] The Role of International Investment Agreements in Attracting Foreign Direct Investment to Developing Countries, UNCTAD Series on International Investment, 2009. At: http://www.unctad.org/en/docs/diaeia20095_en.pdf
[7] http://www.thedti.gov.za/ads/bi-lateral.htm
[8] http://www.dti.gov.za/ads/bi-lateral_policy.doc
[9] http://www.allbusiness.com/legal/labor-employment-law-alternative-dispute-resolution/8906068-1.html

Any **new investment regime for the EU** will need to be guided by:

- the incorporation of **investor obligations** into investment agreements in particular in areas of human rights and corporate accountability
- more **precise and restrictive language** regarding investors' rights
- the **abolition of** one-sided and secretive **investor-to-state dispute settlement mechanisms**
- an explicit recognition of the **right of governments to regulate** and to formulate policies of general interest
- a substantive **social and environmental dimension**

As part of the process to establish the principles that must underpin the EU's common investment policy, all existing EU member states BITs should be thoroughly assessed for their impact on the ability of governments to further sustainable development, gender justice and social equity as well as their obligation to implement international conventions and treaties on human, women's and labour rights, the environment and climate change. Until that assessment has taken place, **all member states' BIT negotiations** should be **put on hold**. All **existing BITs of the member states should be replaced** to comply with the EU's overarching human rights principles.

Influencing Europe's policy choices matters and could make a decisive global difference: The EU is both the world's leading host and source of foreign direct investment. Its member state BITs together represent almost half of the investment agreements currently in force around the world.

Text: Roeline Knottnerus, on behalf of & with help from the S2B Investment Group (www.s2bnetwork.org)

Further reading

- ► Seattle to Brussels Network, Reclaiming Public Interest in Europe's International Investment Policy: EU Investment Agreements in the Lisbon Treaty Era: A Reader: http://www.s2bnetwork.org/fileadmin/dateien/downloads/eu_investment_reader.pdf
- ► Austrian Federal Chamber of Labour, Position Paper on EU Investment Policy: http://akeuropa.eu/_includes/mods/akeu/docs/main_report_en_138.pdf
- ► Public Statement on the International Investment Regime, (by a group of over 35 international academics) 31. August 2010: http://www.osgoode.yorku.ca/public_statement/documents/Public%20Statement.pdf
- ► EU Commission DG Trade website on investment policy: http://ec.europa.eu/trade/creating-opportunities/trade-topics/investment/

Glossary

(Indirect) expropriation
A provision that prohibits the expropriation of nationalisation of foreign investment, except when strict criteria are observed and full compensation is granted. Foreign investors have increasingly and successfully challenged a range of government regulations, including environmental and social acts, arguing that compensation should be granted as the contested measures should be classed as 'indirect expropriations' for having the effect of reducing the value of investors' (future) profits.

National treatment
A clause prohibiting preferential treatment for domestic investors. (Note that the clause does not ban preferential treatment for foreign investors!) NT is a contentious principle, as it makes it harder for countries to, for example, support their infant industries, develop region-specific policies or roll out policies that require foreign investors to use local resources (labour, raw materials) in their production processes.

Most-favoured nation treatment (MFN)
Obligation to accord investors from the partner country similar treatment to the best treatment accorded to any third nation. This clause can hinder regional integration and cooperation between developing countries if preferential treatment automatically has to be extended to powerful multinationals from developed countries.

Fair and equitable treatment
A largely undefined legal concept that is frequently invoked in international investment arbitration. "Fair and equitable treatment" provisions expand on the already extensive rights granted to foreign investors under clauses on "national treatment" or "most-favoured nation treatment" by providing scope for arbitration tribunals to resort to a wide interpretation of what is required to guarantee a stable investment climate or to not impinge on an investor's "legitimate expectations".

Umbrella clause
The duty of either signatory to an international investment agreement to observe all commitments they have entered into with regard to the other signatory's foreign investors. An umbrella clause offers foreign investors extended protection by elevating breaches of contract to breaches of international law.

Investor-to-state arbitration
An increasingly important mechanism for private investors to resolve disputes with government entities of a foreign country and to recover losses caused by government actions at any level (federal, state, provincial, or local). Nearly all investment agreements include a provision that allows for these arbitrations. Investor-to-state arbitration is not available for national investors who only have recourse to their national legal systems.