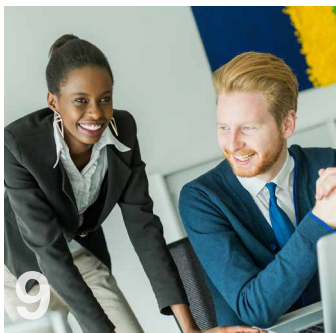




## The Brazilian Agreement on Cooperation and Facilitation of Investments (ACFI): A New Formula for International Investment Agreements?

Fabio Morosini and Michelle Ratton Sanchez Badin

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**Farmland Investments and Water Rights in Africa:  
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# contents

- 3 Features**  
 The Brazilian Agreement on Cooperation and Facilitation of Investments (ACFI): A New Formula for International Investment Agreements?  
*Fabio Morosini and Michelle Ratton Sanchez Badin*
- 6 Farmland Investments and Water Rights in Africa: The Legal Regimes Converging over Land and Water**  
*Makane Moïse Mbengue and Susanna Waltman*
- 9 Working by Design: New Ideas to Empower U.S and European Workers in TTIP**  
*Susan Ariel Aaronson*
- 12 News in Brief**  
 Binding instrument on business and human rights: Working Group holds its first session; European Parliament supports TTIP, but rejects current ISDS model; Bolivia promulgates Conciliation and Arbitration Law with regime for investor–state disputes; European Commission requests Member States to terminate intra-EU BITs; China signs FTAs with South Korea and Australia, conducts new round of BIT negotiation with United States
- 13 Awards and Decisions**  
 Unanimous ICSID tribunal dismisses expropriation claim due to Papua New Guinea’s lack of written consent to arbitrate  
*Marquita Davis*
- 14 Government bonds not covered, despite broad definition of “investment” in Slovakia–Greece BIT; tribunal dismisses claims against Greece**  
*Martin Dietrich Brauch*
- 16 Looking to Venezuela’s Investment Law, majority finds that Venoklim was not a foreign investor and dismisses case against Venezuela; claimant-appointed arbitrator dissents**  
*Martin Dietrich Brauch*
- 18 Majority of ICSID tribunal finds no fair and equitable treatment violation by Albania in petroleum dispute**  
*Matthew Levine*
- 20 Tribunal found Mongolia liable for unlawful expropriation and awarded more than US\$80 million in damages**  
*Joe Zhang*
- 23 Resources and Events**

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# The Brazilian Agreement on Cooperation and Facilitation of Investments (ACFI): A New Formula for International Investment Agreements?

Fabio Morosini and Michelle Ratton Sanchez Badin

## feature 1



Since the signing of the first Agreement on Cooperation and Facilitation of Investments (ACFI) by Brazil, in March 2015, English translations of the document and analyses of its innovative aspects have been published.<sup>1</sup> The hidden question is: to what extent do Brazil's ACFIs innovate in the regulation of foreign investments?

Alternatives to the current liberal international economic system and its framing rules have been rare in the last 40 years. The ACFIs can be considered a pragmatic response to the system, based on Brazil's domestic needs and geo-economic position. The ACFI model was designed taking into consideration economic specificities of a developing country such as Brazil: a historical recipient of investment, a latecomer exporter of capital, and the current combination of both, favouring the triangulation of foreign investments abroad. In this context, the ACFIs have definitely brought new elements to the international investment scene.

Other scholars as well as policy-makers and practitioners have gone into well-done descriptions of the details and novelties of the ACFIs.<sup>2</sup> In this article, we go beyond, by contextualizing the catalysts of these agreements, relating their new elements to the clauses and the legal language used in the Brazilian ACFI model. We also present our understanding of the Brazilian ACFIs as a product of cross-fertilizing narratives: host countries' contestation movements against unequal economic relations crystallized in traditional-type bilateral investment treaties (BITs), the search for alternatives to the hotly debated reengineering of the current international investment regime, and an attempt to create a genuinely Brazilian model investment agreement that is sensitive to internal constitutional limitations and responsive to Brazil's aspirations as an emerging economy.

We address these topics in two sections, followed by a brief conclusion. The first section details the historical and current context of the model, and the second describes the main efforts employed by Brazil to design an agreement with clauses that are symmetrical in form and content.

### 1. The historical track record of the Brazilian ACFIs: domestic and international drivers

From March to June 2015, Brazil signed four ACFIs, with Mozambique, Angola, Mexico, and Malawi.<sup>3</sup> Although Brazil is an emerging economy and has traditionally been one of the top destinations for foreign direct investment (FDI), it has historically played a different regulatory card in a world dominated by a web of BITs.

In the 1990s, Brazil signed BITs with 14 countries. However, strong political opposition by Congress and the Judiciary, combined with an unresolved Executive, impeded the country from ratifying any of the proposed agreements.<sup>4</sup> Brazil then became known as one of the few top economies without BITs or an investment agreement model. Following that failure at the legislative branch, certain bodies of the executive branch, led by the Ministry of Industry, Development and Commerce (MDIC), kept the topic in their agenda, addressing alternative formats for the regulation of investments at the international level. Such efforts first considered external relations with MERCOSUR and other South American countries and later became a broader policy concerning the global South: Africa, Asia, and Latin America.

But it was only in 2012 that the Brazilian Chamber of Foreign Trade (CAMEX) granted a formal mandate to a Technical Group for Strategic Studies on Foreign Trade (GTEX) to work on—among other topics—the drafting of a new investment agreement sensitive to Brazilian needs and concerns at the international economic scenario. In the context of Brazil–Africa relations, GTEX recommended the creation of a new type of investment agreement, under the leadership of MDIC's Foreign Trade Secretariat (SECEX). This gave a new push to the continuous but slow process that had started with the negotiation of the BITs in the 1990s. The GTEX mandate was the zenith of the process, and the result of the technical capacity of MDIC officials in a favourable political moment in Brazil—the right people at the right time.

At that point, Brazilian firms had almost doubled their investments abroad in five years, to a record US\$355 billion. It was a time when national politics met the industry's private interest: firms were investing abroad—mainly in Latin America and Africa—while Brazil's external policy was also geared toward South–South relations, for reasons not limited to economic rationales. GTEX then initiated consultations with the private sector in Brazil<sup>5</sup> concerning the main challenges of the transnationalization of Brazilian companies.

From the beginning of the negotiation process, Brazil envisioned a different agreement from those negotiated

in the 1990s. In parallel to the contestation movement in developing country host states, even if at different paces and intensities, the drafting of the Brazilian model investment agreement was equally influenced by ongoing debates concerning the reform of the international investment regime, lessons learned from the failure of the approval of the investment agreements negotiated in the 1990s, and internal demands for market access. A template for the new agreement—addressing all those concerns—was ready as from 2013 when it was approved by CAMEX, and then proposed to states where Brazilian companies were more consistently investing. Mozambique, Angola, Mexico, and Malawi were the first countries to react positively to Brazil’s negotiating push.

## 2. ACFIs: framing investments under an ought-to-be-dynamic process

The ACFI framework was built on the revision of previous agreements by Brazilian policy makers—considering the limits of domestic regulation—and on the inputs from the Brazilian private sector based on their recent experience as capital exporters.<sup>6,7</sup> The combination of those demands resulted in a model agreement that focuses on investment facilitation and risk mitigation. Although this structure is not new to international investment agreements, the ACFI brought new components to their content. Constant cooperation among governmental agencies, mediated by diplomatic action, and deference to domestic legislation can be considered the leading notions behind this model agreement, which offers an alternative to the current international investment regime.

### 2.1. Investment facilitation

Investment facilitation provisions are mostly concerned with market access, and they prevail in the structure of the ACFIs signed to date. In this respect, simple measures such as visa policy and the regularity of flights were considered basic needs for the effective promotion of investment flows from Brazil into its counterparts (mainly other developing country economies). While those may be problems for an investor from any part of the world, such barriers are more costly for investors from developing countries, to the extent that they limit capital exports in the absence of alternatives. Brazil chose to address such problems through an investment agreement, including a thematic agenda for investment cooperation and facilitation as one of its core elements.

The thematic agendas comprise programs on money transfers, visa proceedings, technical and environmental licenses and certifications, as well as provisions for institutional cooperation.<sup>8</sup> Such agendas also revive developing country claims to technology transfer, capacity building, and other

developmental gains from foreign investment. In addition, they express the understanding that the benefit to the home country must come not only from capital exports, but also from the overall impact that investment from the home country will have on the host country, such as employment of local labour. In this sense, the ACFI model aims at advancing symmetry beyond formal rules, and its design takes into account the domestic needs of both capital importing and exporting countries.

The ACFIs encourage the parties to negotiate special commitments, additional schedules, and other supplementary agreements as part of the main agreement, in order to expand or detail the thematic agendas.<sup>8</sup> In the opinion of Mr. Daniel Godinho, Secretary of SECEX and a key person in designing and negotiating the agreements, the existence of such thematic agendas turn the ACFIs into dynamic agreements that may evolve along with the bilateral investment relations.

### 2.2. Risk mitigation

The risk mitigation dimension of the agreement comprises typical rules for investment and investor protection,<sup>9</sup> and diplomatic and cooperative mechanisms for implementing, overseeing and enforcing the parties’ obligations, including dispute settlement mechanisms. On this issue, we read the ACFI provisions mainly as a product of the international agenda for reforming the investment regime and of specific domestic concerns on the topic.

Each ACFI creates two types of institutions to govern the agreement: a Joint Committee and ombudsmen (Focal Points). The Joint Committee operates at the state-to-state level, while the Focal Points, inspired by the ombudsmen from the 2010 Korean Investment Act, provide government assistance to investors, dialoguing with government authorities to address the suggestions and complaints from the other party’s government and investors. Influenced by multilateral organizations, such as the United Nations Conference on Trade and Development (UNCTAD),<sup>10</sup> and experiences from other countries, Brazil has strongly emphasized the prevention of disputes between the parties in its ACFI template. Therefore, the roles of both the Joint Committee and the Focal Point are, primarily, to promote regular exchange of information and prevent disputes and, if a dispute arises, to implement the dispute settlement mechanism, based on consultations, negotiations and mediation. This mechanism aims to deter investors from judicially challenging host government measures. Unlike traditional BIT-type agreements, the ACFIs do not allow investors to initiate arbitration against the state. Brazilian public officials note that, even though state-to-state arbitration is mentioned in the agreements, it shall not be the foremost mechanism for settling disputes.

The transparency mechanisms in the ACFIs may also serve to mitigate risk. Instead of establishing transparency standards, however, the ACFIs provide that “each Party shall employ its best efforts to allow a reasonable opportunity for those interested to voice their opinion about proposed measures.”<sup>11</sup> This may still be considered a novelty to the current regime. The agreements also include corporate social responsibility (CSR) clauses, encouraging foreign investors to respect human rights and environmental laws in the host state, also in order to mitigate risk. Even though the agreements are ambiguous regarding the binding force of these CSR obligations and even more so regarding mechanisms to enforce them,<sup>12</sup> they do innovate by addressing the protection of interests of the host state and its citizens within an international investment regulation.

## Conclusion

Brazil chose to address its developing country and latecomer limitations to investment flows through an alternative model agreement, which can be seen as a first step toward more symmetry in investments agreements. The provisions on investor and investment protection are not the main focus of the ACFI. In terms of investment policy engineering, the ACFI stands for a regulatory tool that is alternative to investor and investment protection. It emphasizes constant coordination between the parties’ agencies and investment facilitation under thematic agendas for cooperation, and deference to domestic legislation. Although we identify more innovation capacity in this part of the agreement, we also recognize that new elements were brought to the scene with respect to risk mitigation and dispute prevention.

However, the ACFI itself still needs to be further regulated—particularly as to the functioning of institutional mechanisms— and its provisions must be given a breath of life. Brazil and its counterparts have homework to do in detailing the framework for the ACFIs and the investment relations under the agreements. Therefore, the ACFI model and its innovative contribution will be put to test in the regulation and implementation of the concluded agreements, a challenge that highly depends on the coordination and cooperation capacity of the parties’ agencies.

## Authors

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## Notes

1 International Institute for Sustainable Development (IISD). (2015, June 16). *Side-by-side comparison of the Brazil–Mozambique and Brazil–Angola Cooperation and Investment Facilitation Agreements*. Retrieved from <http://www.iisd.org/publications/side-by-side-comparison-brazil-mozambique-and-brazil-angola-cooperation-and-investment>

2 Brauch, M. D. (2015, May). The Brazil–Mozambique and Brazil–Angola Cooperation and Investment Facilitation Agreements (CIFAs): A descriptive overview. *Investment Treaty News*, 6(2), 14–16. Retrieved from <https://www.iisd.org/sites/default/files/publications/iisd-itn-may-2015-en.pdf>; Hamilton, J. C., & Grando, M. (2015). Brazil and the future of investment protections. *Latin Arbitration Law*. Retrieved from <http://www.latinarbitrationlaw.com/brazil-and-the-future-of-investment-protections>; Rolland, S., & Trubek, D. (2015). Brazil develops a new model BIT – A challenge to the US model? *International Trade Daily*, 108. Retrieved from <http://www.washingtontradedaily.com/index.html> (subscription only); Monebhurrin, N. (2014). Crônicas de Direito Internacional dos Investimentos. *Revista de Direito Internacional*, 12(2), 64–77.

3 The text of the Brazil–Mozambique ACFI is available at [http://www.itamaraty.gov.br/index.php?option=com\\_content&view=article&id=8511&catid=42&Itemid=280&lang=pt-BR](http://www.itamaraty.gov.br/index.php?option=com_content&view=article&id=8511&catid=42&Itemid=280&lang=pt-BR); the text of the Brazil–Angola ACFI, at [http://www.itamaraty.gov.br/index.php?option=com\\_content&view=article&id=8520&acordo-brasil-angola-de-cooperacao-e-facilitacao-de-investimentos-acfluanda-1-de-abril-de-2015&catid=42&lang=pt-BR&Itemid=280](http://www.itamaraty.gov.br/index.php?option=com_content&view=article&id=8520&acordo-brasil-angola-de-cooperacao-e-facilitacao-de-investimentos-acfluanda-1-de-abril-de-2015&catid=42&lang=pt-BR&Itemid=280); the texts of the Brazil–Mexico and Brazil–Malawi ACFIs are available, upon request, at SECEX/MDIC.

4 Lemos, L. B., & Campello, D. (2013, April 1). *The Non-ratification of bilateral investment treaties in Brazil: A story of conflict in a land of cooperation*. Retrieved from <http://ssrn.com/abstract=2243120>

5 Private sector consultations were held with the Federation of Industries from the State of São Paulo (FIESP, in Portuguese) and the National Industry Confederation (CNI, in Portuguese).

6 According to MDIC, in contrast to the traditional-type BIT experience, the Brazilian government’s position was: 1) to restrict the expropriation concept only to direct expropriation, and its compensation in accordance with the Brazilian Constitution (Articles 5, 182 and 184 of Brazil’s Federal Constitution of 1988 provide that expropriation of urban and rural real properties may be—among other possibilities—compensated with public and agrarian bonds, respectively); 2) to establish a dispute settlement mechanism limited to state–state disputes; 3) to admit exceptions to the free transfer obligation, aiming at safeguarding the host country’s balance of payments; 4) to limit investor protection under the agreement to productive investments, according to the International Monetary Fund’s definitions and under the conditions of the host country domestic rules; and 5) to welcome host countries’ policy spaces in the definition of exceptions to National Treatment and Most-Favoured-Nation Treatment (MFN) obligations.

7 In addition to that agenda, the Brazilian private sector voiced their position by answering a survey on investment facilitation. Based on the survey and on further studies conducted by GTX, three additional elements were added: 1) a focal point where firms could go for advice and help throughout the investment relation; 2) provisions for risk mitigation and dispute prevention; and 3) a thematic work program for investment facilitation devoted mainly to visa and licencing proceedings, among others. D. Godinho, Head of the Brazilian Foreign Trade Secretariat (SECEX), Ministry of Development, Industry and Commerce, personal communication, April 28, 2015.

8 In June 2014 Angola and Brazil had signed a Protocol about Visa Facilitation that was taken into account in the thematic agenda of the Brazil–Angola ACFI, Annex I, subparagraph 1.2(i).

9 The ACFIs include National Treatment and MFN provisions, but exclude Fair and Equitable Treatment and Full Protection and Security clauses. Indirect expropriation, one of the issues that faced resistance before Congress in the 1990s, is also not covered by the ACFIs.

10 United Nations Conference on Trade and Development (UNCTAD). (2013, June 26). Reform of investor–state dispute settlement: In search of a roadmap. *IIA Issues Note No. 2*, p. 5. Retrieved from [http://unctad.org/en/PublicationsLibrary/webdiaepcb2013d4\\_en.pdf](http://unctad.org/en/PublicationsLibrary/webdiaepcb2013d4_en.pdf) (stating that “ADR methods can help to save time and money, find a mutually acceptable solution, prevent escalation of the dispute and preserve a workable relationship between the disputing parties”).

11 See, for example, Article 13, paragraph 3, of the Brazil–Mozambique ACFI, available at [http://www.itamaraty.gov.br/index.php?option=com\\_content&view=article&id=8511&catid=42&Itemid=280&lang=pt-BR](http://www.itamaraty.gov.br/index.php?option=com_content&view=article&id=8511&catid=42&Itemid=280&lang=pt-BR)

12 Brazilian human rights NGOs have complained about their low normativity, and the lack of international mechanisms to enforce the responsibility for violations in the field, see Borges, C. (2015, May 29). *Acordos bilaterais à brasileira. Valor Econômico*. Retrieved from <http://www.valor.com.br/opiniao/4072416/acordos-bilaterais-brasileira> (subscription only).

## feature 2

# Farmland Investments and Water Rights in Africa: The Legal Regimes Converging over Land and Water

Makane Moïse Mbengue and Susanna Waltman



Access to water is the driving force behind the surge in foreign investment in farmland. Yet, with all the focus on “land grabbing” and food security, water issues have received little attention. Although essential to life, water resources tend to be taken for granted until they are strained or completely depleted. They may seem abundant, but in fact less than 3 per cent of all available water resources are suitable for human consumption or other uses. Of that, over 70 per cent is used in agriculture. Being interconnected and in constant motion, water resources are particularly vulnerable to the impacts of farmland investment. The amount of water extracted for farmland investments and the quantity and nature of the chemicals from pesticides and fertilizers directly impact the water resources available for other users.<sup>1</sup>

Africa is the primary recipient of farmland investments and has been promoted internationally as having vast untapped water resources, but a significant number of Africans already live in water-stressed environments. Population growth, climate change and land use change are predicted to drastically increase that number. Farmland investments—and the large-scale commercial farming they entail—require vast amounts of water and further exacerbate this strain on water resources.

So far, international investment law and the rights of investors have started to receive some attention in this context. However, the location of the investments near international river basins and their sustained water use also trigger obligations under international freshwater law, environmental law and human rights law. Furthermore, these regimes implicate a wider range of stakeholders, including local communities and other riparian states. It is therefore vital to understand all applicable legal regimes and the rights of all stakeholders.

### 1. Problems in the area of water rights and farmland investments

The most significant impact of climate change is on water resources, and Africa is the most vulnerable to

this process. The effects of climate change are not just risks: they are already being experienced in parts of Africa, with lake levels declining in various places due to the combined effects of drought, warming and human activities. Climate change is predicted to cause increased frequency and risk of floods and droughts, and some studies suggest a significant decrease in suitable rain-fed agricultural land. Arid and semi-arid land could increase by 5 to 8 per cent in Africa, that is, 60 to 90 million hectares.<sup>2</sup>

Irrigation is therefore seen as a necessary adaptive response, and host states see foreign investment as a chance to develop it. But if irrigation is simply increased, the overall water use will be increased, depriving downstream areas of water.<sup>2</sup>

Studies suggest that putting all farmland leased to foreign investors into irrigated production would be “hydrological suicide,” because the amount of water that would be required is more than what is available, particularly in the Nile River Basin.<sup>3</sup> Although these fears may be exaggerated, farmland investments will certainly increase water consumption significantly in the region. Large-scale farming impacts both water quantity and quality, given the necessary water to maintain commercial production and the sustained use of pesticides and fertilizers. The impact of these investments on water resources has yet to be evaluated; studies have revealed an almost total lack of monitoring of their water use.<sup>4</sup>

Moreover, studies have revealed that the crops these investments produce are exported to the investor’s home state or destined for high-end urban consumers and are not accessible by the most vulnerable populations in need.<sup>4</sup> The investments therefore do little to address food security concerns in the host state, hardly offsetting the extra strain on water resources.

### 2. The legal framework governing water rights and farmland investments

Several legal regimes were developed to suit different objectives: investment protection, sustainable management of water resources, the environment more generally, or human rights. In the context of farmland investments and their water use, these interests converge and potentially clash. In addition to the increasing pressures on water resources, an imbalance in the legal framework governing farmland investments and water rights exists at both domestic and international levels, as discussed below.

#### 2.1. Domestic law and contracts

##### a. Domestic law

In most African states, water belongs to the public domain; rights to use water can be either exercised by the state or local authority or granted to private

individuals and corporations according to domestic law. Although constitutional arrangements governing water resources vary across Africa, certain common elements are revealed, based on whether the legal system developed out of the common law or the civil law tradition, and due to formal and informal rights resulting from the prevailing role of custom in Africa.

Most local communities hold their land and water rights under customary law. Customary law is the most known and respected source of law by most host state populations, but it places local users at a disadvantage when compared to foreign investors who obtain statutory rights from contracts with the host state. Under most domestic legal systems, customary law and rights are recognized, but cannot apply over areas covered by written law or rights. Foreign investors' statutory written rights will therefore prevail over the customary unwritten rights of local communities in the event of conflict over water or land resources. Further, in states that have adequate water legislation and administration, local usages and customs are left unwritten and unrecorded for the most part, since they mostly apply to minor water utilizations and in cases where the written law does not cover the specific issue at hand.<sup>5</sup> Local communities are thus legally vulnerable even where an administrative framework is in place to govern water resources. Moreover, most formal land and water management systems are poorly implemented and therefore have little effect.

#### b. Contracts between foreign investors and host states

Many agricultural investment contracts between investors and host states do not expressly mention or deal with water or provide for any fees or revision of allocation. Host states may not realize that, when granting foreign investors the right to operate and maintain an agricultural investment, they also grant the necessary water rights to sustain that production, even where water is not mentioned in the contract. Furthermore, far-reaching stabilization clauses prevalent in contracts throughout Africa frustrate the development of regulatory frameworks for sustainable water resource management. If not drafted carefully, these contracts disproportionately strengthen the position of foreign investors.

Nonetheless, the contract between the investor and the host state could and should be used to expressly limit the water use of farmland investments. It is a golden opportunity to set a fee to incentivize limited water use and to recognize the value of water. It should also provide for the right to revise those rights and fees in the event of water shortage.<sup>6</sup>

### 2.2. *International investment law*

International investment treaties further strengthen the position of foreign investors by providing additional legal guarantees and safeguards to their

rights. In times of drought and water shortages, ensuring that basic needs for water are met while maintaining water flows for sustaining river systems and biodiversity—critical for long-term sustainability of the host state—can conflict with the water needs of the farmland investments. Standard provisions in international investment treaties—like the fair and equitable treatment standard, most notably, and the prohibition against expropriation without compensation—may limit the host state's ability to reallocate water resources.<sup>7</sup> In particular, foreign investors may form a legitimate expectation for the necessary water access to maintain an agricultural production if the contract does not expressly limit water use or provide for periodic review of water allocation or access. There could also be claims of expropriation if host states reallocate water resources and encroach upon the foreign investor's right to operate the business of commercial agricultural production. The other international legal regimes described below provide considerations to counter these claims and justify any interference with foreign investor's water use.

### 2.3. *International freshwater law*

International freshwater law requires host states to respect and not to cause harm to the reasonable and equitable share of other state users, to ensure that priority water use goes to vital human needs, to notify and consult other states when a farmland investment is planned near a watercourse, and to protect and preserve water resources against pollution and overexploitation. Given the location of most farmland investments on or around international watercourses, the principles and mechanisms of the 1997 Convention on the Law of the Non-Navigational Uses of International Watercourses (the Watercourses Convention) apply to the water use of farmland investments and should be consulted when issues arise.

In most of Africa, the implementation of the Watercourses Convention has been tailored to meet specific regional and sub-regional needs. Most international watercourses in Africa are governed by their own joint institutional management scheme at the sub-regional level, a regional policy for sustainable water management and the international scheme provided by the Watercourses Convention. For example, the Southern African Development Community (SADC) has developed and effectively implemented a regional institutional framework for the sustainable management of river and lake basins in line with the Watercourses Convention principles. Where no regional mechanisms are in place, the Watercourses Convention provides the fall-back situation. Where the state concerned is not a party to the Watercourses Convention, international environmental law provides general obligations.

## 2.4. International environmental law

The International Court of Justice has recognized the duty in customary international law to conduct a transboundary environmental impact assessment if an activity is likely to result in transboundary harm, particularly on shared water resources.<sup>8</sup> The obligation applies to all states and all international water resources, not just those covered by the Watercourses Convention. This assessment should call attention to the water use of farmland investments and reveal their impact on transboundary waters. Unfortunately, it does not seem that any of these obligations has been implemented and enforced at the domestic level in Africa; they have therefore had little impact.

## 2.5. International human rights law

Numerous human rights instruments recognize the human right to water either expressly or implicitly as a fundamental prerequisite to the enjoyment of all other rights.<sup>9</sup> The UN General Assembly has recently recognized the right to water as universally binding, and the UN Human Rights Council has called on states to pay particular attention to vulnerable groups in ensuring it is guaranteed.<sup>10</sup> Accordingly, host states must ensure that the water use of farmland investments does not interfere with the vulnerable water rights of local communities, regardless of the applicable investment treaty.

## 3. Building bridges towards a holistic legal and policy framework

The principles and obligations under international freshwater, environmental and human rights law may be used as justifications or defence to claims by foreign investors in the event host states must reallocate water in the public interest. These international regimes therefore serve to counter the extensive rights and legally secured position of foreign investors under the contract and the applicable investment treaty. However, to have any impact, these regimes must be implemented and enforced, which does not seem to have yet occurred. Consequently, the first step is to implement and enforce these regimes at the domestic level.

Furthermore, existing legal mechanisms for the sustainable management of water resources should be implemented in domestic law. Water governance schemes should also be reformed to allow for increased stakeholder participation in water management decisions and to incorporate principles of integrated water resources management, giving effect to the link between water and land in the administrative framework.

Before contracting with foreign investors, host states must carefully consider their wide-ranging international obligations, particularly the duties to notify and consult other states if the investment is located near transboundary water or an international border, and

to conduct an environmental impact assessment expressly considering water use. Their contracts with investors should include specific provisions on water rights, use and fees that clearly provide for periodic revision of water allocation and rights, particularly due to environmental and human rights concerns. They should also include safeguard clauses to the effect that nothing in the contract shall impede or frustrate the implementation of host state obligations under freshwater, environmental and human rights law, to strengthen the host states' ability to reallocate water resources and undercut investor claims.

Finally, international investment treaties should include similar provisions, to ensure coherence between the investment regime and the other applicable international regimes and to preserve the host states' right and duty to manage water resources sustainably.

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### Notes

1 This article summarizes the following report: Mbengue, M. M., & Waltman, S. (2015). *Farmland investments and water rights: The legal regimes at stake*. Geneva: IISD. Retrieved from <http://www.iisd.org/publications/farmland-investments-and-water-rights-legal-regimes-stake>

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## feature 3

## Working by Design: New Ideas to Empower U.S. and European Workers in TTIP

Susan Ariel Aaronson



The 21<sup>st</sup> century has not been the best of times for U.S. and European workers. They have been buffeted by job losses, underemployment, and economic insecurity. Many individuals toil without benefits or job security.<sup>1</sup> Although workers are increasingly productive, many of them earn less than they did 20 years ago.<sup>2</sup> EU and U.S. policy-makers argue that one way to create new or better jobs is to conclude a trade and investment agreement between the United States and the 28 EU member states: the Transatlantic Trade and Investment Partnership (TTIP).

The United States and the European Union rely on longstanding templates for their trade agreements, but these templates may not adequately address the labour rights and employment issues bedeviling the workers of both trade giants. Moreover, because they rely on these templates, policy-makers may not be able to think creatively about these issues. In recognition that the debate is stuck in a rut, the Washington Office of the International Labour Organization (ILO) asked me to engage other scholars and put forward some new ideas.

This paper is organized as follows: first, I discuss how the European Union and the United States promote labour rights in trade and investment agreements. Next, I warn that language in the investment and regulatory coherence chapters may contradict the language in the labour rights chapters. Finally, I suggest ways that TTIP can be redesigned to benefit workers and promote employment, based on interviews with 23 eminent scholars as well as my own ideas.<sup>3</sup>

### 1. EU and U.S. approaches to promote labour rights

The European Union and the United States are prominent proponents of disseminating labour rights in their bilateral and multilateral free trade agreements (FTAs). Their trade agreement templates are built on the ILO core labour standards of:

- freedom of association and the effective recognition of the right to collective bargaining;

- the elimination of all forms of forced or compulsory labour;
- the effective abolition of child labour; and
- the elimination of discrimination in respect of employment and occupation.

They also include a non-derogation clause that prevents either party from weakening its labour laws and lowering its labour standards in order to attract trade or investment. Both the European Union and the United States recognize that public participation and support are essential to the success of the negotiations and the final agreement. The United States encourages public participation in the development of the labour chapter as well as comments concerning matters related to the labour chapter once in force.<sup>4</sup> The European Union recently adopted similar strategies in the Comprehensive Economic and Trade Agreement (CETA) it concluded with Canada.<sup>5</sup>

However, the European Union and the United States have different approaches to labour regulation. U.S. policy-makers believe that in general the market should determine labour market outcomes. European regulators generally believe that unregulated markets create an imbalance of power between employer and employee, so the government should regulate appropriately to empower workers, create counterweights to business, and protect labour rights.<sup>6</sup> In the United States, policy-makers view obligations on labour rights as a means of ensuring that trade and investment agreements do not undermine the rights of workers at home or within U.S. trade partners. EU policy-makers view labour rights as central to achieving sustainable development and as part of a broad set of human rights that they seek to advance through dialogue, cooperation, and capacity building. The EU and U.S. negotiating templates reflect these differences.

The two trade giants also have different strategies to encourage the dispersion of labour standards. The United States includes labour rights in a separate chapter and since May 2007 has made labour rights binding and disputable, while the European Union includes labour rights as part of its sustainable development chapter and requires both parties to effectively enforce their labour laws.<sup>7</sup>

The European Union–Canada CETA and the United States–Korea FTA, agreements in which both parties are advanced industrialized economies, provide insights into how the two trade giants might approach labour rights language in TTIP.

As before, CETA includes labour rights in its chapter on sustainable development; both parties agree to respect the ILO core conventions, and effectively implement the

ILO conventions that each party has ratified. Finally, CETA sets up a panel of experts to review alleged violations of the trade agreement. However, this review panel can only issue recommendations to the signatory nations and does not require them to respond. Hence, it creates no direct accountability to remedy the alleged violation.

The United States also did not think differently about how to address labour rights problems in Korea. The U.S. agreement with Korea (2012) includes the same core labour rights as those with Peru (2009), Colombia (2012), and Panama (2012).<sup>8</sup> But Korea is very different from those nations; although it has a strong and vibrant democracy, and high levels of unionization, the U.S. Government<sup>9</sup> and international organizations have expressed concerns about labour conditions and government willingness to effectively enforce labour rights.<sup>10</sup>

But the two trade giants seem unwilling to move beyond their templates. In fact, they may be talking past each other on labour rights. The European Union says its priority regarding labour rights is to maintain the policies EU member states have long adopted to ensure that international economic integration does not lead to domestic social disintegration. Meanwhile, the U.S. Trade Representative (USTR) states: “Our trade agreements are designed to prevent a race to the bottom on labor protections.”<sup>11</sup> The United States does not seem to be hearing European concerns that TTIP should not just prevent a race to the bottom, but it should also cushion workers from the adverse impact of trade and investment liberalization. Neither the European Union nor the United States seems to be encouraging new ideas that can help workers who feel threatened not just by globalization but also by wage stagnation, income inequality, and technologies such as robotics.

## 2. Incoherence within TTIP could undermine labour rights

Officials from both negotiating partners argue that the labour rights and sustainable development chapters illuminate their commitment to labour rights and employment issues in TTIP. But these goals cannot be successful if they are confined to one chapter rather than embedded throughout the document. Both partners have included regulatory coherence and investment chapters in recent trade agreements that could have negative labour rights and employment side effects. This section explains why negotiators must examine each chapter for coherence—to ensure that it in no way undermines or contradicts the goals of advancing labour rights and employment.

### 2.1. The regulatory coherence chapter

EU and U.S. policy-makers have long understood that domestic regulations designed to protect public health, safety, and the environment could distort trade because foreign producers may find it harder to comply with such regulations. Both negotiating partners insist

that democratically determined regulation will not be undermined by TTIP.<sup>12</sup> However, some critics argue that regulatory coherence efforts will inevitably lead to a race to the bottom<sup>13</sup> and that efforts to re-regulate domestic regulations in a trade and investment agreement are a 21st century strategy to internationalize deregulation.<sup>14</sup>

Unfortunately, policy-makers have not clarified whether labour-related regulations such as workplace health and safety regulations will be included in or excluded from the negotiations. Moreover, the United States has not ratified the same ILO conventions related to health and safety as has the European Union. U.S. workers generally have fewer protections than in much of Europe. Since the European Union and the United States have similar labour costs and productivity, some trade critics assert that EU and U.S. manufacturing firms may move their operations to venues with fewer or less costly labour-related regulations. For example, European firms could move investment to “right to work” U.S. states (where it is hard for workers to unionize), and U.S. firms could move to countries such as Romania, where labour rights are considered inadequately protected.<sup>15</sup>

### 2.2. The investment chapter

Negotiators from the United States and the European Commission want to include investor–state dispute settlement (ISDS) provisions in TTIP. These provisions are designed to encourage investment by giving investors the right to sue for compensation if their investments are expropriated by a participating government. Most investment agreements define expropriation as the direct or indirect seizure of property. However, when governments regulate, cut subsidies or slash budgets, investors may see their investments losing value, directly or indirectly as the result of such government action (“a regulatory taking”). Although the European Union and the United States have clearly stated that government regulatory policies cannot be challenged as regulatory takings, critics are not reassured.<sup>16</sup>

For example, foreign investors in Egypt challenged the establishment of minimum wages as a regulatory taking because these requirements were not in place at the time of the original investment contract. In Romania and Bulgaria, foreign investors initiated investment disputes arguing that the governments had failed to quell frequent strikes, thereby depriving the claimants of their full investment.<sup>17</sup> No investor has so far won an investment dispute on labour issues. But policy-makers have yet to clarify whether investors can challenge collective bargaining agreements or other worker protections.<sup>18</sup> Until they do, the investment chapter could pose a threat to labour rights.

## 3. Key takeaways and recommendations

The experts I interviewed felt strongly that TTIP could provide an opportunity to think differently about how policy-makers in advanced industrialized economies can protect labour rights, encourage job creation,

and empower workers. The recommendations below deserve policy-maker and public attention; they are designed to ensure that TTIP works for workers.<sup>19</sup>

*i. To enhance human welfare and empower workers:*

- Empower workers with broader human rights language and specifically expand coverage to workers in the informal sector as well as workers who are trafficked;
- Ensure that signatories are obligated to meet ILO core labour standards as a minimum;
- Encourage unions to offer cross border services such as collective representation, benefits, training, and other workplace services; and
- Experiment with allowing less skilled workers to offer services across borders.

*ii. To ensure that the agreement fully enhances labour rights and employment:*

- Consider each chapter as part of a coherent whole: review each chapter for coherence with labour and employment objectives.

*iii. To ensure that other chapters do not undermine labour rights and employment, therefore creating a dynamic of a regulatory race to the top:*

- Include specific language stating that signatories cannot use regulatory coherence chapters to reduce worker protections;
- Clarify that investors cannot use ISDS provisions to challenge minimum wages, collective bargaining agreements, procurement standards, or regulations meant to protect public health or welfare; and
- Ask the ILO to examine whether domestic tax or monetary policies in one trade partner can affect the provision of public services and human welfare in another. Policy-makers should then examine whether these provisions can and should be disciplined under trade agreements.

*iv. To improve the dispute settlement process:*

- Broaden and clarify why, how, and when signatories can engage in a trade dispute and consider other nations' approaches to investigating and improving labour rights.

*v. To develop strategies that encourage cooperative learning and collaboration:*

- Create a secretariat to research and monitor the trade agreement; provide periodic reports on how it is affecting workers and worker rights; and delineate best practices to mitigate negative effects;
- Build trust in the negotiating process with increased transparency and collaboration;
- Focus less on enforcement as a means of changing behaviour and more on collaboration; and
- Encourage greater understanding of how EU member states use social dialogue.

## Authors

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## Notes

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# news in brief

## **Binding instrument on business and human rights: Working Group holds its first session**

From July 6 to 10, 2015, a UN working group\* convened its first meeting in Geneva, Switzerland, to discuss a legal instrument on human rights and transnational corporations. The working group was established by UN Human Rights Council **Resolution A/HRC/RES/26/9**.

The inaugural session was attended by representatives of UN member and observer states, UN agencies and other intergovernmental organizations, and national human rights institutions and non-governmental organizations with consultative status at the UN Economic and Social Council. The session was also broadcasted live and archived at **UN Web TV**.

After electing Ambassador Maria Fernanda Espinosa of Ecuador as Chairperson-Rapporteur, the participants focused on the scope of coverage of the future instrument and on principles and key elements it should include, such as state obligations, legal liability of transnational corporations and other business entities, as well as national and international mechanism for access to remedies. They also acknowledged the importance of taking into account the UN Guiding Principles on Business and Human Rights as a reference point in the drafting process.

The Working Group will convene its second session in 2016. In the meantime, it will engage in informal consultations with various stakeholders.

## **European Parliament supports TTIP, but rejects current ISDS model**

On July 8, 2015, the European Parliament adopted a **non-binding resolution** guiding the European Commission on the negotiations of the Transatlantic Trade and Investment Partnership (TTIP) with the United States. The resolution generally supports TTIP—but rejects its investor–state dispute settlement (ISDS) provision.

The Parliament asked the Commission to replace the provision with a new system that is “subject to democratic principles and scrutiny” and conducted “in a transparent manner by publicly appointed, independent professional judges in public hearings.” It also called for an appellate mechanism, consistency of decisions, respect for the jurisdiction of EU and member state courts, and prevalence of public policy objectives over private interests.

For **EU Trade Commissioner Cecilia Malmström**, the resolution signalled that “the old system of [ISDS] should not and cannot be reproduced in TTIP.” She committed to flesh out the reform ideas she presented in May and to incorporate them into the TTIP.

## **Bolivia promulgates Conciliation and Arbitration Law with regime for investor–state disputes**

On June 25, 2015, Bolivian President Evo Morales promulgated Law No. 708 on Conciliation and Arbitration, approved by the Bolivian parliament with inputs from the private sector, academia and civil society. The law creates a Special Arbitration Regime for resolving investor–state disputes, particularly concerning strategic natural resources.

Bolivia’s Attorney-General Héctor Arce stated that the law guarantees the rights of both the state and domestic and foreign investors. **President Morales added** that “now no business sector can complain that Bolivia offers no legal guarantees or security.”

## **European Commission requests Member States to terminate intra-EU BITs**

On June 18, 2015, the **European Commission initiated infringement proceedings** against Austria, the Netherlands,

Romania, Slovakia and Sweden, formally requesting them to terminate their bilateral investment treaties (BITs) with other EU Member States.

According to the Commission, these treaties are out-dated and no longer necessary, since all Member States are subject to the same rules on cross-border investments, such as freedom of establishment and of capital. It indicates that the rights conferred by intra-EU BITs on a bilateral basis to investors of some Member States constitute nationality-based discrimination and are incompatible with EU law.

The five states have two months to reply to the request. While other infringement proceedings are expected, the Commission is initiating an administrative dialogue on intra-EU BIT termination with all other Member States—except for Ireland and Italy, which terminated their own in 2012 and 2013, respectively. A meeting to ensure coordinated termination will be held in October.

In parallel, the Commission plans to discuss improved investment protection within the bloc. Lord Jonathan Hill, EU Commissioner for Financial Services, Financial Stability and Capital Markets Union, stated that “the Commission is ready to explore the possibility of a mechanism for the quick and efficient mediation of investment disputes.”

## **China signs FTAs with South Korea and Australia, conducts new round of BIT negotiation with United States**

On June 1, 2015, China and South Korea signed a free trade agreement (FTA), after three years of negotiations. Chapter 12 (Investment) of the FTA updates the 2007 China–Korea BIT with key provisions, including pre- and post-establishment national treatment, minimum standard of treatment, denial of benefits, and dispute settlement.

It also establishes a Committee on Investment as a bilateral communication channel for matters arising under the FTA. Each party will also designate a national contact point to receive complaints from investors of the other party regarding administrative measures and to assist in resolving difficulties of investors of the other party.

Later, on June 17, China entered into another landmark FTA with Australia, concluding decade-long negotiations. The national treatment provision in Chapter 9 (Investment) contains asymmetrical commitments rarely seen in recently concluded treaties: Australia commits to extend national treatment for Chinese investors to pre-establishment market access, while China only agrees to post-establishment national treatment.

Traditional provisions were left out, such as standard of treatment, expropriation and transfers, leaving related commitments under the 1988 Australia–China BIT intact. However, the FTA significantly updates the dispute settlement mechanism of the 1988 BIT. The parties also agree to establish a work program to consolidate the FTA’s Investment Chapter and the BIT into a Comprehensive Investment Chapter, which will likely include provisions on minimum standard of treatment, expropriation, transfers, performance requirement, senior management and board of directors, and dispute settlement.

Meanwhile, from June 8 to 12, China and the United States conducted the 19th round of BIT negotiations in Beijing. During the negotiations, the parties discussed core issues on substantive obligations and exchanged their preliminary negative lists. Both parties agree that the BIT negotiations are still in early stages.

\* The Open-ended Intergovernmental Working Group for the Elaboration of an International Legally Binding Instrument on Transnational Corporations and Other Business Enterprises with respect to Human Rights.

# awards and decisions

## Unanimous ICSID tribunal dismisses expropriation claim due to Papua New Guinea's lack of written consent to arbitrate

*PNG Sustainable Development Program Ltd. v. Independent State of Papua New Guinea, ICSID Case No. ARB/13/33*

**Marquita Davis**

In an award dated May 5, 2015, a tribunal at the International Centre for Settlement of Investment Disputes (ICSID) dismissed PNG Sustainable Development Program Ltd.'s (PNGSDP) claim against Papua New Guinea for an alleged unlawful expropriation. It found that Papua New Guinea had not given "consent in writing" to arbitrate claims under the ICSID Convention.

### *Background and claims*

The dispute centered on PNGSDP's alleged investment in Ok Tedi, an open-pit copper and gold mine located in Papua New Guinea. PNGSDP owned a majority shareholding in the Papua New Guinean company that had a mining lease for the Ok Tedi mine.

In September 2013, Papua New Guinea adopted the Ok Tedi Tenth Supplemental Mining Agreement, which purported to cancel all shares in the Ok Tedi mine owned by PNGSDP and create new shares to be issued to the State. PNGSDP claimed the enactment of the act amounted to an unlawful expropriation without compensation, and initiated arbitration in December 2013, based on two domestic laws of Papua New Guinea: the 1992 Investment Promotion Act (IPA) and the 1992 Investment Disputes Convention Act (IDCA). It also claimed violations of the fair and equitable treatment standard, the guarantee of free transfers, the full protection and security standard, the national treatment standard, among other breaches of the two statutes.

### *Jurisdiction: did Papua New Guinea "consent in writing" to ICSID arbitration?*

The threshold issue of PNGSDP's claim was whether Papua New Guinea had given "consent in writing" to arbitration, a jurisdictional requirement under Article 25 of the ICSID Convention (para. 44). PNGSDP argued that the requirement was satisfied because IPA Article 39, either on its own or in conjunction with IDCA Article 2, constituted a standing offer by Papua New Guinea to arbitrate investment disputes under ICSID.

The relevant language of IPA Article 39 states: "The Investment Disputes Convention Act 1978, implementing the [ICSID Convention], applies, according to its terms, to disputes arising out of foreign investment" (para. 46). IDCA Article 2 states: "A dispute shall not be referred to the Centre [the International Centre for Settlement of Investment Disputes (ICSID)] unless the dispute is fundamental to the investment itself" (para. 47).

Papua New Guinea argued that neither provision constituted "consent in writing" under national or

international law standards: IPA Article 39 merely stated that the IDCA "applied, according to its terms."

The parties disagreed over what interpretive standard the tribunal should use to examine the disputed provisions.

Papua New Guinea asserted that a literal interpretation of the IPA and IDCA was appropriate under both national and international law and that it required the tribunal to examine the "grammatical and ordinary meaning of the words" (para. 52). Furthermore, it indicated that the tribunal should adopt a restrictive approach, arguing that a state's written consent to arbitrate must be "clear and unambiguous" (para. 56).

“Where domestic legislation has both national and international effects, the legislative provisions are of a ‘hybrid’ nature and, therefore, must be interpreted from a hybrid perspective, taking into account both domestic and international law. ”

PNGSDP countered that the correct interpretive approach of IPA Article 39 was the one outlined in *SPP v. Egypt*, which held that jurisdictional instruments should be interpreted "neither restrictively nor expansively, but rather objectively and in good faith" (para. 108). It invoked the *effet utile* principle of treaty interpretation, which asserts that a text should be read in such a manner that a reason and meaning can be attributed to every word in the text (para. 252). PNGSDP also offered up a "quasi-Vienna" approach, which would allow the tribunal to bring in additional interpretive factors, such as good faith, the object and purpose of Papua New Guinea's alleged unilateral declaration in its national investment legislation, the circumstances surrounding the declaration, and subsequent state conduct that might indicate its meaning. Again invoking *SPP*, PNGSDP also asserted that official investment promotion literature, most notably, the statements found on the websites of Papua New Guinea's Investment Promotion Authority and its Embassy to the United States, should be used to help interpret national investment legislation.

The tribunal sided with PNGSDP and agreed with the *SPP* decision that jurisdictional instruments should be interpreted objectively and neutrally, rather than expansively or restrictively. It determined that it was well settled that there is no presumption against a finding of jurisdiction under the ICSID Convention, and no greater requirement of proof of an agreement to

arbitrate. It concluded that the standard of proof is in most cases “the preponderance of the evidence or a balance of probabilities” (para. 255). The tribunal also “considered the legislative history of th[e] provisions and the investment promotion materials as part of the relevant context in which the legislation was adopted and understood” (para. 274).

According to the tribunal, where domestic legislation has both national and international effects, the legislative provisions are of a “hybrid” nature and, therefore, must be interpreted from a hybrid perspective, taking into account both domestic and international law. Where the two methods conflict, the international law principles will generally prevail, though it is a case-specific determination. The tribunal also agreed with PNGSDP that the *effet utile* principle of statutory construction was applicable when interpreting “hybrid” provisions. It concluded that, although a state’s interpretation of its own legislation “is unquestionably entitled to considerable weight, it cannot control the Tribunal’s decision as to its own competence” (para. 273).

After examining IDA Article 39, the tribunal concluded that the provision’s “natural and ordinary meaning is a declaration that the terms—all of the terms—of the IDCA apply to foreign investments” (para. 286). As such, Article 39 could not be credibly read to satisfy the specific requirement for written consent to ICSID jurisdiction under Article 25 of the ICSID Convention.

Turning to IDCA Article 2, the tribunal determined that the provision clearly contemplated that future consent was required for submission of claims to ICSID. It then held that there was no other provision in the IDCA that would constitute written consent to ICSID jurisdiction.

“The language of IPA Article 39 even when read together with IDCA Article 2 was insufficient to establish ‘consent in writing’ on behalf of Papua New Guinea to arbitrate claims under ICSID. ”

To interpret the provisions, the tribunal declined to use the cases provided by the parties, namely *Brandes Investment Partners v. Venezuela*, *CEMEX v. Venezuela*, *ConocoPhillips v. Venezuela and SPP v. Egypt*, because they dealt with different language in dissimilar legislative provisions, and therefore provided no material benefit to interpreting what constituted consent in writing in this case.

Although the tribunal determined that the *effet utile* principle was applicable to interpreting the provisions, it did not accept PNGSDP’s argument that IDA Article 39 should be interpreted to “trigge[r] the actual application of the ICSID Convention to this dispute” (para. 306). Though the tribunal agreed that meaning should be given to the words of states, and interpretations of treaties that would render particular meanings or provisions redundant or meaningless should be disfavored, it agreed with Papua New Guinea that *effet utile* did not authorize it to re-write legislative provisions. The party’s intent and good faith are primary, while *effet utile* “plays a subsidiary role in determining intent” (para. 307). The tribunal distinguished states’ unilateral declarations from cases involving negotiated, bilateral treaties, stating that in some cases a state’s legislation may be “merely confirmatory” (para. 309). Here, the tribunal reasoned that the objective of the IPA was to detail the state’s comprehensive legislative regime addressing foreign investments. For that reason, “recording the continued force and effect of a prior legislative enactment, for the benefit of readers (including investors and courts), serves a useful purpose” (para. 312).

As a result, the tribunal determined that the language of IPA Article 39 even when read together with IDCA Article 2 was insufficient to establish “consent in writing” on behalf of Papua New Guinea to arbitrate claims under ICSID. The tribunal dismissed the case for lack of jurisdiction and further declined to consider other jurisdictional objections. Each party was ordered to bear its own litigation costs and split the costs of arbitration.

*Notes:* The tribunal was composed of Gary Born (President appointed by the Chairman of the Administrative Council, U.S. national); Michael Pryles (claimant’s appointee, Australian national) and Duncan Kerr (respondent’s appointee, Australian national). The award is available at <http://www.italaw.com/sites/default/files/case-documents/italaw4257.pdf>.

**Government bonds not covered, despite broad definition of “investment” in Slovakia–Greece BIT; tribunal dismisses claims against Greece**  
*Poštová Banka, a.s. and Istrokapital SE v. The Hellenic Republic, ICSID Case No. ARB/13/8*  
**Martin Dietrich Brauch**

On April 9, 2015, a tribunal at the International Centre for Settlement of Investment Disputes (ICSID) dismissed for lack of jurisdiction a case against Greece related to the downgrading of Greek Government Bonds (GGBs) as a result of the economic crisis in the country.

The claimants were Poštová banka, a.s. (Poštová banka), a Slovak bank, and Istrokapital SE (Istrokapital), a company organized under Cypriot law. Poštová banka had acquired a total of €504 million in GGBs through several transactions in 2010; Istrokapital held shares in Poštová banka. The deterioration of Greece’s economy

and the downgrading of the GGBs by bond rating agencies led the claimants to initiate arbitration on May 3, 2013 under the Slovakia–Greece and Cyprus–Greece bilateral investment treaties (BITs).

#### *Greece’s jurisdictional objections*

Greece objected to the tribunal’s subject matter, personal, and temporal jurisdiction; it also maintained that the claims should be dismissed for abuse of process, and that the tribunal had no jurisdiction over the umbrella clause claims. The tribunal focused first on Greece’s two-fold objections to subject matter jurisdiction, concerning Istrokapital’s claims under the Cyprus–Greece BIT and Poštová banka’s claims under the Slovakia–Greece BIT.

#### *Istrokapital under Cyprus–Greece BIT: “indirect investment” not protected*

Istrokapital argued that it had made an indirect investment in GGBs through its shareholding in Poštová banka, and that this investment—and not its shareholding in Poštová banka—was protected under the Cyprus–Greece BIT. Greece objected to the tribunal’s jurisdiction on the grounds that Istrokapital itself did not have an investment under the Cyprus–Greece BIT and could not base jurisdiction on Poštová banka’s GGBs.

The tribunal extensively reviewed case law on whether shareholders have claims or rights in assets of companies in which they hold shares; it looked at *HICEE B.V. v. Slovakia*, *ST-AD GmbH v. Bulgaria*, *El Paso v. Argentina*, *BG v. Argentina*, *Urbaser v. Argentina*, *CMS v. Argentina*, and *Paushok v. Mongolia*. For the tribunal, these decisions established that, while “a shareholder of a company incorporated in the host State may assert claims based on measures taken against such company’s assets that impair the value of the claimant’s shares,” the shareholder does not have “standing to pursue claims directly over the assets of the local company, as it has no legal right to such assets” (para. 245).

Considering that Istrokapital had sought jurisdiction on its indirect investment, but failed to establish that it had any rights to Poštová banka’s assets protected by the BIT, the tribunal dismissed all of Istrokapital’s claims for lack of jurisdiction.

#### *Poštová banka under Slovakia–Greece BIT: the tribunal structures its approach to interpreting whether GGBs qualified as “investments”*

The parties disagreed as to how the Vienna Convention on the Law of the Treaties (VCLT) guides the interpretation of “investment” under the ICSID Convention and the Slovakia–Greece BIT, and as to whether Poštová banka’s GGBs were within the scope of those definitions of “investment.”

The tribunal first analyzed how the GGBs were issued by Greece and acquired by Poštová banka. In particular, it pointed out that Poštová banka acquired its interests in the GGBs not in their initial distribution, but on the secondary market, and that it deposited these interests with Clearstream Banking Luxembourg (Clearstream), a universal depository. It then turned to analyzing whether Poštová banka’s interests in the GGBs qualified as “investments” under Article 1(1) of the Slovakia–Greece BIT.

“Investor–State tribunals are not authorized to expand the scope of the investments that the State parties intended to protect merely because the list of protected investments in the treaty is not a closed list.”

#### *If “investment” is “every kind of asset,” does the illustrative list serve a purpose?*

The claimants understood that their interests were encompassed in the broad definition of “investment” in the *chapeau* of the Article 1(1) (“[i]nvestment means every kind of asset and in particular, though not exclusively includes: [...]”) and in the references to “loans” or “claims to money” in its section (c). They argued that “investment” has no inherent meaning under international law. Greece disagreed, maintaining that the term has an inherent meaning, and that the tribunal should not look for a special definition under the treaty.

The tribunal considered that, while the definition of “investment” under the BIT was broad (“every kind of asset”), this meant neither that all categories qualified as an “investment” nor that the only way to exclude a category would be an express exclusion. It held that “investor–State tribunals are [not] authorized to expand the scope of the investments that the State parties intended to protect merely because the list of protected investments in the treaty is not a closed list” (para. 288).

While observing that several treaties include broad asset-based definitions of “investment,” the list of categories that illustrate what may constitute an investment can vary significantly. To interpret the treaty in good faith—considering its text, context, object, and purpose, as required by the VCLT—the tribunal understood that it should interpret the list of examples under the “investment” definition without making the list useless or meaningless.

The tribunal also looked to case law to support its conclusion. It found that the decisions in *Fedax v. Venezuela*, *Abaclat v. Argentina* and *Ambiente Ufficio v. Argentina* “have consistently considered the text of the list of categories that may constitute an investment as a definitive element to determine whether the activity or operation at stake may be considered an investment” (para. 303).

*Are GGBs “investments” under any of the categories of the illustrative list?*

The tribunal set out to determine whether Poštová banka’s interests in GGBs fit within the categories of investments listed in the BIT. It started from the premise—undisputed by the parties—that GGBs constitute sovereign debt, which cannot be equated to private debt, as well as securities in the form of bonds, which are subject to specific and strict regulation.

It then noted that none “[n]either Article 1(1) of the Slovakia–Greece BIT nor other provisions of the treaty refer, in any way, to sovereign debt, public titles, public securities, public obligations or the like” (para. 332). The only reference to bonds, under Article 1(1) (b), is limited to bonds issued by private companies (“debentures”). The tribunal agreed with Greece that the exclusion of sovereign bonds from the definition of “investment” indicates that the contracting parties did not intend to cover them as investments.

The claimants had proposed that GGBs fit within a wide interpretation of Article 1(1)(c), which refers to “loans, claims to money or to any performance under contract having a financial value.”

The tribunal disagreed that GGBs could be considered loans, because of the distinction between loans and bonds. Loans generally have identified creditors and limited tradability, are not subject to securities regulations, and involve a contractual relationship between lender and the ultimate debtor. In turn, bonds are generally held by large groups of anonymous creditors, have high tradability, are subject to restrictions and regulations, and involve a contractual relationship between the holder and the intermediaries (not with the ultimate debtor). The facts of the case emphasized the relevance of the distinction: Poštová banka was able to trade the GGBs fast, and had a direct contractual relationship not with Greece, the ultimate debtor, but with Clearstream, the intermediary from which it had acquired GGBs.

The claimants had also wanted to include GGBs within “claims to money” under Article 1(1)(c). The tribunal again disagreed. First, it explained that it should not lightly expand treaty language to interpret a general reference to “claims to money” as including government bonds. Second, looking at the context—“claims to money or to any performance *under contract having a financial value*”—the tribunal held

that any claim to money, to fall within the definition, must arise from a contract with the respondent. This was not the case, given that Poštová banka did not have a contract with Greece.

*Dismissal and costs*

Concluding that neither of the claimants had an “investment” within the meaning of the relevant BITs, the tribunal dismissed the case for lack of jurisdiction, and considered it unnecessary to examine Greece’s other objections.

Even ruling in favour of Greece, the tribunal noted that “the jurisdictional issue was not clear-cut and involved a complex factual and legal background” (para. 377), and ordered each party to bear its own legal costs and an equal share of the arbitration costs.

*Notes:* The ICSID tribunal was composed of Eduardo Zuleta (President appointed by the Secretary-General of ICSID, Colombian national), John M. Townsend, (claimant’s appointee, U.S. national) and Brigitte Stern (respondent’s appointee, French national). The award is available at <http://www.italaw.com/sites/default/files/case-documents/italaw4238.pdf>.

**Looking to Venezuela’s Investment Law, majority finds that Venoklim was not a foreign investor and dismisses case against Venezuela; claimant-appointed arbitrator dissents**

*Venoklim Holding B.V. v. Bolivarian Republic of Venezuela*, ICSID Case No. ARB/12/22

**Martin Dietrich Brauch**

The majority of a tribunal at the International Centre for Settlement of Investment Disputes (ICSID) dismissed an expropriation case against Venezuela on jurisdictional grounds, finding that the investor did not qualify as a foreign national under Venezuela’s Investment Law. The award was rendered on April 3, 2015.

*Background and decision to bifurcate*

By Decree No. 7712 of 2010, Venezuela ordered the forced acquisition of the assets of five companies owned and controlled by Venoklim Holding B.V. (Venoklim), incorporated in the Netherlands. According to the Decree, the acquisition would be essential for Venezuela’s autonomy in the production of certain lubricants.

Based on Venezuela’s Investment Law and the ICSID Convention, Venoklim initiated arbitration in July 2012 on expropriation claims. It was only in September 2013, when presenting its counter-memorial to Venezuela’s jurisdictional objections, that Venoklim expressly referred to the Venezuela–Netherlands bilateral investment treaty (BIT). The tribunal decided to bifurcate the arbitration, dealing first with Venezuela’s jurisdictional objections and leaving the matters for a later stage.



*Venezuela's denunciation of the ICSID Convention effective after six months*

Recalling that it denounced the ICSID Convention on January 24, 2012, Venezuela argued that the tribunal did not have personal jurisdiction. It read ICSID Convention Article 72 to mean that valid consent would only exist if the arbitration request had been received before the notice of denunciation. In response, Venoklim maintained that, under ICSID Convention Article 71, Venezuela's denunciation would only be effective six months after receipt of the notice of denunciation, and pointed out that the arbitration was initiated before the six months lapsed.

The tribunal rejected the objection, disagreeing with Venezuela's interpretation of Article 72. According to the tribunal, this interpretation would give Venezuela's denunciation immediate effect, disregarding the six-month period provided for by Article 71. It would also violate the principle of legal security, to the detriment of investors.

*Date when the arbitration request is presented—not registered by ICSID—is the relevant date to establish investor's consent*

Venezuela objected that, when the dispute was registered on August 15, 2012 and the proceeding began, it was no longer a party to the ICSID Convention, even considering the six-month period under Article 71. For Venoklim, however, the registration of the dispute by the ICSID Secretariat is a mere administrative measure, and consent had already been perfected when the request was presented on July 23, 2012. The tribunal sided with Venoklim, concluding that the relevant date for establishing jurisdiction is the date when the investor gives consent by presenting the request, not the date when ICSID registers it.

*Venezuela's Investment Law is not an independent basis for ICSID jurisdiction*

Venezuela argued that Article 22 of its Investment Law is not an open and general offer to arbitrate, based on the provision's ordinary meaning, on political declarations made when the law was enacted, and on comparisons between the provision and offers to arbitrate contained in Venezuelan BITs and in ICSID model clauses. According to Venoklim, the provision implicitly incorporates the BIT and constitutes an independent jurisdictional basis.

After it analyzed the spirit, context and purpose of the provision and the circumstances under which it was drafted, the tribunal concluded that the provision served to confirm Venezuela's offers to arbitrate made under other legal instruments, such as BITs—but could not be considered an "independent, clear and general" offer to arbitrate (para. 104). Accordingly, it dismissed the objection, in line with earlier ICSID decisions in the *Mobil*, *Cemex*, *Brandes*, *Tidewater*, *OPIC* and *ConocoPhillips* cases.

*BIT not an independent jurisdictional basis—but incorporated by indirect reference in Venezuela's Investment Law*

Venezuela claimed that the late invocation of the BIT—not in the request, but later, in the counter-memorial—breached the ICSID Convention and procedural rules, which require that the request must present all the elements necessary to establish jurisdiction.

The tribunal agreed with the investor that there was no late invocation. It reasoned that the counter-memorial merely explained and elaborated on the jurisdictional basis presented in the request—the Investment Law. Article 22 of the Investment Law refers to international arbitration provided for in investment treaties generally. Since Venoklim claimed to be a Dutch investor, the tribunal held that the reference to investment treaties in Venezuela's law should be read, in this case, as a reference to the Venezuela–Netherlands BIT.

*Adopting the effective control criterion under the Investment Law, tribunal finds that Venoklim is not a foreign investor*

To demonstrate its foreign nationality, Venoklim invoked the incorporation criterion (referred to in the BIT), but Venezuela argued that the effective control criterion (referred to in the Investment Law) should be used instead. According to Venezuela, the effective control over Venoklim ultimately lay with a Venezuelan company. Therefore, the investor could not be considered foreign nationals under the ICSID Convention, the Investment Law or the BIT.

The majority of the tribunal emphasized that Venoklim needed to fulfill the requirements of Article 22 of the Investment Law to benefit from the BIT, as well as to prove its foreign nationality under the ICSID Convention.

Analyzing Article 22, the majority noted that the provision refers to "ownership" and "control," but not "incorporation," as the relevant criteria to determine nationality. Therefore, it held that the investor's place of incorporation was irrelevant in this determination and, given that the parties had not discussed ownership, it focused on analyzing the control criterion. In this analysis, it found that Venoklim was indeed controlled by a Venezuelan company, which in turn was owned and controlled by Venezuelan nationals.

Finding that Venoklim did not qualify as a foreign investor under Article 22, the majority held that the investor was not entitled to the protections of the provision and, as a consequence, could not benefit from the protections of the BIT either. Accordingly, the majority of the tribunal dismissed the case for lack of jurisdiction.

Briefly analyzing the ICSID Convention, the majority reasoned that to look solely at Venoklim's incorporation in the Netherlands to consider it a foreign investor, even though the investment was ultimately owned by

Venezuelans, “would be to allow formalism to prevail over reality and to betray the object and purpose of the ICSID Convention” (para. 156).

According to arbitrator Enrique Gómez Pinzón, the majority was mistaken to analyze the investor’s nationality based on the Investment Law. Given the earlier conclusion that Article 22 could not be considered an “independent, clear and general” offer to arbitrate, but merely confirmed Venezuela’s commitments under investment treaties, he argued that the investor should have been subjected to the nationality requirements of the BIT.

The dissenting arbitrator also disagreed with the majority’s interpretation of the nationality requirements under the ICSID Convention. According to him, the ICSID Convention is silent on a definition of nationality to give the contracting parties leeway to choose a nationality criterion in more specific instruments. In the Venezuela–Netherlands BIT, the two contracting parties chose “incorporation” as the applicable criterion, but the majority disregarded that choice. He also criticized the majority’s decision to pierce Venoklim’s corporate veil without a detailed analysis of whether its incorporation in the Netherlands had been fraudulent or done to evade legal requirements or to harm the shareholders or third parties.

*Case dismissed—but Venezuela ordered to cover half of arbitration costs and own legal fees*

Even though Venezuela demonstrated that Venoklim was not a foreign investor, leading to a dismissal on jurisdictional grounds, the tribunal reasoned that, since most of Venezuela’s jurisdictional objections were rejected and since Venoklim acted correctly throughout the proceedings, “it would be unfair” (para. 163) for Venoklim to bear all costs. Accordingly, the tribunal ordered Venezuela to bear half of the arbitration costs, including the arbitrators’ fees, and ordered each party to cover its own legal fees and expenses.

*Notes:* The ICSID tribunal was composed of Yves Derains (President appointed by the Chairman of the Administrative Council, French national), Enrique Gómez Pinzón, (claimant’s appointee, Colombian national) and Rodrigo Oreamuno Blanco (respondent’s appointee, Costa Rican national). The award is available, in Spanish only, at <http://www.italaw.com/sites/default/files/case-documents/italaw4229.pdf>; the concurring and dissenting opinion, also in Spanish only, at <http://www.italaw.com/sites/default/files/case-documents/italaw4230.pdf>.

**Majority of ICSID tribunal finds no fair and equitable treatment violation by Albania in petroleum dispute Mamidoil Jetoil Greek Petroleum Products Societe S.A. v. The Republic of Albania, ICSID Case No. ARB/11/24 Matthew Levine**

An arbitration between a Greek petroleum products firm and the Republic of Albania has reached the award stage at the International Centre for Settlement of Investment Disputes (ICSID). The ICSID tribunal found

jurisdiction under the 1991 Greece–Albania bilateral investment treaty (BIT).

The tribunal unanimously dismissed the investor’s claim in relation to a purported indirect expropriation. A majority of the tribunal dismissed the investor’s claim that Albania had failed to provide fair and equitable treatment (FET); however, the claimant’s nominated arbitrator found Albania’s conduct to breach the FET standard.

### *Background*

Mamidoil Jetoil Greek Petroleum Products Societe S.A. (Mamidoil) is a corporation organized and existing under the laws of Greece. From 1991 onwards, Mamidoil explored various commercial opportunities in Albania related to its major business activities, namely, the transport, storage and sale of petroleum products.

Mamidoil eventually settled on the construction and operation of an oil tank farm in the Durrës port area (Durrës Tank Farm), which led to a series of increasingly substantial investments in 1999 and 2000. During this period, local government officials sent a series of letters related to Mamidoil’s failure to obtain permits. The Durrës Tank Farm is situated close to a residential area.

The claimant substantially finished the construction of the Durrës Tank Farm by 2000. Subsequently concerns arose regarding the social impact of the tank farm, and the Albanian government embraced, in tandem with the World Bank and the European Union, re-zoning proposals that would relocate Durrës. Albania contended that an eventual ban on fuel vessels at Durrës was part of its long-term transport sector strategy as part of the necessary modernization of its port system.

“To look solely at Venoklim’s incorporation in the Netherlands to consider it a foreign investor, even though it was ultimately owned by Venezuelans, ‘would be to allow formalism to prevail over reality and to betray the object and purpose of the ICSID Convention’.”

Mamidoil contended that Albania encouraged it to invest in the country. Albania did not contest that it provided some support to Mamidoil, but contended that this was purely provisional and high level.

*Business activities considered as unitary investment for purposes of jurisdiction*

Albania had argued that “the composite parts of the investment form a whole and must be considered together”

(para. 364). The tribunal agreed that construction of the Durrës Tank Farm, establishment of an Albanian subsidiary that was first controlled and later wholly owned by the claimant, conclusion of a Durrës-related lease by the subsidiary, and operation of Durrës by the subsidiary must be considered as constituting a single investment.

As the tribunal agreed with Albania that the investment be considered as a unity, it was not persuaded by Albania's argument that certain elements of the investment failed to fulfill the ICSID Convention's criterion for a covered investment. Rather, it found that the investor's business activities clearly constituted an investment under the ICSID Convention.

Albania also objected on the basis of illegality, arguing that the investor had failed to obtain required permits. The tribunal found this more relevant to the merits stage: as Albania had informed the investor that it was ready to consider curing the illegalities, it could be expected to accept jurisdiction. (However, the majority subsequently found that without such permits the investor could have no legitimate expectation of proceeding with the investment and that the claim for breach of FET, among other claims, must be rejected.)

#### *Energy Charter Treaty invoked at pleadings stage*

In its Request for Arbitration, the claimant based its claim exclusively on the BIT and the ICSID Convention. The claimant's memorial, however, subsequently asserted that the respondent's consent to ICSID arbitration of the dispute was also found in the Energy Charter Treaty (ECT).

The tribunal rejected the ECT as applicable law, but took into account the legitimate disagreement between the parties as to whether the investment had been made illegally and therefore could not benefit from the protection of the ECT. In concluding its discussion of this complication, the tribunal noted that, "to the extent the Parties both took positions as to the propriety of the Respondent's conduct under the ECT, for this reason alone the Tribunal will consider the ECT when addressing the existence and legality of an investment under each of the BIT and the ECT and Respondent's compliance with both the BIT and the ECT." (para. 278).

#### *Indirect expropriation claim is unanimously dismissed*

The claimant submitted that Albania had indirectly expropriated its investment under both under the BIT and the ECT. It relied on the following key facts: in June 2000, Durrës was re-zoned to exclude the investment; in July 2000, the investor was ordered to suspend construction of the tank farm, which was subsequently re-authorized; and, as of July 2009, Durrës was closed to petroleum vessels.

The tribunal disagreed, finding that re-zoning was transportation policy and that in any case the claimant had been allowed to operate profitably until the port was closed in 2009. It pointed out that "[r]egulations that

reduce the profitability of an investment but do not shut it down completely and leave the investor in control will generally not qualify as indirect expropriations" (para. 572), referencing *El Paso v. Argentina*.

#### *Majority dismisses FET- and discrimination-based claims*

The majority (Rolf Knieper and Yas Banifatemi) noted that Albania's recent history—"a highly repressive and isolationist communist regime" followed by "a severe economic financial crisis" (para. 625)—was relevant to the FET obligation under the BIT, especially the obligation to provide a stable and transparent legal framework. For the majority, Mamidoil knew that Albania was a country with run down infrastructure and a problematic legal and regulatory framework, and could not therefore legitimately expect the same stability as in other jurisdictions.

“For the majority, Mamidoil knew that Albania was a country with run down infrastructure and a problematic legal and regulatory framework, and could not legitimately expect the same stability as in other jurisdictions.”

In terms of unreasonable and discriminatory measures, for the majority "the State's conduct bore a reasonable relationship to some rational policy. [...] Finally, the closure did not favour a local competitor because it concerned all importers of petroleum products" (para. 791).

#### *Dissenting arbitrator finds violation of FET standard*

The dissenting arbitrator (Stephen Hammond) disagreed with the majority's conclusion that Albania provided fair and equitable treatment. The dissent disagreed with several important factual findings in the award, for example, that the claimant was aware that transformation of the port was imminent when it began construction of the tank farm.

The dissent also disagreed with the legal implications of continued construction after notification of imminent re-zoning. Citing the award in *MTD v. Chile*, it suggested that this was a mere failure to mitigate and could not result in a forfeiture of treaty rights. In terms of legitimate expectations specifically, the dissent found that the relevant time for determination of whether legitimate expectations had been created was the moment when the decision to invest was made.

#### *Dissent finds violation of Energy Charter's prohibition on unreasonable and discriminatory measures*

The dissent found that Albania's ban of fuel vessels at Durrës resulted in a failure to accord fair and equitable

treatment and also constituted a breach of the ECT's prohibition on unreasonable and discriminatory measures. While Albania maintained that its decision to ban fuel tankers at Durrës was based on public policy considerations, Mamidoil contended that it was instead driven by the need to settle another arbitration, this time under contract at the International Chamber of Commerce in Paris. Mr. Hammond agreed that the available documents showed the ban to have been triggered by Albania's settlement agreement. (The majority had found in the award that the settlement agreement reiterated the government's policy objectives.)

*Notes:* The tribunal was composed of Rolf Knieper (President appointed by the Chairman of the ICSID Administrative Counsel, German national), Stephen A. Hammond (claimant's appointee, U.S. national), and Yas Banifatemi (respondent's appointee, French national). The final award of March 30, 2015 is available at <http://www.italaw.com/sites/default/files/case-documents/italaw4228.pdf>. The dissenting opinion of March 20, 2015 is available at <http://www.italaw.com/sites/default/files/case-documents/italaw4235.pdf>.

### Tribunal found Mongolia liable for unlawful expropriation and awarded more than US\$80 million in damages

*Khan Resources Inc., Khan Resources B.V. and CAUC Holding Company Ltd. v. The Government of Mongolia and MonAtom LLC, PCA Case No. 2011-09*

**Joe Zhang**

In an award dated March 2, 2015, a tribunal under the arbitration rules of the UN Commission on International Trade Law (UNCITRAL) found Mongolia illegally expropriated the assets of foreign investors in breach of its Foreign Investment Law and the Energy Charter Treaty (ECT). The claimants were awarded compensation of US\$80 million plus interest and costs.

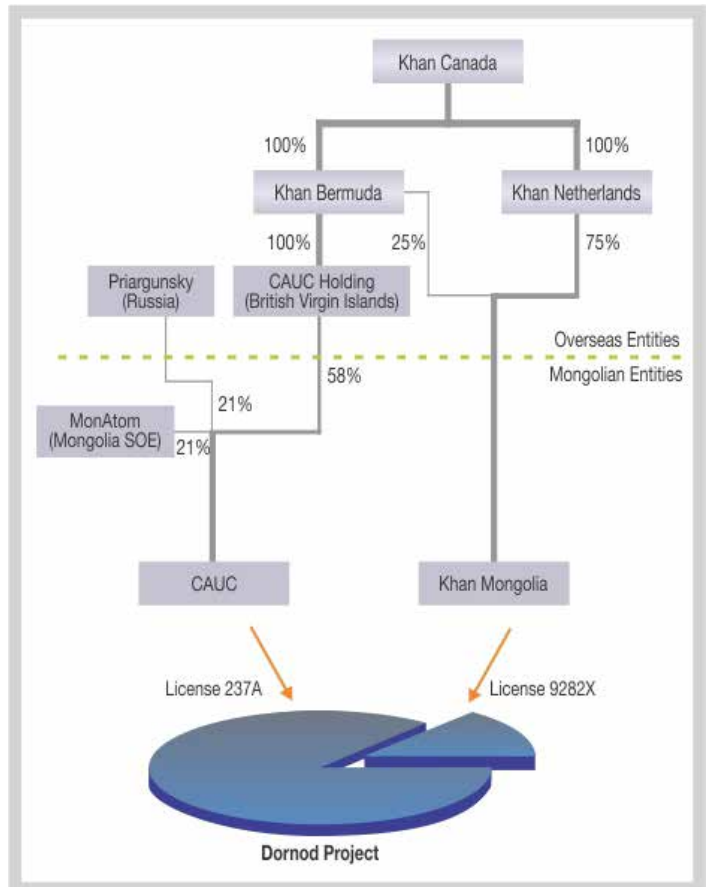
#### *The claimants and the project*

The arbitration was brought by three claimants for their investment in a uranium exploration and extraction project in the Mongolian province of Dornod (the Dornod Project). The claimants were (1) CAUC Holding Company Ltd (CAUC Holding), a British Virgin Islands (BVI) company investing in the Dornod Project through its majority-owned Mongolian subsidiary Central Asian Uranium Company (CAUC); (2) Kahn Resources B.V. (Kahn Netherlands), a Dutch company investing in the Dornod Project through its fully-owned Mongolian subsidiary Khan Resources LLC (Kahn Mongolia); and (3) Kahn Resources Inc. (Kahn Canada), a Canadian company that wholly owns both CAUC Holding, through a Bermuda vehicle, and Kahn Netherlands.

CAUC operated in the Dornod Project under a mining license (License 237A) what initially covered two deposits, but which later, on CAUC's application, was reduced to exclude a segment aimed at tax and fee savings. Such

excluded segment was later acquired by Kahn Mongolia and covered by a separate mining license (License 9282X).

The figure below illustrates the ownership structure of the companies involved immediately before the disputes arose.



#### *The disputes*

In 2009, as part of its nuclear energy reform, Mongolia enacted a Nuclear Energy Law (NEL) and established a Nuclear Energy Agency (NEA). In October 2009, NEA issued Decree No. 141, which suspended 149 uranium exploration and exploitation licenses, including Licenses 237A and 9282X, pending confirmation from NEA of their re-registration under the NEL. In March 2010, NEA inspected the Dornod Project site, noting that the project failed to remedy certain previously identified violations of Mongolian law and listing further breaches. In April 2010, NEA invalidated both mining licenses, and declared later that year that it would not re-register to the claimants.

The claimants initiated the arbitration in 2011, relying on three different instruments. Khan Canada and CAUC Holding invoked the arbitration clause of the joint venture agreement that created CAUC (Founding Agreement), claiming the suspension and invalidation of the licenses constituted an unlawful expropriation, in breach of Mongolia's obligations under the Founding Agreement, Mongolian law (including the Foreign Investment Law), and customary international law. Khan

Netherlands relied solely on the ECT, claiming that, by violating the Foreign Investment Law, Mongolia also breached its commitment under the ECT through the operation of the treaty's umbrella clause.

#### *Jurisdictional challenges*

In a separate Decision on Jurisdiction issued on July 25, 2012, the tribunal had ruled on several jurisdictional challenges raised by Mongolia.

#### *Non-signatory becomes "real party" to the arbitration clause by "common intention"*

Mongolia objected to the tribunal's personal jurisdiction over Khan Canada, which was not a party to the Founding Agreement. While noting that the Canadian compliant was indeed not a signatory, the tribunal held that a non-signatory could become a "real party" to the agreement if this was the common intention of the signatory and non-signatory parties. The tribunal found such common intention based on evidence that Khan Canada had assisted CAUC Holding in performing its financial obligations under the Founding Agreement and that various non-official exchanges had in some occasions referred to Khan Canada, instead of its BVI subsidiary CAUC Holding, as one of the shareholders of CAUC.

#### *Sovereign commitment made by state-owned enterprise binding on Mongolia*

Mongolia further argued that it should not be bound by the arbitration clause of the Founding Agreement, to which it was not a party. Relying on testimony provided by the claimants' legal expert, the tribunal found that one of CAUC's shareholders, MonAtom, a Mongolian company wholly owned by the state, acted as Mongolia's representative and undertook obligations that only a sovereign state could fulfill, namely, committing to reduce the natural resource utilization fees to be paid by CAUC, thereby giving the tribunal personal jurisdiction over Mongolia under the Founding Agreement.

#### *Broad arbitration clause opens door to claims based on contract, domestic law and customary international law*

Mongolia also disputed the tribunal's subject matter jurisdiction over the claims under the Founding Agreement. However, the tribunal found the broadly drafted arbitration clause of the Founding Agreement covered all claims raised, including claims to breaches of domestic law and customary international law, as they were all sufficiently connected to the Founding Agreement.

#### *Denial of benefits clause of the ECT must be actively exercised before the commencement of arbitration*

In terms of the claims raised by Khan Netherlands under the ECT, Mongolia argued that these claims were barred, as ECT Article 17(1) allowed it to deny treaty benefits to investors with "no substantial business activities"

in the home state. The tribunal began its analysis of the issue by noting that this was a question of merit, not jurisdiction, as Article 17(1) only concerned Part III (Investment Promotion and Protection) of the ECT, not its Dispute Settlement Chapter (Part V). Even so, the tribunal went on and discussed (a) whether Article 17(1) constituted an automatic denial of benefits and, (b) if not, whether the right to deny benefits may be exercised after the commencement of arbitration. The tribunal largely followed the decisions in *Yukos v. Russia and Plama v. Bulgaria*, considering it had "a duty to take account of these decisions, in the hope of contributing to the formation of a consistent interpretation of the ECT capable of enhancing the ability of investors to predict the investment protection which they can expect to benefit from under the Treaty" (Decision on Jurisdiction, para. 417). The tribunal held that a state must actively exercise its right under ECT Article 17(1), and that such active exercise must be in time to give adequate notice to investors, so there would be no lack of certainty to "impede the investor's ability to evaluate whether or not to make an investment in any particular state" (Decision on Jurisdiction, para. 426).

#### *Unlawful expropriation claims*

A large portion of the tribunal's analysis on the merits was devoted to the claims of unlawful expropriation, that is, whether the invalidation of the mining licenses and failure to re-register them constituted an unlawful expropriation under Mongolia's Foreign Investment Law.

#### *Tribunal disagrees with Mongolia on the interpretation of Mongolian law*

Mongolia first argued that the mining licenses were not covered investments under its Foreign Investment Law, which defined "foreign investment" as "every type of tangible and intangible property." Mongolia further argued that mining licenses were not property under Mongolian law, as a decision of the Mongolian Supreme Court has held that "[a] mining license [...] is possessed but not owned by any entity, and therefore there is no legal ground to consider such mining license to be a property right which is transferable to the ownership of others" (Award on the Merits, para. 303).

Noting there was a "general notion the rights under licenses (as well as contractual rights) to exploit natural resources constitute intangible property" (Award on the Merits, para. 302), the tribunal disagreed with Mongolia's interpretation of its laws and its Supreme Court decision, and found Mongolia failed to convince it to "depart from the general notion" (Award on the Merits, para. 307).

#### *Tribunal looks at substantive and procedural aspect of the expropriation claims*

In its analysis of whether an unlawful expropriation had occurred, the tribunal first noted there were two types of expropriation under Mongolian Law. A *khuraakh* takes

place when a state deprives the owner of his property due to legal breaches or to the use of the property in a manner that endangers the interests of third parties. A *daichlakh* is a state-ordered deprivation of property where necessary to satisfy an important public need. Given the facts of the case, the tribunal found the invalidation of the licenses and failure to re-register them must be analyzed as a *khuraakh* under Mongolian law (Award on the Merits, paras. 313–317). Relying on the testimony of the claimants’ legal expert, the tribunal held that, for the *khuraakh* to have been lawful, (a) it must have had a legal basis and (b) it must have been carried out in accordance with due process of law.

The tribunal first looked at whether Mongolia had a legal basis for the invalidation of the licenses. Disagreeing with Mongolia, it did not find that the claimants breached Mongolian law. After a proportionality analysis, it concluded that the invalidation of the licenses was not an appropriate penalty, even if the alleged violations had existed. Therefore, the tribunal found Mongolia failed to “point to any breaches of Mongolian law that would justify the decisions to invalidate and not re-register” the mining licenses (Award on the Merits, para. 319). Further, it found, based on evidence presented by the claimants, that the alleged breaches were pretexts for Mongolia’s real motive to “[develop] the Dornod deposits at greater profit with a Russian partner” (Award on the Merits, para. 340).

“The tribunal disagreed with Mongolia’s interpretation of its laws and its Supreme Court decision, and found Mongolia failed to convince it to “depart from the general notion” that contractual rights to exploit natural resources constitute intangible property. ”

Turning to the procedural requirement, the tribunal found that the claimants were denied due process of law. In particular, it found Mongolia had an obligation to re-register the mining licenses as there was “no legally significant reason why the Claimants would not have fulfilled the [prescribed] application requirements” (Award on the Merits, paras. 350, 358). The tribunal further found that, since the mining licenses were never re-registered under the newly enacted NEL, the invalidation procedure provided in the NEL would not apply to those mining licenses, and NEA did not have authority to invalidate the licenses unless they were re-registered under the NEL (Award on the Merits, paras. 352–365).

### *Mongolia breached ECT by operation of umbrella clause*

After concluding that Mongolia “breached its obligation under the Foreign Investment Law” (Award on the Merits, para. 366), the tribunal swiftly found Mongolia also liable toward Khan Netherlands under the ECT through operation of the umbrella clause (Award on the Merits, para. 366). It cited to its Decision on Jurisdiction, which had held that “a breach by Mongolia of any obligations it may have under the Foreign Investment Law would constitute a breach of the provisions of Part III of the [ECT]” (Decision on Jurisdiction, para. 438).

### *Damages*

In calculating the damages, the tribunal rejected traditional methodologies proposed by the parties and decided to value the investment analyzing three offers received between 2005 and 2010 to purchase the Dornod Project, thus reaching a final amount of US\$80 million in damages. The tribunal also awarded interest at a rate of LIBOR plus 2 per cent compounded annually from July 1, 2009 (the date of valuation) until the date of payment. In addition, the tribunal awarded the claimants legal fees and costs of US\$9.07 million, including a “success fee” based on the contingent fee arrangement between the claimants and their counsel.

*Notes:* The Tribunal was composed of David A. R. Williams (President appointed by the agreement of co-arbitrators, New Zealander national), L. Yves Fortier (claimants’ appointee, Canadian national), and Bernard Hanotiau (respondents’ appointee, Belgian national). The Decision on Jurisdiction is available at <http://www.italaw.com/sites/default/files/case-documents/italaw4268.pdf>. The Award on the Merits is available at <http://www.italaw.com/sites/default/files/case-documents/italaw4267.pdf>.

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# resources and events

## Resources

### **The Origins of International Investment Law: Empire, environment and the safeguarding of capital** By Kate Miles, Published by Cambridge University Press, July 2015

This book examines the historical evolution of international investment law (IIL), from its origins in the commercial and political expansionism of dominant states during the 17<sup>th</sup> to early 20<sup>th</sup> centuries to the continued resonance of those origins within modern IIL. An overview of the activities of the Dutch East India Company, Grotius' treatises, and pre-World War II international investment disputes provides insight into current controversies surrounding the interplay of public and private interests, the systemic design of investor-state arbitration, the substantive focus of principles, and the treatment of environmental issues within IIL. The book provides a conceptual framework, new understandings, an assessment on trends in investment law and policy, and practical measures for reform. Available at <http://www.cambridge.org/br/academic/subjects/law/arbitration-dispute-resolution-and-mediation/origins-international-investment-law-empire-environment-and-safeguarding-capital>

### **Investment Contracts for Agriculture: Maximizing gains and minimizing risks**

By Carin Smaller and William Speller, with Hafiz Mirza, Nathalie Bernasconi-Osterwalder and Grahame Dixie, Published by the World Bank, United Nations Conference on Trade and Development (UNCTAD), and IISD, June 2015

Private investment in agriculture in developing countries, both domestic and foreign, has been on the rise for nearly two decades. The paper focuses on large-scale agricultural projects in developing countries, involving the lease of farmland. It marries two substantial bodies of research to show how investment contracts can be set up to promote sustainable development. The paper presents the top five positive outcomes and the five downsides from private sector investments in large-scale agricultural projects. The paper then proposes legal options to maximizing the main positive outcomes and minimizing the main downsides through better drafting of contracts between investors and governments for the lease of farmland. This paper contributes to the growing body of international norms and guidance on the conduct of responsible agricultural investment, such as the recently adopted Principles for Responsible Investment in Agriculture and Food Systems, of the UN Committee on World Food Security (CFS). Available at <http://www.iisd.org/publications/investment-contracts-agriculture-maximizing-gains-and-minimizing-risks>

### **World Investment Report (WIR) 2015: Reforming international investment governance** By UNCTAD, June 2015

The WIR presents global investment trends in 2014, indicating that global foreign direct investment (FDI) inflows fell by 16 per cent to US\$1.23 trillion. FDI flows to developed countries continued to be low, while flows to developing countries increased by 2 per cent to a historic high of US\$681 billion, with China as the largest recipient. FDI inflows to Asia increased by 9 per cent to historically high levels, while inflows to Africa remained flat, and inflows to Latin America and the Caribbean decreased by 14 per cent. In the policy realm, government measures continued to be geared towards liberalization, promotion and facilitation. There were relatively few measures for investment in sectors important for sustainable development. The search for reform of the international investment regime continued, as at least 50 countries and regions conducted reviews of their treaty models. The number of investor-state arbitration cases rose by 42 in 2014, bringing the total number to 608. Decisions were rendered in 43 cases, bringing the number of concluded cases to 405. Recognizing the need for systematic reform, UNCTAD suggests focusing on: (1) safeguarding the right to regulate in the public interest, (2) reforming investment dispute

settlement, (3) promoting and facilitating investment, (4) ensuring responsible investment, and (5) enhancing the systemic consistency of the regime; the report also presents policy options for meeting these challenges. Finally, the WIR discusses international tax and investment policy coherence, the fiscal contribution of multinational enterprises, and the issue of tax avoidance. Available at <http://unctad.org/en/pages/PublicationWebflyer.aspx?publicationid=1245>

### **Farmland Investments and Water Rights: The legal regimes at stake**

By Makane Moïse Mbengue and Susanna Waltman, Published by IISD, May 2015

The rise of foreign investment in farmland over the past decade is partly driven by a search for access to water resources. Land without water has no value; it is the key ingredient for agricultural production. Over 70 per cent of all freshwater resources are used for agricultural production. However, the value of water has yet to be fully understood or appreciated, and its fundamental role is often overlooked in the context of farmland investments. This report, focused on Africa, provides an overview of the international legal regimes governing water rights and investment in land and the implications for foreign investors, governments and communities. Available at <http://www.iisd.org/publications/farmland-investments-and-water-rights-legal-regimes-stake>

## Events 2015

### September 8

**BIICL SHORT TRAINING COURSE: HUMAN RIGHTS FOR BUSINESS PEOPLE**, British Institute of International and Comparative Law, London, United Kingdom, <http://www.biicl.org/event/1115>

### September 18

**25<sup>TH</sup> INVESTMENT TREATY FORUM (ITF) PUBLIC CONFERENCE: THE ICSID CONVENTION AT 50**, British Institute of International and Comparative Law, at BMA House, London, United Kingdom, <http://www.biicl.org/event/1117>

### September 21-22

**WORKSHOP ON STRENGTHENING TECHNICAL ASSISTANCE FOR RESOURCE-RICH AFRICAN COUNTRIES**, Columbia Center for Sustainable Investment, African Legal Support Facility, African Minerals Development Centre, and New Partnership for Africa's Development, Pretoria, South Africa, <http://ccsi.columbia.edu/2015/09/21/september-workshop-on-strengthening-technical-assistance-for-resource-rich-african-countries>

### September 25

**CIDS INTERNATIONAL CONFERENCE 2015: INTERNATIONAL DISPUTE SETTLEMENT AT THE CROSSROADS OF PUBLIC AND PRIVATE INTERNATIONAL LAW**, Graduate Institute of International and Development Studies, and University of Geneva Law School, Geneva, Switzerland, <http://cidsconference2015.ch>

### September 30

**SINGAPORE INTERNATIONAL ARBITRATION FORUM (SIAF) 2015**, Maxwell Chambers, Singapore, <http://www.siaf.sg>

### October 15-16

**INTERNATIONAL DISPUTE RESOLUTION: DIVERSITY TOWARDS CONVERGENCE?**, Jagiellonian University, Krakow, Poland, <http://mediujmy.pl/en/icc-uj-conference>

### October 21

**INTENSIVE COURSE ON ICSID PRACTICE AND PROCEDURE**, Secretariat of the International Centre for Settlement of Investment Disputes, Prague, Czech Republic, [https://icsid.worldbank.org/apps/ICSIDWEB/Pages/Events.aspx?CID=81&ListID=a7dadf11-0f78-4bf6-b631-002ae87dae0d&variation=en\\_us](https://icsid.worldbank.org/apps/ICSIDWEB/Pages/Events.aspx?CID=81&ListID=a7dadf11-0f78-4bf6-b631-002ae87dae0d&variation=en_us)

### October 26-30

**INTERGOVERNMENTAL FORUM ON MINING, MINERALS, METALS AND SUSTAINABLE DEVELOPMENT (IGF)**, IGF Secretariat, at Palais des Nations, Geneva, Switzerland, <http://unctad.org/en/Pages/MeetingDetails.aspx?meetingid=682>



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