



REPUBLIC OF SOUTH AFRICA

BILATERAL INVESTMENT TREATY POLICY FRAMEWORK

REVIEW

Government Position Paper

Department of Trade and Industry

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EXECUTIVE SUMMARY

This paper attempts to consolidate and reflect the work of a Department of Trade and Industry (DTI) Task Team mandated to review Bilateral Investment Treaties (BITs) entered into by the Republic of South Africa to date. This review was partly necessitated by various arbitral proceedings initiated against the Republic of South Africa (RSA) and the need to conduct a comprehensive risk assessment. Prior to 1994, the RSA had no history of negotiating BITs and the risks posed by such treaties were not fully appreciated at that time. The Executive had not been fully apprised of all the possible consequences of BITs. While it was understood that the democratically elected government of the time had to demonstrate that the RSA was an investment friendly destination, the impact of BITs on future policies were not critically evaluated. As a result the Executive entered into agreements that were heavily stacked in favour of investors without the necessary safeguards to preserve flexibility in a number of critical policy areas. In reviewing the *travaux préparatoires* of the various BITs entered into at the time, it became apparent that the inexperience of negotiators at that time and the lack of knowledge about investment law in general resulted in agreements that were not in the long term interest of the RSA. To a large extent, the review seeks to correct this misalignment and to place before the Executive the true facts inherent to commitments undertaken by the RSA under BITs whilst at the same time updating the RSA's BIT regime as is being contemplated by many developed as well as developing countries whose history and experience of BITs is similar to that of the RSA.

This review consists of two parts, a macro - and micro policy framework analysis. The dual analysis alluded to above was necessitated by the fact that very little policy work had been done in this area. This review does not intend to provide an economic analysis of the investment policy that the RSA needs to follow in order to maximize growth. It merely flags this as an issue that would

need to be examined in the near future. The linkages on a policy level between industrial development, trade and investment is also flagged, a deeper analysis of these linkages also fall beyond the scope of this analysis.

The macro-policy research seeks to determine the policy and strategy considerations that are applied in respect of the initiation of Bilateral International Treaties (BITs). This process was undertaken by means of detailed interviews at management level with the various sector desks at the International Trade and Economic Development division (ITED) of the DTI and other relevant stakeholders. The outcome of these interviews seem to suggest that the RSA's investment approach to both inward and outward Foreign Direct Investment (FDI) has not been informed by a holistic policy perspective but rather a patchwork of general policy considerations. Thus, it is not argued that no policy exists, merely that the formal legal basis for FDI policy is scattered across various line function departments that do not always coordinate policy interventions. It is proposed that the legal basis for both inward and outward FDI be placed on a more secure footing by developing an overarching policy on FDI with more direct mechanisms for cooperation. A much closer link must be established between investment promotion activities, industrial policy and trade policy. The legal basis for an FDI policy is not fully captured in the terms of reference of the BIT Task Team, hence the recommendation that this issue be dealt with in a separate process.

Reference is made to various policy documents that line function government departments use to inform their work. The RSA's economic relations during the last decade have been defined by the very influential *Global Economic Strategy* which formed the backbone of the RSA's regional and bilateral relations with key trading partners. The DTI has been in the process of updating this document to better reflect the changing world order and the need for the RSA to reposition itself in such a dispensation. To the extent that this process is yet to be completed, the

BIT Task Team can merely recommend that the emerging trade policy fully account for coordination between industrial planning on the one hand, and investment policy and promotion on the other.

The RSA has also emerged as a capital exporter into the African continent and beyond. RSA companies have established a footprint on the continent, a foray that has been fully endorsed and encouraged by government. In the SADC region the *Protocol on Finance and Investment* (FIP) creates a framework for investment in the SADC region. This instrument seems only to cater for inward FDI and does not cater for intra-SADC investment. There seems to be little or no integration between the FIP and investment protection and promotion policies followed by the RSA. Given the sizable intra-Africa investments made by RSA companies, the RSA ought to assess how best such investments by its citizens may be safeguarded. Already the issue of diplomatic protection has been raised in the context where no BIT was in place to protect such interests. Different considerations apply in situations where either inward or outward FDI is contemplated. This raises some difficult questions with relation to the appropriate model for investment protection since clearly different needs may be articulated by RSA companies that invest in the African continent or elsewhere and investment entering the RSA. Many countries, particularly developing countries who seek to promote sustainable development, have an investment law which regulates issues pertaining to sectoral interventions, incentives and the role of an Investment Promotion Agency. Clear policy guidelines must inform approaches to both inward and outward investment.

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The micro policy analysis seeks to develop a policy framework for future engagement of investment issues and to assess the impact of obligations undertaken in BITs on the RSA. A legal analysis of various provisions found in

BITs has also been undertaken. Though most BITs follow a similar basic structure, nuances in language may result in very different legal consequences. This review takes place against the backdrop of a rapidly changing investment law environment. It is, therefore, important to gauge such changes against an emerging body of international practice. Policy recommendations are made with regard to the emerging legal trends and issues that have come to dominate investment treaties.

The analysis compares 11 standard clauses to be found in BITs concluded by the RSA. Typical clauses include issues such as the scope of an investment; the definition of an 'investment'; who qualifies as an 'investor'; geographic application; duration and termination; standards of treatment (including national treatment and MFN treatment); expropriation; transfer of funds and dispute resolution.

Investment law is an emerging discipline and in the words of a leading scholar should be approached with extreme caution. Few areas of international law excite as much controversy as the law relating to foreign investment. Much of the discipline as it exists today was created by developed (capital exporting) countries that sought to protect investments made by their citizens. The recipients of FDI, mostly developing countries, opposed notions set forth by developed countries as may be apparent from the Calvo doctrine. This doctrine has its origin in South America and emphasizes that the responsibility of governments towards foreigners cannot be greater than that which such governments have towards their own citizens. It explicitly rejects the notion of a so-called 'international minimum standard' as a standard applicable to the treatment of foreigners, including foreign investors. However, developing countries also started to compete with each other for investment and entered into BITs containing rules on investment protection. The treaties created jurisdiction

in arbitral tribunals at the unilateral instance of a foreign investor. This in turn led to an articulation by such tribunals of principles which confirmed and extended notions that favoured the treatment of foreign investment in accordance with 'external' standards. In the broader scheme of things it restrained governmental interference with such investments. The real debate is to what extent host states should be allowed to regulate foreign investment.

The interplay of various economic, political and historical factors shaped and continues to shape the development of international law on foreign investments. Traditionally investments by metropolitan powers were protected by virtue of their dominant military position (a result of colonialism), gun-boat diplomacy was sufficient to ensure that both trade and investment were protected. In parts of the world where such a colonial relationship did not exist, the genesis of state responsibility may be found. The United States is the progenitor of the doctrine on state liability for injury to aliens and their property. The United States sought to externalize the norms that governed aliens and their property and it argued for an international minimum standard in accordance with which aliens should be treated. Foreign investors were entitled to compensation in accordance with the hallowed formula devised by Cordell Hull that compensation should be 'prompt, adequate and effective'.

There is agreement that international law does not prohibit the expropriation of alien property. Disagreement, however, exists as to the conditions that must be fulfilled to prevent it from becoming unlawful. It seems clear that pronouncements by Secretary of State Hull in 1938, that compensation must be 'prompt, adequate, and effective', is no longer accepted by international law. Today the standard of 'appropriate' compensation seems to enjoy the greatest support and has been approved in several arbitral awards. This debate has also

played out in the RSA since BITs call for the traditional standard of compensation, while the Constitution of the RSA mandates a lesser standard.

Investment agreements contain obligations specifying the treatment that the contracting parties are required to provide to the investment once it has been established. In many instances it has been contended that an international minimum standard exists. Apart from the rule relating to compensation for expropriation and the settlement of such issues through a tribunal that sits outside the host state, there does not seem to be any guidance as to what the content of the standard is. The existence of a minimum international customary law standard has long been disputed. Such standards impact on the ability of governments to prefer its own nationals on grounds of past discrimination or on the basis of economic considerations. Greater balance must be injected into relationships governed by BITs.

Investment dispute settlement has now embarked on a course that effectively assigns arbitral panels an active role in implementation and interpretation of BITs. Investors have become aware of the attractive *status quo* under the global investment regime – literally hundreds of long-ignored investment treaties offer investors access to an investor-state dispute settlement mechanism, allowing them to take their disputes directly to international arbitration – leapfrogging domestic legal systems (and thus, any safeguards designed to protect important public goods). Some investors are using bilateral investment treaties to challenge treatment of foreign investments in various sensitive areas, including water and sewage provision, oil and gas exploitation and mining concessions. Major law firms are using BITs as the tool of choice for challenging host state regulation of public services. Solutions to the issues of dispute settlement are available. They include greater transparency; selection of arbitrators in a neutral manner rather than by the parties; proper deference to domestic dispute settlement procedures;

clear separation of the functions of arbitrator and advocate; and the introduction of an appellate process. Most of these changes by now appear inescapable.

Existing international investment agreements are based on a 50-year-old model that remains focused on the interests of investors from developed countries. Major issues of concern for developing countries are not being addressed in the BIT negotiating processes. BITs extend far into developing countries' policy space, imposing damaging binding investment rules with far-reaching consequences for sustainable development. New investment rules in BITs prevent developing country governments from requiring foreign companies to transfer technology, train local workers, or source inputs locally. Under such conditions, investment fails to encourage or enhance sustainable development. There are many who question whether BITs in fact attract FDI at all. Various countries are reviewing their BIT regimes, so RSA is not alone in the process. Whilst a revised BIT will go a long way in resolving critical problems which the RSA now faces, it will not, however, be a panacea for all other FDI problems. These problems can only be tackled by proper policy integration, co-ordination and implementation.

PART I

I. MACRO POLICY FRAMEWORK

1. INTRODUCTION

The Macro Policy Framework has been developed taking account of the RSA's differentiated approach to FDI policy encompassing both political and economic considerations. The review of the RSA's Bilateral Investment Treaty Policy Framework was initiated in 2005 when it became apparent that the RSA was facing serious challenges from developed nations seeking to rely on the provisions of BITs in order to claim compensation from the RSA for alleged failure to comply with its obligations in under BITs with respective countries.

The DTI sought to suspend the further negotiation and conclusion of BITs pending a comprehensive review of the policy framework informing the BIT process, as well as the possible outcome of pending litigation in this arena. The review, which was formally commenced in early October 2008, therefore seeks to develop a policy framework and to recommend guidelines for the future engagement of BITs as well as assessing current BITs which have been concluded.

2. METHODOLOGY

A proposed work-plan was drafted on 12 September 2008, which approached the review in terms both of macro and micro policy considerations. In this regard, the specific working methodology of the team consisted of:

- An assessment of the status of BITs;
- Location and analysis of the texts of same;

- Compilation of a detailed index of BITs concluded, ratified and those under negotiation
- Assessment of policy/strategies informing the conclusion of BITs

The aforesaid deliverables were achieved by means of detailed interviews at management level with the various sector desks at International Trade and Economic Development (ITED) and other relevant stakeholders, the full details of which are outlined hereunder. Interviews were conducted with:

- Bilateral desks at ITED
- Multilateral desks for SACU, SADC and AU/NEPAD
- TISA (Trade and Investment South Africa)
- Department of Foreign Affairs (Trade Policy and Economic Relations as well as Office of Chief State Law Advisor)
- Presidency

The interviews were conducted on the basis of a detailed questionnaire designed for information sought from bilateral desks at ITED and were adapted for interviews with other divisions.

3. BASIS OF CURRENT FDI POLICY

3.1 Policy framework that informs the conclusion of BITs.

The macro-policy research conducted under this project seeks to determine the policy and strategy considerations that inform the initiation of BITs. Interviewees were requested to provide an indication of their working methodology and in particular, what policies and or strategies informed the inclusion of a particular BIT in their work plans.

In several instances, it was pointed out that the conclusion of the BITs were historical (particularly with regard to BITs concluded shortly after 1994 and up to about 1999), and that no policy documentation informing the rationale for the conclusion of such BITs could be found. A draft DTI Cabinet Memorandum of 1994 indicates that 16 countries had requested the conclusion of BITs and that the DTI was convinced that such agreements would create an “investor friendly” environment. There seems to have been no legal or economic analysis of the risk associated with the conclusion of BITs. The memorandum concludes with the following remark:

“The aspects covered by the bilateral agreements can be viewed as “basic investor rights”... that the same rights and privileges extended to foreign investors in terms of the agreement also be extended to South African investors.”

The above-mentioned excerpt demonstrates a lack of understanding regarding the real nature and consequences of BITs at that time. Cabinet was not fully apprised of the dangers inherent in BITs. The confusion on a policy level also spilled over into the operational areas of the various DTI desks. Some desks indicated that they were reliant on the *Global Economic Strategy Document* (DTI, 2000) as a basis for their strategic planning. The DTI has also developed a “Butterfly Strategy” in order to forge and develop strategic regional and bilateral economic relations with key trading partners. This strategy aims to diversify the RSA’s economic relations by opening new ‘trade wings’ from the body of traditional trade with Africa, the EU and North America, to Latin America and the East. In pursuance of this goal FTAs have been concluded with the Southern African Development Community (SADC) and the EU (TDCA), while trade deals have been concluded with MERCOSUR (Common Market of the Southern Cone) and EFTA (European Free Trade Area).

In an interview with DFA officials, it was pointed out that BITs were largely driven by an inter-departmental task team (including participation from the DTI) and that the pursuance of such a course of action was within the broader mandate of the RSA to attract FDI and open up its economy, post-democracy. Overall, however, it was agreed that there does not appear to be a consistent approach to bilateral policy-making and strategic planning.

Similarly, officials from the Presidency concluded that in the arena of foreign bilateral relations, the Presidency took guidance from the DFA. In this regard, officials from the Presidency clearly stated that they did not draft any policies pertaining to RSA's foreign political and economic relations. Reference was made to two policy documents utilised by the DFA, namely, the *Economic Diplomacy Strategy* and the *Co-ordination of International Relations strategy*.

TISA officials, who were interviewed, indicated that until recently, Trade and Investment South Africa (TISA) did not have a global investment strategy in place. The latter has only recently been formulated and concentrates on *sectors* as opposed to *regions*. TISA officials confirmed that they rarely ever co-ordinate their working programmes and strategies with the work being conducted at ITED.

4. OUTWARD FDI POLICY

4.1 South Africa's outward investment policy

Findings from the interviews conducted revealed mixed results in terms of the existence of a formal outward investment policy. It can be concluded that no coordinated policy exists with regard to outward FDI policy. It was therefore necessary to analyze *de facto* outward investment trends on the basis of

information gathered through engagement with various stakeholders. Though no general trends regarding the outward investment strategy is discernable, anecdotal evidence suggest why substantial investment flows into the rest of the continent have occurred.

The RSA is in a unique position on the African continent as being both a *capital exporting* and *importing* country. In 2004 the RSA's inward FDI stock stood at 46.3 billion USD, while outward FDI stock stood at 28.8 billion USD (Peterson: 2006 8). RSA firms have displaced European and American firms and in the process have become significant investors and trading partners of other African countries (UNCTAD: 2008 39). In 2007, FDI inflows into Africa grew by 16% to reach 53 billion USD. The RSA and Madagascar joined the list of top 10 FDI host countries (*Ibid*). FDI outflows in 2007 was mainly driven by the RSA and reached 6 billion USD. This was mainly due to the expansion of operations by transnational corporations (TNCs) from the RSA. The RSA has encouraged its companies to invest in other African countries and has used BITs to protect such investments.

4.2 Outward FDI Policy in relation to various regions

4.2.1 Africa

Certain African desks concluded that they were reliant on statements emanating from the Presidency in relation to NEPAD and the RSA's attempts at strengthening political relations on the continent. It would appear, however, that the NEPAD secretariat does not have a comprehensive strategy document in respect of investment in Africa. Similarly, it was pointed out that the AU does not have a strategy document focusing on investment and that there was no current focus in the AU on factors affecting investment in Africa or perceived risks associated with investing in Africa from a continental perspective. Other

desks intimated that they were reliant on the now-outdated *Global Economic Strategy* for their policy thrusts in Africa.

In respect of the Southern African Development Community (SADC), reference was made to the *Protocol on Finance and Investment* (FIP), in particular to Annex 1 thereof which deals with co-operation on investment. The Annex aims to create the framework for broader FDI promotion in the SADC and in some aspects emulates the provisions of a typical BIT. The FIP has not been harmonized within current RSA treaty making practice since it appears that standard clauses in RSA BITs differ substantially from equivalent provisions to be found in the FIP.

The effect of the Annex appears to be that of promoting the SADC region as an attractive destination for FDI and as such does not really cater for intra-SADC investment, the latter being a factor which is directly relevant to the RSA in respect of its *de facto* intra-African investment stance and the sizeable investments which the RSA companies are making in SADC and Africa. In this regard, the SADC desk has confirmed that the RSA has entered into 5 BITs with states in the SADC and that there are several more being negotiated. It was specifically indicated that these BITs were driven by the RSA, largely influenced by private sector interest in SADC countries. A similar sentiment was expressed in terms of bilateral desks responsible for Central and Eastern Africa & West Africa. In respect of North Africa, it was suggested the RSA *could* be both a capital-exporting and capital-importing country vis-à-vis certain North African countries.

4.2.3 Middle East

The RSA's economic relationship with Middle Eastern countries, from an investment point of view, may be generally categorised as being both capital-exporting and capital-importing. The basis for South Africa's economic focus in

the Middle East is a cabinet decision of 2006 in terms of which it was decided that more emphasis should be placed on relations between the RSA and Gulf Cooperation Countries (GCC) countries. It was mandated that recruitment of investment from the GCC would be targeted.

The information obtained from the desks seem to suggest that there is both local pressure (from RSA companies wishing to pursue investment opportunities in the Middle East) as well as from Middle East countries intending to diversify their investment portfolios and looking to the RSA as a potential destination for the investment of Sovereign Wealth Funds (SWF) and other forms of investment emanating from newly emergent Middle East economies. This perspective is enhanced by the current global crisis since most sovereign wealth funds are seeking to diversify their investments toward emerging market assets. In the current economic climate investments by SWF may contribute to greater economic stability in sectors that receive such investments. However, some concern has also been raised with regard to the nature of activities of SWF since investments made by such organisations may not purely be based on commercial incentives. A dominant theme of recent discussions of recipient country attitudes and policies toward foreign government controlled investors relates to whether or not these investors are following “hidden political agendas”. The following concerns or risks have been identified with regard to SWF: competition-related concerns; sabotage, espionage or impeding the implementation of host country policies; and foreign sovereign immunity.

The current suspension of BITs appears to affect this region the most as many of our missions located in Middle East countries have identified the conclusion of BITs as key responsibility areas for their particular missions and the same seems to be applicable to Middle East representatives resident in the RSA.

4.2.4 Europe

As discussed above, the BITs concluded between the RSA and many European countries were concluded immediately post-1994 elections (with some having commenced negotiations prior to 1994, e.g. the United Kingdom (UK)) and were largely managed by the DFA. According to officials at the DFA, the approach taken at the time was to go on a road show in an attempt to promote the RSA as an attractive destination for FDI. The result of this road show was that BITs were concluded with the RSA's main traditional trading partners at the time, namely, Western European countries. The formulation of the BITs concluded during at this time largely followed the format of the Organisation for Economic Cooperation and Development (OECD) model and most BITs appeared to be fairly similar in substance, format and intention.

In interviews concluded with the desks, it has also become apparent that there are now instances arising in respect of which the RSA is exporting capital to European countries, particularly to new-accession European Union (EU) countries and also EU countries in transition. It would seem that there is a policy imperative to protect RSA companies' interests in Europe. Hence, proposed BITs with new European partners should take these factors in account. Similarly, the fact that many of the early BITs that were signed immediately post-1994, would now be approaching the end of their term and should be revisited with a view to ensuring that they incorporate measures which ensure that national developmental objectives may be pursued (see discussion under part II par 3.2.6 regarding the amendment and termination of BITs).

4.2.5 Americas

Officials interviewed, indicated that not many BITs were signed with this region and that those which had been signed were concluded in the early “opening-up” years, post-1994. It was further pointed out, that only one of those that were signed was now being reviewed, with a view to including aspects which catered for developmental objectives. It was, however, indicated that although there was an overall strategy for the region, that there was a need to strengthen economic analysis of relations and also to streamline and focus attention on identified strategic partners.

5. INWARD FDI POLICY

5.1 Investment policy and risks associated with investing in the RSA

The key to the RSA’s industrial performance is the ability to attract export-oriented FDI, which will reinforce the current momentum of export-orientation. The essence of this approach coalesces around the *Accelerated Growth and Shared Initiative for South Africa (ASGI-SA)* and the *National Industrial Policy Framework (NIPF)*. This paradigm calls for diversification beyond traditional reliance on minerals and mineral-processing, an intensification of industrialization and a move towards a knowledge-based economy.

FDI investors have a poor understanding of the nature of democracy in the RSA, hence struggle to identify it as an investment destination distinct from the rest of Africa. Some investors see Black Economic Empowerment (BEE) requirements, consistency of public reforms, inflexible labour standards and the high crime rate in the RSA as significant risk factors. These risk factors apply to inward FDI of both developed and developing countries.

5.2 Instruments that mitigate investment related risks

The RSA is also a signatory to international investment protection agreements, including the Multilateral Investment Guarantee Agency (MIGA) of the World Bank. The RSA signed the Convention establishing the MIGA on 16 December 1992 and ratified it on 2 March 1994. The Overseas Private Investment Corporation (OPIC), the self-sustaining US government risk agency, has committed more than US\$45mn in political risk insurance and project financing to US companies investing in SA, since 1994.

5.3 Country Profiles in relation to inward FDI

5.3.1 Developed Countries

The EU is the RSA's largest investor (within the EU, the UK), followed by the Americas (the US and Canada). The strong investor relations between the RSA, the EU and the Americas can, in part, be explained by well-established trade (and tourism) links. Investors from these two regions have heavily invested in mining and quarrying, services, and manufacturing in the RSA.

5.3.2 South-South Countries

Asia has a much more diversified investment position in the RSA, where key sectors include financial services, community services, transport storage and communication, trade catering and accommodation and manufacturing. The key Asian sources of FDI are Malaysia, Japan, Taiwan and Hong Kong and China.

5.3.3 Other Developing Countries

With the price of crude oil trading above the level of US\$50 per barrel for a sustained period (reaching highs of US\$140 per barrel), the countries of the Gulf region have reported record surpluses. While domestic investment in the region has increased, Gulf Governments and private investors are increasingly looking

at opportunities elsewhere in the world. The United States, Europe and Japan remain favoured investment destinations, but there are significant opportunities for the RSA in this regard: infrastructure, including Coega, Dube Tradeport (IFA of Kuwait offered to finance development of King Shaka International Airport); tourism; telecommunications, transport, energy - including investment in new refining capacity; mining and financial services. Latin America is also emerging as an important trade partner for the RSA.

6. OBSERVATIONS AND CONCLUSIONS

6.1 Preliminary assessment

Most officials concluded that insufficient analysis is undertaken in respect of the correlation (if any) between FDI flows and the conclusion of BITs. It is uncertain whether a direct correlation exists between FDI and the conclusion of BITs. FDI has many determinants and BITs may account for at least one of them, namely legal certainty. In many instances, officials are of the view that bilateral relations were forged in the absence of a policy framework. Further, it has been noted that countries are not individually analysed with a view to determining what the most appropriate forms of cooperation would be. As a matter of course a generic mix of agreements is often proposed, very often resulting in a plethora of agreements in a variety sectors involving more than one government department in the RSA. It is also clear that there does not appear to be sufficient co-ordination across all levels of government ensuring that there is a streamlined focus in relation to RSA's international relations.

6.2 Alternatives to negotiating BITs?

As noted most governments have concluded large numbers of BITs, and are learning that the BITs may have significant policy implications. Some governments have had occasion to reflect upon the nature and extent of their BITs obligations and to question whether such agreements provide an appropriate framework for governing foreign investments.

It is noteworthy that some Latin America countries have withdrawn from the Washington Convention on the Settlement of Investment Disputes (ICSID Convention) e.g. Bolivia, while Ecuador has announced that consent to ICSID arbitration is no longer available for certain categories of disputes (UNCTAD: 2008 15). Countries such as Nicaragua and Venezuela are considering such a move, while other countries in the region are denouncing the renegotiating existing BITs. Other countries are also questioning the degree to which BITs undercut the jurisdiction of local courts. The Czech Republic upon its accession to the European Union, suggested that it would terminate its pre-existing treaties with fellow EU Governments - a move which would return foreign investment disputes to Czech Courts, and, if domestic remedies were exhausted, to EU institutions (Peterson: 2005). Meanwhile, Australia rejected the need for an investor-state arbitration mechanism in its Free Trade Agreement with the United States, insisting that its domestic courts are adequate to serve the need of foreign investors. Countries such as Brazil and Mexico are not members of ICSID, but have become members of the New York Convention facilitating the enforcement of arbitration awards made in other states.

Other governments, including Canada and the United States, have sought to revise negotiating templates for BITs, so as to ensure that new agreements provide narrower protections for investors - thus ensuring greater freedom for governments to regulate in certain contexts, without fear of investment treaty

lawsuits. While the BITs pursued by these governments continue to offer high levels of protection, they have been tightened in key respects, including through the insertion of express language which safeguards the rights of governments to regulate for public welfare reasons (including new generation issues such as health, environment, labour *etcetera*). During a workshop held on 16 April 2009 with various government departments, differing views were expressed regarding the role, function and impact of BITs. A large number of participants concluded that BITs should be reviewed with a view to establishing clearer and more explicit drafting modalities, more balanced rights and obligations between parties and the adherence to standards that would not undermine national development policies. The view was also expressed that due to the severe impact that BITs may have on both constitutional imperatives and government's policy space, coupled with the financial liability, no further BITs should be entered into. In both instances participants emphasized the need for further policy intervention to ensure equilibrium between investor rights' and the legitimate right of the RSA to regulate in the public interest. There seemed to be overwhelming consensus that this BIT review could not take place in the absence of a comprehensive FDI policy for the RSA

6.3 Summary and recommendations

There is clearly an urgent need for a unified, well coordinated strategic investment document which will ensure that the role and responsibilities of individual stakeholders is coordinated in such a way that will give direction to current trade policy statements premised on ASGI-SA and the NIPF. Account should also be taken of the Industrial Policy planning of EIDD (Enterprise and Industrial Development Division of the DTI) in order to accentuate the link between trade policy on the one hand and industrial policy on the other. This may be done by forging deliberate linkages between specific sector strategies, tariff policy (tariff

policy may stimulate growth competitiveness of targeted sectors) and the RSA's international economic engagements (including trade negotiations, proactive use of WTO dispute settlement provisions to advance trade policy objectives, participation in standard setting global *fora* & BIT negotiations that reinforce core policy cohesion in foreign economic relations). It is particularly telling that no direct policy statement could be identified that informs an investment policy that speaks to both inward and outward FDI.

PART II

II. MICRO POLICY FRAMEWORK

1. OBJECTIVES

This analysis compares the substantive treaty provisions used in the various generations of BITs concluded by the RSA. The changing *context* of investment relations between countries has largely lead to an expansion of the areas covered by BITs. It is therefore important to gauge such changes against an emerging body of international practice. Policy recommendations will be made with regard to the emerging legal trends and issues that have come to dominate investment treaties. The legal analysis that underlies such policy recommendations focuses on explicit language that is found in BITs concluded by the RSA. Though most BITs follow a similar basic structure, nuances in language may result in very different legal consequences. This review does not intend to provide an economic analysis of the investment policy that the RSA needs to follow to maximize economic growth. It also does not speak to the ongoing trade and industrial policy review directly, since these issues fall beyond the scope of this analysis. However, as pointed out above (see Part I, section 6.3) some sort of policy integration needs to occur across the board. In the absence of an integrated approach to investment, both inward and outward, any legal analysis occurs within a policy vacuum.

2. BREATH AND DEPTH OF ISSUES COVERED

The analysis compares 11 standard clauses to be found in BITs concluded by the RSA. Typical clauses include issues such as the scope of an investment; the definition of an 'investment'; who qualifies as an 'investor'; geographic

application; duration and termination; standards of treatment (including national treatment and MFN treatment); expropriation; transfer of funds and dispute resolution. The ultimate objective of the above-mentioned analysis will be to develop a policy response that may be used by the RSA to guide investment protection negotiations. The more immediate objective is to create a position paper that will be circulated to both internal and external stakeholders. These consultations will guide the preparation of a Cabinet Memorandum. In order to develop an informed position, the analysis must take note of international practices that have emerged in the field of investment law. BITs concluded by other (developing) countries may be very helpful, especially where such BITs have been subject to arbitral proceedings or where such BITs incorporate a developmental approach. The RSA's own experiences with arbitral proceedings will further influence the debate.

3. SCOPE OF COMMITMENTS AND RESERVATIONS

3.1 Preambular Language

The general practice is that most BITs will be prefaced by a preamble in which parties state their intentions and objectives when concluding the agreement. The preamble does not create any legally binding rights and duties; however this does not mean that the preamble is irrelevant. Article 31 of the Vienna Convention on the Law of Treaties (hereinafter "the Vienna Convention") states that the preamble constitutes part of the context of an agreement. Preambles play an important role in guiding the interpretation of treaties where there is ambiguity in the language. The absence of references to development objectives or public interest goals strengthens the case for investors arguing that the primary objective of a BIT is to protect investor interests. Parties must ensure that the preamble is consistent with the substantive provisions of a BIT. It may be advisable to introduce more specific language into preambles that emphasizes the fact that investment promotion and

protection should not undermine other key public values and should promote sustainable development.

3.2 Scope of Investment Clause

3.2.1 General Overview

The scope of application of a BIT may have various dimensions as it may relate to: (i) the subject matter of the agreement (investments made and investors of parties to the agreement); (ii) the geographical scope; and (iii) the temporal scope of application of the BIT. Traditionally, BITs do not deal with all these dimensions in one single clause. A vast majority of BITs lump the subject matter of the agreement and the geographic application together in a 'general clause' which deals with the definitions of 'investment', 'investor' and 'territory'. Other terms that are often included in such a general clause, include the definition of 'returns' (forms of yields) and 'change of form' of an investment. The temporal application is usually dealt with in the "final clauses" of a BIT. In recent times some BITs, in response to legal drafting considerations, attempt to clarify the different dimensions of the scope of application of the agreement in one single provision

3.2.2 Definition of Terms

The purpose of definitions in legal instruments such as BITs is to determine the object to which the rules of the agreement shall apply and the scope of their applicability. BITs typically protect investments made by investors of one contracting party into the territory of another contracting party. The scope and subject-matter of the treaty will depend on the definition of certain key terms. Most of the RSA BITs contain a 'definition clause' that define concepts such as 'investment', 'investor', 'returns', 'expropriation', 'territory' and 'without undue delay'.

3.2.3 Investment

Traditionally most BITs define 'investment' in broad and open-ended terms and follow an asset-based approach. Such a definition not only covers capital, but 'every kind of asset' of an investor in the territory of the host country. The manner in which the concept of investment is defined has also evolved. This is captured in the evolution of RSA BITs, where certain assets not acquired for investment purposes are excluded. The nature of assets that will be regarded as investments have been closely scrutinized and assets that are speculative in nature are now generally excluded from the definition of an investment (this also includes portfolio investments). In some BITs real estate or other property not acquired for the purpose of economic benefit or for business purposes are excluded. If an investor purchases property as a holiday home, this purchase will not be seen as an investment that will be covered by the BIT. An important development to some of the recent RSA BITs is the recognition that any investment made into the country will only be covered if it is done *in accordance with the domestic law* that governs such an investment. If an investment is not done in accordance with the domestic law of a country, it may not be covered by the BIT. In recent times questions have been posed about foreign ownership of immovable property in the RSA. A commission chaired by Prof Shadrack Ghutto has delivered a report on this subject which has not yet been circulated publicly. It is understood that if a recommendation is made that foreign ownership in immovable property should be limited, it would not affect existing foreign ownership since such a limitation will operate prospectively.

3.2.4 Investor

3.2.4.1 *Natural Persons*

BITs apply to investments made by investors of one contracting party in the territory of the other contracting party. Most BITs have traditionally included a definition of investor that covers both natural and juristic persons. In the RSA-Ethiopia BIT (2008) the concept 'national' is explicitly linked to a determination under the national law of a party. Internationally, an investor has been defined more broadly to also include persons who qualify as permanent residents under the domestic law of a party.

3.2.4.2 *Juristic persons*

A legal entity is seen as an investor if it is incorporated in accordance with the law of a party and has its seat in the territory of such a party. In addition, some RSA BITs also require an effective economic activity, in the territory of such a party. Such a provision merely ensures that the legal entity has a genuine connection with the home country. One difficulty which has arisen in context of BITs has been the issue of control in relation to a particular investment. The issue of control is an important factor to assess to what extent an investor should be linked to an investment in order for that investment to be considered as a foreign investment. The classical asset-based definition of investment holds that 'every kind of asset' in the territory of one party, which is held by an investor from the other party, should qualify as an investment. This is also true for BITs concluded by the RSA.

3.2.4.3 *Control Criterion*

A question has arisen whether a shareholder has legal standing to bring a claim under a BIT if the interests of the company in such an investment have been compromised by host state regulations. In the ICSID case of *CMS Gas Transmission Company v The Republic of Argentina* (Case No ARB/01/8, judgment delivered on

17 July 2003) the tribunal found that there was no bar in current international law to the concept of allowing claims by shareholders independently from those of the corporation concerned, not even if those shareholders are minority or non-controlling shareholders (CMS Gas: 2003 par 48). Most international BITs provide that claims are justified if an investor actually owns or controls an investment, whether directly or indirectly.

The RSA-Ethiopia BIT (2008) provides that:

“...investment shall mean the assets invested or acquired through total ownership of enterprise or participation in ownership of an enterprise which give a significant grade of influence to the investor in the management of the asset.”

The formulation in this BIT provides further clarification of the ‘control’ criterion, though it requires ‘a significant grade of influence’ which seems to be contrary to what was held in the *GMS Gas* case with regard to minority shareholders. In addition, control over the selection of the majority of members of the board of directors may similarly satisfy the control requirement.

3.2.4.4 A case study

A good illustration of the issue of ownership and control is to be found in the facts of the case of *Foresti and others v the Republic of South Africa* (ICSID Case No ARB(AF)/07/1). The claimants’ case is that mineral rights were directly expropriated on the passage of the *Mineral and Petroleum Resources Development Act*, No 28 of 2002 (MPRDA). The related alternative claim is that the MPRDA indirectly expropriates mineral rights. All the mineral rights are owned indirectly through intermediaries and subsidiaries. The claimants seem to invoke investments that are not directly owned by them, and none of the subsidiaries in question are parties to the arbitral proceedings. In light of cases such as *CSM Gas* it is probable that claims of this nature would be admissible and that any

jurisdictional or standing issues may be overcome. However, there is also a formidable body of law that holds that a distinction must be made between the claims of a company on the one hand, and claims of shareholders who only have an indirect interest by virtue of their shareholding.

3.2.5 Geographic application

BITs typically define the term territory as "...those maritime areas over which the contracting parties exercise sovereign rights or jurisdiction in accordance with international law." Such areas include territorial waters, the exclusive economic zone and the continental shelf over which countries may have jurisdiction. New RSA BITs tend to define the concept of territory more comprehensively as may be seen from the Ethiopian BIT (2008):

"...the territory shall include the territorial sea, air space and any maritime area situated beyond its territorial sea, which has been or might in the future be designated under its domestic law, in accordance with international law, as an area within which it may exercise sovereign rights and jurisdiction."

3.2.6 Entry into force, validity, amendment and termination

The RSA BITs under review uniformly state that contracting Parties shall notify each other when their respective constitutional requirements for entry into force of this Agreement have been fulfilled. The process set out in section 231(2) of the Constitution has been followed when a BIT is ratified. However, there seems to be some ambivalence regarding which procedure should be followed since section 231(3) has also been mentioned in this context. The question may also be posed whether BITs or certain sections thereof are self-executing within the meaning of section 231(4). In the constitutional judgment of *President of the Republic of South Africa v Nello Quagliano and others* Case CCT 24/08 [2009] ZACC 1 the contention by the respondents was that certain extradition agreements were not enforceable under RSA domestic law. The respondents argued that the relevant extradition

agreements were not self-executing and had not been enacted into legislation. Judge Sachs decided that it was unnecessary to deal with the question whether the extradition treaty was self-executory (*ad par 37*). In light of the uncertainty with regard to the relationship between the above-mentioned provisions, it is not surprising that only a small number of BITs have been ratified to date.

According to the Vienna Convention, there is usually a presumption against the retrospective application of a treaty. This is also true for BITs. The prevailing trend is to provide protection to both future investments and investments already established at the date of entry into force of the agreement. Furthermore, it is stated that the agreement shall not apply to any investment-related dispute or claim that arose or was settled before the entry into force of the BIT

Most RSA BITs provide that agreements will remain valid for a period of ten (10) years. More recent RSA BITs provide for a period of fifteen (15) years or even longer. Most BITs provide that after the initial fixed period has ended, each party may terminate the treaty, usually with one year's written notice. Any investments that have been made prior to the date when the notice of termination becomes effective will be protected for a further ten (10) year period. Most of the early BITs that were concluded from 1994 onwards have either reached the ten (10) year limit or will soon do so. It is the prerogative of the RSA to give notice of termination and to request renegotiation.

4. STANDARDS OF TREATMENT OF INVESTMENTS

4.1 Introduction

Investment agreements contain obligations specifying the treatment that the contracting parties are required to provide to the investment once it has been established. In many instances it has been contended that an international minimum standard exists. Apart from the rule relating to compensation for expropriation and the settlement of such issues through a tribunal that sits outside the host state, there does not seem to be any guidance as to what the content of the standard is (Sornarajah: (2004) 148). The existence of a minimum international customary law standard has long been disputed. The struggle to create such a standard has been manifested in several ways. First, the articulation of the standard through official positions taken by developed states. These positions have been contested by developing states. Second, the argument has been advocated that the incorporation of the standards in investment treaties is evidence of customary international law. However, the form and ambit of such standards in investment treaties differ substantially in objectives, scope, exceptions and general applicability.

One can distinguish between general treatment standards, in other words standards relating to all aspects of the existence of a foreign investment in a host country, and specific treatment standards addressing particular issues.

4.2 Absolute standards of treatment

4.2.1 Scope and content of absolute standards of treatment

First, there are “absolute standards” of treatment, so called because they are non-contingent. They establish the treatment to be accorded to the investment without

referring to the manner in which other investments are treated. Examples of absolute standards are the provisions on fair and equitable treatment, full protection and security, expropriation and the transfer of funds

4.2.2 Applicable standards of international law

Very few BITs attempt to clarify the meaning and relationship between the standards of fair and equitable treatment, full protection and security (these standards are either treated together or separate with regard to formulations in BITs) and how they relate to minimum standards that may be set by international law. Though the fair and equitable standard is commonly used in BITs, the standard itself lacks a precise meaning. Internationally there are two different opinions regarding the precise content of fair and equitable treatment. Some commentators may argue that this standard is no different from the obligation to treat investments in accordance with international minimum standards of customary international law.

Others argue that fair and equitable treatment means something different from the international legal standard. The crux of this argument is that the term “fair and equitable treatment” should be given a plain meaning, and that a test based on equity (which is more subjective) should be applied in order to ascertain whether the standard has been infringed. This implies a more expansive test under this standard. Due to uncertainties that exist regarding the true meaning of the fair and equitable standard, it would be preferable to spell out more clearly and comprehensively what is meant by this concept. The *Note of Interpretation* issued by the NAFTA Free Trade Commission provides a good example of how greater clarity may be inserted into BITs by defining the application of the customary law minimum standards in relation to the treatment of aliens within the NAFTA context.

4.3 Relative standards of treatment

4.3.1 Scope and content of relative standards of treatment

A second category relates to “relative standards” of treatment. They define the required treatment to be granted to investment by reference to the treatment accorded to other investment. National treatment and MFN treatment are the relative standards *par excellence*. Thus, in the case of national treatment, reference must be made to the treatment of nationals of the host country. Similarly, in determining the content of the MFN standard, reference must be made to the treatment granted to investments from the “most favoured nation”.

4.3.2 National Treatment

There has been considerable disagreement between states regarding the question of state liability for injury to aliens. Article 2(2) of the Charter of Economic Rights and Duties of States articulated the national treatment principle. Capital exporting countries, however, have argued that aliens should be treated in accordance with an international minimum standard. Unlike in the past when national treatment was rejected altogether because such treatment in the case of some countries was lower than the minimum standard contended for by capital exporting countries, national treatment may have its advantages as states reserve many of their economic sectors and privileges to their nationals (Sornarajah: (2004) 234).

The existence of a national treatment standard could provide a basis for arguments that performance requirements such as export quotas or local purchase requirements should not be imposed on foreign investors, at least until entry has been made. Such requirements are not imposed on local investors and the national

treatment standard may militate against the imposition of performance requirements unless exempted from the national treatment standard. In the NAFTA case of *ADF v United States* the issue was raised as to performance requirements, in this case 'buy America' statutes, being a violation of national treatment.

National treatment clauses in RSA BITs exhibit a progression from early treaties that make no mention of any exclusion to national treatment – to later generation BITs that provide for limited exceptions to this standard. Due to the number of early treaties that do not contain exclusions to national treatment clauses, and considering current arbitral proceedings underway, the lack of express language which would safeguard for example affirmative action measures or state regulation of certain sectors, creates a real danger that tribunals could find that affirmative action measures or regulatory state measures breach obligations under the national treatment clause. There is an emerging acknowledgement that sectors that requires exemption from the scope of the treaty or to preserve regulatory controls relating to competition and similar factors that may be exempted from the scope of national treatment.

Later generation RSA treaties have limited exception to certain preferential treatment. BITs concluded with the People's Republic of China, Iran, the Russian Federation, Ghana, Nigeria, the Czech Republic and Mauritius provide exceptions in relation to National Treatment and MFN where preference are granted for purposes of promoting equality or to protect or advance natural or legal persons, or categories thereof, disadvantaged by unfair discrimination. The RSA-Tanzania BIT (2005) provides for national treatment in Article 3(2), while Article 4(c) contains the exception to the above-mentioned national treatment clause. Article 4(c) reads as follows:

“The provisions of sub-Articles (2) and (3) shall not be construed so as to oblige one Party to extend to the investors of the other Party the benefit of any treatment, preference or privilege resulting from... any law or other measure the purpose of which is to **promote the achievement of equality in its territory, or designed to protect or advance persons, or categories of persons, disadvantaged by unfair discrimination in its territory.**”

This explicit provision affirms the rights of the state to provide preferential treatment to locals. Various BITs also contain a clause that exempts development finance institutions that provide development finance through mainly non-profit activities.¹ This exception may not go far enough to cover preferential subsidies, grants and other forms of special treatment provided to local culture industries, such as television or film production. For this purpose a more general exception clause should be considered. It is also not uncommon to have subject or sector specific exceptions.

4.3.3 MFN Treatment

The basis of comparison under the MFN standard differs from the national treatment standard because one contracting state (receiving) is obliged to give investors or investments from the other contracting state (sending) no less favourable treatment than it grants to investors or investments from third countries. This levels the playing field for all foreign investors protected by a BIT. The RSA follows the ‘admission’ approach to investment and does not provide any pre-establishment rights. Thus, MFN treatment only becomes applicable once an investment has been ‘admitted’ into the territory of the RSA. Further, a substantial number of RSA BITs seem to grant MFN treatment to both investors and their investment. The RSA has encouraged investment and there are generally no restrictions on the type and extent of investments. There are no exchange controls or restrictions on the repatriation of capital investments, profits, or dividends.

¹ Sweden, Denmark, Greece, Netherlands, Cuba, Italy, Egypt, Mozambique, Switzerland, Senegal, Spain, Korea, Chile, China, Germany, Mauritius and France.

Royalties, license fees and certain other remittances require approval by the Reserve Bank, while double taxation treaties are in place with various countries.

RSA BITs providing protection only in the post-establishment phase normally include two MFN exceptions. One permits the contracting parties to deny investors of the other contracting party more favourable treatment resulting from membership of regional economic integration organizations (REIO). The rationale for this REIO exception stems from the nature of regional economic integration, which purports to grant privileges to the member countries in exchange for a reciprocal preferential treatment. The REIO exception prevents these privileges from being extended to those contracting parties of BITs with which such a reciprocal integration relationship does not exist. The second exception excludes any advantage granted to a third country under a double-taxation treaty (DTT) from the application of the MFN clause. The reason for this exception is once again the inherent reciprocal nature of these kinds of agreements and the complexity involved in dealing with tax matters. Explicit language should be included in BITs to exclude the possibility of extending MFN treatment to dispute resolution provisions, in light of pronouncements in the *Maffezini* case.²

² Since *Maffezini* there have been three more major cases dealing with the applicability of the MFN standard to dispute settlement before ICSID (*Salini*, *Siemens*, and *Plama*). While *Maffezini* and *Siemens* are in favour of it, *Salini* and *Plama* say, at least in principle, the opposite, focusing on the intention of the parties as the decisive factor. In this view, incorporating dispute settlement provisions from other treaties via the MFN clause is only possible if the parties to the BIT have a clear and unambiguous intention to do so. The RSA-Korea BIT makes provision for the application of treatment as regards to "...management, maintenance, use, enjoyment or disposal of their investments, treatment not less favourable than that which it accords to its own investors or to the investors of any third State." It would seem that MFN treatment is limited only substantive provisions in relation to the investment. This formulation could be another method of overcoming the unlimited application of the MFN clause to non-substantive provisions.

5. EXPROPRIATION

5.1 Introduction

Most BITs have always guarded against this possibility, and continue to express investors' fears of being expropriated unlawfully. States are not prohibited from expropriating foreign investments, merely that if expropriation does take place that it is done on a non-discriminatory basis, for a public purpose and against payment of compensation. The right of host countries to expropriate or nationalise foreign property, subject to certain requirements, has been recognised in BITs. The prerequisite conditions for lawful expropriation of foreign investors by host countries have been considered to be the following: it had to be taken for a public purpose, on a non-discriminatory basis, under due process of law and based upon the payment of prompt, adequate and effective compensation. However, the Hull formula (prompt, adequate and effective) has been contested by developing countries who maintain that the applicable criterion for payment of compensation is that of 'appropriate compensation.'

5.2 Terminology and differences between BIT expropriation standards and RSA domestic law

Although most BITs use the terms expropriation and nationalisation, most do not attempt to define either of the terms or try to clarify what the difference between said terms would be. The wording used in various BITs also incorporate additional language that extend protection to actions of a host country that may be 'tantamount' or 'equivalent' to expropriation or that may have an 'effect that is equivalent' to expropriation. The term 'indirect expropriation' is also encountered. What constitutes expropriation remains a deeply contentious issue. A comparison between various BITs, as compared to domestic law, has demonstrated that

standards with relation to expropriation differ from standards under domestic RSA law.

BITs do not make a distinction between deprivation (Section 25(1) of the property clause) and expropriation (Section 25(2) of the property clause). The concept of nationalization is not used in the constitution, while terms such as '*measures having effect equivalent*' to expropriation are totally absent from the RSA's constitutional vocabulary. The failure to distinguish between regulation and expropriation leaves the prospect that legitimate government regulation will be deemed to constitute a form of 'indirect' expropriation.

5.3 Measure of compensation

Further requirements of such BITs (depending on the language and approach) state that prompt, *adequate* and effective compensation is paid. In this regard there have been some differences between the various RSA BITs. The RSA-Italy BIT (1997) calls for '*immediate, full and effective compensation*'. The jurisprudence of Article 25 of the RSA Constitution, though limited to date, indicate that '*less than market value*' compensation may be awarded to claimants, especially where compelling public interest purposes lie behind the expropriation of property. There is a clear tension between the BIT standards of '*full and effective compensation*', '*market value compensation*' and the '*less than market value*' compensation prescribed by the constitution. A clear example of this tension is the conversion of '*old order rights*' into '*new order rights*' under the MPRDA and the claims by some investors that such a conversion leaves them worse off than before. The debate about expropriation and related standards of compensation has further been informed by the Expropriation Bill [B 16 – 2008] which was published in the Government Gazette on 11 April 2008. This bill was recalled, however the Department of Public Works intends to launch a new consultative process to revise the bill.

6. TRANSFER OF FUNDS

6.1 Introduction

This Article assures investors of their ability to move their funds from the place of the investment to the home state. In the light of the importance of transfer obligations to foreign investors, a country wishing to attract investment stands therefore to benefit from the inclusion of a comprehensive and sufficiently detailed transfer provision. But a host country may also seek qualifications, the most important of which relates perhaps to the ability of the country to impose restrictions on transfers in response to balance-of payments crises.

6.2 Recent trends

Most BITs include a clause on the transfer of funds, which gives foreign investors the right to transfer funds related to an investment without delay, and to use a particular currency at a specified exchange rate. At the same time, a significant number of BITs contain exceptions, mainly to ensure compliance with specific laws e.g. on insolvency or to safeguard flexibility for host countries to properly administer financial and monetary policies. There are differences regarding whether the provision covers both inbound and outbound transfers, whether any kind of transfer is protected or only those explicitly mentioned, and whether the transfer right is subject to national law. The majority of BITs do not contain an exception clause dealing with a balance-of-payments crisis (UNCTAD: 2007 57).

The first group of BITs contains a transfer clause covering only transfers of funds out of the host country.³ The inclusion of the right to make transfers *into* the host country is more common in BITs granting the investor a right of establishment.

³ Belgo-Luxembourg - Hong Kong BIT (China) (1996).

As most BITs do not go so far, the transfer clause usually focuses on the stage once the investment has been undertaken. A second group of BITs contain transfer clauses that explicitly apply to inbound and outbound transfers.⁴ Another category of BITs has transfer clauses that do not explicitly apply to inbound and outbound transfers, but nevertheless use language general enough to have this effect.⁵

6.3 RSA practice in relation to the transfer of funds

The RSA does not impose any exchange control of foreign investors or restrictions on the repatriation of profits. A general feature of the RSA's BITs is that the transfer of payments be made without delay, in freely convertible currency, at market rate of exchange applicable on the date of transfer. It has adopted two approaches to the transfer of payments that seems to contemplate only outbound transfers. The first approach is to guarantee the free transfer of all payments related to, or in connection with, an investment. Due to the uncertainty that may arise over which payments are covered by this provision, a non-exhaustive list of payments that are to be covered is included (see BITs with Chile, Czech Republic, Egypt, Greece, Mauritius and Spain). The second approach is simply to list the types of payments covered by the provision (e.g. Denmark, France and Iran). In some instances the transfer of payments may be limited.

The Protocol to the BIT between the RSA and Chile provides that capital invested may only be repatriated one year after it has entered the territory of a party, unless legislation accords more favourable treatment. Free transfer provision do not apply to nationals of one country that may acquire permanent residence in the RSA and who have decided to immigrate and who have completed the

⁴ Japan - Viet Nam BIT (2003).

⁵ Malaysia - Saudi Arabia BIT (2000) .

exchange control formalities once a five year period from the date of immigration has lapsed (see Protocols to BITs with Denmark, Argentina, Czech Republic, Finland, Germany, Greece, Mozambique, Netherlands, Spain, Sweden and Switzerland). In each of these instances it is provided that the provision shall terminate upon removal of the relevant Exchange Control limitations by the Republic of South Africa. The RSA undertakes every effort possible for the early removal of exchange control.

7. DISPUTE RESOLUTION

7.1 Introduction

Dispute settlement is a key institution for implementation of trade agreements. BITs typically allow for investors to directly initiate arbitration with host states, using what is known as an investor-state dispute mechanism. This has led to the introduction of the investor-state dispute settlement process in BITs. This process contrasts with the process used in trade law, which is an exclusively state-state. International dispute settlement was originally designed to resolve specific instances of conflict between states and between private parties. It was not designed for disputes between private parties and states that require much more elaborate procedural safeguards to protect the rights of both parties. It was also not designed to create a body of interpretation that could shift the balance of rights and obligations of parties to an agreement or of those affected by it.

7.2 Impact of investment dispute provisions

Investment dispute settlement has now embarked on a course that effectively assigns dispute panels an active role in implementation and interpretation. Investors have become aware of the attractive *status quo* under the global investment regime – literally hundreds of long-ignored investment treaties offer investors access to an investor-state dispute settlement mechanism, allowing

them to take their disputes directly to international arbitration – leapfrogging domestic legal systems (and thus, any safeguards designed to protect important public goods). Some investors are using bilateral investment treaties to challenge treatment of foreign investments in various sensitive areas, including water and sewage provision, oil and gas exploitation and mining concessions. Major law firms are using BITs as the tool of choice for challenging host state regulation of public services.

Central to any developing country agenda on investment is a requirement to ensure that the approach to dispute settlement is fully revisited. There is no compelling reason why review of an investor’s claims against a state cannot be undertaken by the institutions of the state in question—provided these are independent of the public authority that is in dispute and they discharge their duties in accordance with basic principles of good governance, including an independent judiciary. Unfortunately, there is little indication in the texts of BITs that negotiators have acted with prudence to promote better domestic dispute settlement in the host state.

7.3 Conclusions regarding dispute resolution provisions in BITs

Existing dispute settlement institutions were not designed to address complex issues of public policy that now routinely come into play in investor-state disputes. They were created at a time when there was little international investment, few international investment agreements and scant discussion of what the appropriate rules for a globalised economy might look like.

In response to criticism, some modest changes have occurred in some of the available dispute settlement institutions. Disputes filed with ICSID, which is closely linked to the World Bank, are now listed on a publicly available register.

An arbitral panel (operating under rules of the United Nations Commission on International Trade Law, UNCITRAL) has accepted *amicus curiae* briefs.

Solutions to the issues of dispute settlement are available. They include greater transparency; selection of arbitrators in a neutral manner rather than by the parties; proper deference to domestic dispute settlement procedures; clear separation of the functions of arbitrator and advocate; and the introduction of an appellate process. Most of these changes by now appear inescapable. The precise manner in which these steps are taken must be the outcome of analysis, debate and proper negotiations, in which developing countries participate. Developing country host states are more affected by them than any other actors in the investment process by the simple fact of the number of arbitration claims they face, and will continue to face into the future.

8. DEVELOPMENTAL ISSUES

8.1 Introduction

Trade and investment are essential for sustainable development, and the imbalances that characterise and distorted global trade and investment flows must be addressed as a matter of urgency. Unequal and exploitative investment agreements, which prohibit the very policies developing countries need to fight poverty, is no way to put trade and investment at the service of sustainable development.

Existing international investment agreements are based on a 50-year-old model that remains focused on the interests of investors from developed countries. Major issues of concern for developing countries that are vital from the perspective of sustainable development are not being addressed in the current negotiating processes.

8.2 More Equitable Relations

In the light of recent experiences the RSA should assess to what extent an investment policy framework may be used to create more equitable relationships between investors and itself as a host state as well as the home state. In this context, difficult questions may arise regarding the standard of conduct that is expected from the investor. To what extent would investors incur liability for their operations in the host state? If so, to what extent can such obligations be enforced? This debate may be escalated to the question whether BITs should also create obligations for home states, thus to what extent may home states be required to ensure compliance of BIT obligations by their nationals?

8.3 The Right to Regulate

One of the most fundamental elements of state sovereignty is both the right and the duty of governments to regulate economic activities and actors in the broader public interest. The right to regulate arises out of the basic attributes of the sovereignty of states. While the duty to regulate arises from a range of domestic law elements (constitutional, administrative and legislative mandates); as well as from the international level.

While all BITs limit the regulatory flexibility within which contracting parties can pursue their economic development policies, more recent BITs include a wider variety of disciplines affecting more areas of host country activity in a more complex and detailed manner. Investment promotion and protection must not be pursued at the expense of other key policy objectives. The use of exceptions to general treaty provisions is a popular way to achieve this balance. Such exceptions cover a broad range of issues, including taxation, essential security interests and public order, protection of human health and natural resources, protection of culture and prudential measures for financial services. However such clauses may

raise more questions than answers due to the fact that some exclusion clauses are modeled on Article XX of the GATT of 1994. The transposition from a trade law to investment environment is not straightforward, and may lead to more interpretational difficulties.

8.4 Performance Requirement

Performance requirements are obligations imposed upon an investor by host state's public authorities. They are typically part of the pre-establishment negotiations conducted between a prospective investor and the relevant home state authorities. A wide range of performance requirements have been identified and fall into six broad categories: export performance; joint venture and equity ownership; research and development; technology transfer; employment and training; and other requirements such as local content requirements or the provision of surety in the form of bonds or otherwise. Performance requirements require an investor to give undertakings to meet certain criteria. Consequently performance requirements are widely seen as imposing an economic burden or otherwise decreasing the economic efficiency of an investment. Performance requirements are subject to a range of disciplines in some BITs, while others do not address them. The *Agreement on Trade-Related Investment Measures* (TRIMS) specifies that the RSA cannot give national investors any preferential treatment over foreign investors once they are established in the country. This means that no government law may require established investors to use domestic inputs (labour and suppliers) or limit a foreign investor's use of imported products to the volume or value of locally manufactured products that it exports. The RSA, for example, as part of its TRIMS commitments, abolished all local content performance requirements from its new Motor Industry Development Programme in 1995. To date, the RSA has not notified any performance requirements that do not conform to the Agreement. It must be noted that TRIMS

is not a comprehensive statement on investment and deals only with certain types of performance requirements. The main aim of TRIMS is to prohibit the use of certain types of performance requirements (i.e. such measures which cause 'trade restrictive and distorting effects'). An annex to the agreement contains an illustrative list of measures, thus not all performance requirements are prohibited, only those that fall within the narrow definition provided for in the TRIMS. There is no prospect of extending such limitations since developing countries strongly oppose such an extension.

8.5 Promotion of Human Rights through Investment Treaties

Host states may put certain policies in place that seek to promote and enhance human rights interest. Examples of such intervention may include a state's efforts to protect citizens from having their rights interfered with by foreigners, policy measures designed to promote the right to food, the right to health or the right to water. These measures may be challenged through international arbitration.

It is almost unheard of for BITs to include substantive clauses on human rights. Some RSA BITs include exceptions which shelters certain forms of human rights-inspired legislation which might affect foreign investors. However, these provisions are quite limited and provide exceptions only to one of more than a dozen investment treaty provisions. The question which arises is how and to what extent human rights should be considered in arbitral disputes, considering that very few BITs directly address this issue.

8.6 Standards of conduct for MNC's

Further, multinational corporations (MNCs) are not bound any international standards of conduct. The OECD Guidelines for Multinational Enterprises and the UNCTC Draft Code on Multinational Corporations may be useful instruments to

consider in the context of BITs. Globally businesses have been incorporating Responsible Business Conduct (RBC) and Corporate Social Responsibility (CSR) as part of core business strategies. Emphasis should be placed on how international standards and harmonisation could be accommodated in a legal framework that enhances RBC and CSR disciplines.

8.7 Home state rights and responsibility

Existing BITs do not address home state rights and obligations. Yet home states are indubitably stakeholders when it comes to foreign direct investment. The interests of home states are largely determined by their desire to ensure the security of their investors, who will in many instances be exporting capital from the home state and repatriating profits.

The obligations of home states are more difficult to define. Home states may be expected to provide certain information, assist in combating corruption and ensure that investor liability extends to the home state in an appropriate manner. An emerging problem is the use of “home states of convenience” by investors who have no substantial activity in those states, with the potential to undermine the effectiveness of BITs in much the way that flags of convenience render the control of shipping practices particularly difficult. Each of these areas presents challenges in terms of drafting and implementing BITs that promote development in host states.

The problem of “home states of convenience” can be resolved by making the designation of a home state a matter of mutual agreement between investor and host state, subject to certain principles that establish that an investor must have a material relationship to a designated home state. This approach permits the development of more substantive provisions concerning home state obligations.

The problem of corruption is widely recognized. Yet combating corruption that involves international investment is particularly challenging since it requires commitment and effort on the part of all actors, investors, home states and host states. Home states may be needed to ensure, in particular, that investors publish information on payments they make to public authorities or their agents in host countries, and to make corruption by investors a criminal activity at home, even for acts taking place abroad.

Finally, home states have a role to play when their investors incur liability in the host states through actions that originated in the home state, or when those who are liable are out of reach of host state authorities without assistance from home states. Home states have a much more active and important role than is generally recognized. The simple conclusion from the perspective of a Southern agenda is that many host states cannot respond appropriately to investment opportunities without the help of home states.

8.8 Investor rights and responsibility

The focus of many BITs is on investor rights; mention of investor obligations is rare. Yet an investment agreement that does not address investor obligations is manifestly incomplete. An international agreement between sovereign states that seeks to create specific investor obligations is in many ways problematic. International agreements are concluded between—and impose obligations on—states. Normally, they impose obligations on individuals only by obligating states to take all necessary measures to ensure that their citizens act in accordance with international agreements. Yet in the absence of enforcement by states, the enforcement of these rights through international institutions is exceedingly difficult.

BITs that create rights for investors move into an environment with few precedents. They have succeeded by subjecting the conduct of states to investor-state arbitration. They do not, however, take the next step and seek to create obligations for foreign investors.

A number of investor rights have emerged from existing BITs. They include a parallel to the non-discrimination approach that has served the trade regime well that is “national treatment,” “most-favoured-nation treatment” and dispute settlement.

Other key investor rights have also not been without problems. The most critical of these have been the right to a minimum standard of treatment by host states and protection against expropriation without compensation. The former is emerging, at least under some arbitrations, as an international law standard of transparency and good governance that is being imposed on host states. The latter has now been expanded to include claims to compensation for regulatory measures that impact the economic performance of an investment. To a significant degree these problems are attributable to lax drafting practices that many assumed were appropriate for agreements between states. From a developing country perspective, what seems more critical than the idea of investor rights is the ability to generate sufficient clarity in the scope of these rights so as to ensure both the investor and the host state has the capacity to function properly and without undue fear or burden.

9. Recent Arbitral Decisions by tribunals and impact on BIT policy guidelines

At the end of 2007, of the 95 known treaty-based disputes in infrastructure investment, 38 had been concluded either through settlement (20) or a final decision of the arbitration tribunal (18). Thus, the majority of the known disputes remained pending (57). The large majority of arbitral decisions have addressed one or more of the following investment protection standards: fair and equitable treatment, expropriation and the umbrella clause (UNCTAD, 2008 166).

Several infrastructure-related investment disputes are based on alleged violation of the *fair and equitable* standard. Recent arbitral cases tended to interpret this principle broadly, which does not only limit state conduct to cases that are aimed to undermine investments. The 2007 award in *Parkerings-Compagniet v. Lithuania* the tribunal expressly recognized the host state's right to policy space in its analysis of 'like circumstances'. The issue of direct expropriation is also prevalent as demonstrated by the case of *ADC v Hungary*. In this case the tribunal found that the government's take-over of the investor's activities concerning the operation of two terminals at Budapest airport did not comply with the requirements of a lawful expropriation.

The issue of expropriation of contractual rights has also emerged in infrastructure related investment. The problem is the difficulty of distinguishing between normal contractual breach and the expropriation of contractual rights. For the latter investment tribunal require that (a) the host state acted in its sovereign capacity and (b) the breach of contract has given rise to a substantial decrease in the value of the investment. In the case of *Vivendi v Argentina* the tribunal concluded that the claimants' concession rights had been expropriated because conduct of the Argentinean province constituted a sovereign act that "struck at the economic heart of [the company], and crippled the claimant's investment."

An issue brought several times before arbitration tribunals is whether the umbrella clause protects against breach by the host State of any kind of obligation it has entered into vis-à-vis a foreign investor (e.g. a commercial contract), or whether such protection is limited to obligations entered into by the host State in its capacity as a sovereign (e.g. a concession agreement). This distinction can have huge implications for the host country. For example, under a broad interpretation of the umbrella clause, a “mere” dispute about the agreed quantity of electricity to be purchased by the host State from the investor could give rise to treaty-based arbitration. A narrow understanding would exclude arbitration in this case, unless the purchase commitment was included, for example, in a concession agreement. Arbitration tribunals have taken different stances on this issue. While the tribunal in *LESI-DIPENTA v. Algeria* opted for a broad interpretation, the one in *El Paso v. Argentina* excluded ordinary commercial contracts from the scope of the umbrella clause (UNCTAD, 2008 167).

10. POLICY RECOMMENDATIONS

10.1 Introduction

The balance of power in North–South negotiations is tipped heavily in favour of developed countries and large, politically influential corporations. Much of the recent debate and controversy in BITs has revolved around the policy space that developing countries need to promote development. Adequate policy space is a key developmental tool for developing countries. However, the current BITs extend far into developing countries’ policy space, imposing damaging binding investment rules with far-reaching consequences for development. New investment rules in BITs prevent developing country governments from requiring foreign companies to transfer technology, train local workers, or source inputs locally. Under such conditions, investment fails to encourage or enhance

development. BITs allow foreign investors to sue for lost profits, including anticipated future profits, if governments change regulations, even when such reforms are in the public interest.

For its part, the RSA faces some challenges regarding the provisions of BITs already concluded. The legal and business community is increasingly aware of the protections available under BITs, and increasingly inclined to invoke those rights in the face of undesirable government initiatives or proposals. Accordingly, the RSA has to review its stance on BITs, so as to ensure that they are in harmony with the country's broader social and economic priorities.

10.2 Policy options

10.2.1 Assessing present liabilities

A preliminary step which the RSA is already embarking on is to review its current BITs commitments, as an exercise to do damage control. As questions arise regarding the divergence between protections offered under South African law and under investment BITs, these international agreements should be subjected to much closer scrutiny and review.

The RSA might learn from the experience of other countries which have already undertaken a review of their own BITs commitments. After losing a \$350 million (US) lawsuit, the Czech Republic set up a parliamentary commission to examine its investment treaty programme (Vis-Danbat: 2006). There has already been one arbitral decision against the RSA, with another case pending before an ICSID tribunal. While amendment of already concluded and ratified BITs is not possible, a review of commitments under such BITs may point out possible liabilities for the RSA. Many of the initial BITs signed after 1994 will soon expire and this may be an opportunity for the RSA to reassess its position regarding the form and content of such instruments.

10.2.2 Minimizing future liabilities

Demands for the conclusion of additional BITs are unlikely to recede. *Demandeurs* include not only foreign governments, but the RSA's own business community who seek protection for their outward-bound investments. Such demands have been a factor motivating a number of recent BIT negotiations. Ultimately, some level of international investor protection may be unavoidable – as a supplement to protections found in domestic law – however; there is an accompanying need to make a clear assessment of the potential downside of such BITs. To this end, the RSA should review its BIT practices, with a view to developing a model BIT which is in line with its development needs, balancing the need for investor certainty on the one hand, but also ensuring that its own legitimate interests are not compromised. Further domestic legislative intervention may be needed to ensure that such a balance is achieved.

11. AUTHORITIES

1. Policy Documents

Accelerated Growth and Shared Initiative for South Africa (ASGI-SA)

Co-ordination of International Relations strategy

Economic Diplomacy Strategy

National Industrial Policy Framework (NIPF)

Global Economic Strategy Document

2. Publications

2.1 Journal Article and Institutional Publications

Peterson L.E "South Africa's Bilateral Investment Treaties. Implications for Development and Human Rights." (2006) Friedrich Ebert Stiftung, SAIIA, IISD Berlin.

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2.2 Books

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3. Cases and arbitral awards

3.1 International cases and awards

ADC v Hungary (ICSID Case No ARB/03/16) (2006)

ADF v United States (Case No ARB (AF)/00/1) (2003)

CASE CONCERNING THE BARCELONA TRACTION, LIGHT AND POWER COMPANY, LIMITED (NEW APPLICANT: 1962) (*BELGIUM v. SPAIN*)
PRELIMINARY OBJECTIONS JUDGMENT OF 24 JULY 1964 *COUR INTERNATIONALE DE JUSTICE*

CMS Gas Transmission Company v The Republic of Argentina (Case No ARB/01/8, judgment delivered on 17 July 2003)

El Paso v. Argentina (ICSID Case No ARB/03/15) (2006)

Foresti and others v the Republic of South Africa (ICSID Case No ARB(AF)/07/1)

EMILIO AGUSTÍN MAFFEZINI (CLAIMANT) and THE KINGDOM OF SPAIN (RESPONDENT) (ICSID CASE NO. ARB/97/7)

SALINI COSTRUTTORI S.P.A. AND ITALSTRADE S.P.A. AND THE HASHEMITE KINGDOM OF JORDAN (ICSID CASE NO. ARB/02/13)

Siemens v Argentina (ICSID Case No. ARB/02/8) (2007)

Parkerings-Compagniet v. Lithuania (ICSID Case No ARB/05/8) (2007)

Plama Consortium Limited (Claimant) and Republic of Bulgaria (Respondent) (ICSID Case No. ARB/03/24)

Vivendi v Argentina (ICSID Case No ARB/03/19)

3.2 South African case law

President of the Republic of South Africa v Nello Quagliano and others Case CCT 24/08 [2009] ZACC 1

4. Legislation

4.1 Acts

Constitution of the Republic of South Africa Act No 108 of 1996
Mineral and Petroleum Resources Development Act, No 28 of 2002

4.2 Bills

Expropriation Bill [B 16 - 2008] which was published in the Government Gazette on 11 April 2008

5. Treaties and Protocols

5.1 Multilateral Treaties

Agreement on Trade Related Investment Measures (TRIMS) 1995 (WTO)

5.2 Regional Treaties

SADC Protocol on Finance and Investment (FIP)

6. Other Instruments

The OECD Guidelines for Multinational Enterprises (1992)

The United Nations Commission on Transnational Corporations (UNCTC) Draft Code on Multinational Corporations

Charter of Economic Rights and Duties of States