

A Road Map for Cotonou Investment Negotiations

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A Road Map for Cotonou Investment Negotiations

Much has been written about foreign direct investment and yet success in attracting such investment remains elusive. At one level, investment decisions are a matter of the relationship between risk and return, given the constraints of capital, which is in limited supply in most developing countries. Governments can act to create perfect institutional conditions for FDI, and no FDI flows, for lack of infrastructure, markets or needed private institutions. Infrastructure may be constructed and no FDI flows. International Financial Institutions can provide support to improve the risk/return relationships, and no FDI flows. Bilateral investment agreements may have been concluded, and no FDI flows. Skilled labor may be available at modest cost, and still no FDI flows. At the same time, FDI may flow towards countries with problematic institutions and limited infrastructure. It would appear that the ability to attract FDI is marked by numerous identifiable conditions that may be necessary but none of which are themselves sufficient conditions. Investment agreements must promote these conditions but the result in terms of actual investments will never be automatic. This renders the negotiation of investment agreements difficult from the perspective of developing countries.

1. Identify a clear purpose.

International investment agreements have not generated identifiable benefits. Liberalization of investment and investor protection do not automatically lead to more investment or any other economic benefit. There is no theory of liberalization of investment rules that suggests what benefits may accrue and how. Under these circumstances it is vital to identify clear objectives for a Cotonou Investment Agreement. Then it becomes possible to determine subsequently whether the objectives have been met.

The purpose of a Cotonou Investment Agreement is:

To increase long term foreign investment into the ACP countries for activities that support the sustainable development goals of the host country, consistent with the Cotonou Partnership Agreement (CPA).

2. Identify the principles on which a Cotonou Investment Agreement is to be based

Negotiations must focus on establishing a number of core principles that are essential to ensure a stable and supportive environment for long term foreign direct investment that supports the sustainable development objectives of ACP countries.

2.1. Balance between investor rights, development objectives and the protection of public goods.

This is the core principle for any investment agreement, which must promote the development of the necessary domestic and regional institutions. This principle must also apply to all the institutions of the Agreement itself.

2.2. *Legitimacy.*

Actions of public authorities must be based on the rule of law and the principles of good governance.

2.3. *Transparency*

The most effective tool to ensure the respect of principles of an Investment Agreement is to achieve high standards of transparency

2.4. *Accountability*

Actors at all levels must be held accountable for their activities, based on legitimately determined criteria.

Note that these principles subsume the concept of non-discrimination that is often presented as the primary basis for international investment agreements.

3. Establish criteria for success

Investment is a complex process, involving numerous factors, only some under the control of governments. It will consequently be necessary to develop a system of criteria to determine whether a Cotonou Investment Agreement is achieving its goals. This is a matter for negotiation (see Annex 1).

3.1. *Create an ACP Investment Observatory to monitor results*

Given greater reliance on FDI as a means to achieve the sustainable development objectives of ACP countries it will also be necessary to monitor results much more closely. An ACP Investment Observatory is proposed for this purpose.

3.2. *Include commitments to take measures to improve performance should the Agreement not achieve its objectives, as determined by the criteria.*

The Agreement must include a process by which its performance is regularly reviewed and steps are taken as needed to increase chances for success.

4. Distinguishing and incorporating pre-establishment and post-establishment rights

The negotiation of investment agreements today includes two distinct phases associated with investment, pre-establishment and post-establishment. Pre-establishment rights indicate what areas are open for investment by foreign investors, and what rights are available to them prior to making, or completing the opening of, an investment. Post-establishment rights deal with how an investor is treated after the investment is made. The scope of pre-establishment rights is a critical aspect of the relationship between an investment agreement and the right of host states to promote and direct their own development strategies.

- 4.1. ***Pre-establishment rights should be limited to those that are supportive of national development strategies.***
They should be based on positive lists of industries or sectors where foreign investment is considered appropriate.
- 4.2. ***Phase in periods for future investment liberalization, if included at all, should also be consistent with, and not in advance of national development strategies.***
This requirement is often difficult to meet since phase-in periods are typically the result of last-minute compromises rather than of a considered balancing of means and objectives.
- 4.3. ***The establishment of performance requirements for foreign investors will be addressed in most negotiations.***
There is a critical relationship to national development strategies. Empirical evidence suggests, however, that high levels of performance requirements act as a strong disincentive for foreign investments. Some developed countries seek the elimination of host country rights to set out performance requirements. We do not believe this is necessary or appropriate, but note that while the right to do so may be maintained in an agreement, the use of such requirements carries market-based risks of losing investments.

The pre and post-establishment phases also help set out a useful grid of rights and obligations that can guide negotiators.

5. Within the framework of the principles outlined, identify host state rights and obligations

- 5.1. ***Host states are responsible for articulating and implementing their sustainable development objectives in a manner that is consistent with the principles set out above.***
These objectives deserve the respect of investors and the institutions of a Cotonou Investment Agreement.
- 5.2. ***Host states are responsible for maintaining a stable, transparent and non-arbitrary environment.***
The law must be applied in a manner that is fair and equitable.
- 5.3. ***Host states must provide investors with review and recourse to ensure that their rights have been respected.***
The Agreement will additionally provide international dispute settlement (see below)
- 5.4. ***Host states will maintain the rights to protect themselves in foreign currency crises***
- 5.5. ***The Cotonou Investment Agreement must provide EU support to these functions.***

6. Within the framework of the principles outlined, identify investor rights and obligations

6.1. *Once an investment has been made, foreign investors are economic citizens of the host country.*

They must enjoy the same rights that domestic investors enjoy under like circumstances. They must be free to repatriate legitimate profits and to move key employees as required by their enterprise. Foreign investors will be expected to respect the best practices as set out in internationally agreed Guidelines and Codes of Conduct.

6.2. *Foreign investors must be free from discrimination based on their nationality*

6.3. *Foreign investors have the same obligations that domestic investors do.*

They must obey the law and support the development objectives of the host state. ACP countries should also, however, consider establishing minimum international standards of conduct for foreign investors in both the pre and post-establishment phases. Areas where such minimum standards can be usefully established include environmental impact assessment of a proposed investment; environmental management system standards (based on ISO 14,000); respect for reference human rights standards as set out in specified international human rights instruments; respect for core labour standards as set out by the ILO; corporate reporting responsibilities; and anti-corruption responsibilities as a minimum set of duties.

7. Within the framework of the principles outlined, identify home state rights and obligations

7.1. *Home states must support the efforts of host states to articulate their development objectives and to ensure that foreign investment supports these objectives.*

Home states must supply host states with appropriate information concerning practices in the area of investment under consideration. Upon request they must supply information that may be available to them about an investor's practices.

7.2. *Home states shall also assist in promoting foreign investment into ACP through country or region specific FDI-promoting activities.*

This activity will be part of the broader Cotonou Partnership. It should include site visits by home state authorities.

7.3. *Home states should be prepared to ensure that investors have liability for the investment decisions they make at the location of those decisions.*

This includes decisions made in the home state: the right to make profit has to carry with it the liability for damages caused in the making of those profits. This is already part of European law within the EU.

8. Create a structure to reward good governance

Good governance is widely viewed as an important factor in attracting long term foreign investment. A Cotonou Investment Agreement must create incentives to reward good governance. In this respect it meshes easily with the CPA.

8.1. *Establish criteria for “good governance”*

In order to provide incentives to reward good governance it will be necessary to agree criteria and the manner in which they are to be applied. This is a problem the Cotonou Investment Agreement shares with the CPA itself. See Annex 2 for a List of possible criteria.

8.2. *See the Report “Lowering the Threshold” for options¹*

The report outlines a number of practical options to improve the situation of small and vulnerable economies (SVE) countries. These can be implemented in connection with a Cotonou Investment Agreement.

8.3. *Exhaustion of remedies.*

In countries with recognized good governance, investors will be expected to exhaust domestic remedies before using regional or international dispute settlement.

8.4. *Deference.*

In countries with recognized good governance, regional and international dispute settlement will be required to show deference to the sustainable development goals as well as to measures taken by public authorities in their furtherance when considering investor claims within a dispute.

9. Establish international dispute settlement that corresponds to the above principles

Dispute settlement has emerged as a major issue in international investment agreements. For a number of reasons, investor-state dispute settlement is a necessary component of investment agreements that have a chance of being successful. Any dispute settlement system established by a Cotonou Investment Agreement must meet the fundamental principles and the criteria of good governance that underlie the Agreement.

9.1. *Existing arbitration systems do not correspond to the principles outlined above.*

The existing systems (the International Center for the Settlement of Investment Disputes (ICSID) and the United Nations Committee on Trade Rules and Law (UNCITRAL) in particular are lacking in terms of legitimacy, transparency, and accountability. They are unacceptable when matters of development policy and public goods are being decided.

9.2. *Procedures must be transparent, with a proper public record of proceedings and decisions*

With matters of development and public goods at stake, the dispute settlement process must meet basic standards of due process. This includes as a minimum:

¹ Anthony Hughes and Havelock Brewster, *Lowering the Threshold. Reducing the Cost and Risk of Private Direct Investment in Least Developed, Small and Vulnerable Economies*. London: Commonwealth Secretariat, 2002.

- Public notification of all claims under an Agreement
- Public access to all documents issued in the course of a claim, subject to business confidentiality protections
- Public access to all oral hearings;
- Rights of a tribunal to accept amicus submissions according to a defined process

9.3. *Members of dispute panels or judicial bodies must be chosen by a procedure that is neutral and legitimate*

Litigants should not be able to participate in the selection of panelists. Panelists must be publicly accountable, for example for conflicts of interest. They should be chosen from a standing body of people with expertise in investment and sustainable development matters.

9.4. *Decisions by panels must be subject to a process of review*

Experience in the WTO has shown that review by a standing body is essential to correct the numerous mistakes that are bound to occur in an ad hoc procedure. If permanent bodies are constituted for the first instance then review is necessary to promote consistency in interpreting the law.

10. Invest in regional institutions to support long term foreign investment

A significant development of regional institutions is one of the central pillars of the CPA. These institutions must be integrated into the Investment Agreement.

10.1. *Support the development of regional markets*

Investment requires markets. Many ACP countries, smaller and SVE countries in particular, do not have sufficiently large markets to attract the levels of investment envisaged by the CPA. This requires continuing effort on the part of the Partners.

10.2. *Develop regional administrative institutions*

Certain administrative functions essential to promoting sustainable development in connection with long term investment can also be provided at a regional level, in particular where human resources at country level are limited. This requires investment and capacity building by the Partners.

10.3. *Develop regional judicial institutions for investment*

In light of the need for investor/state dispute settlement, the options for regional institutions need to be explored. This can also create the possibility of keeping disputes closer to the host country and increase the chance that panelists will know local conditions and provide more balanced interpretation.

10.4. *Invest in regional infrastructure*

Infrastructure is important if goods and services produced by foreign investment are to be exported. There are opportunities for the development of regional infrastructure from which several countries can benefit.

11. Replace existing bilateral investment treaties (BITs) with a single Cotonou Investment Agreement.

The CPA Partners have signed numerous BITs among themselves. The provisions of these BITs are quite heterogeneous but few if any meet the standards outlined here for a Cotonou Investment Agreement. One goal of negotiations must be the replacement of the BITs by a single Cotonou Investment Agreement. An Agreement that meets the objectives and principles outlined here will be more effective at protecting investor rights as the existing BITs, whose effectiveness as a tool of development is very doubtful.

12. Establish a Cotonou Investment Fund

Attracting long term foreign investment that supports the sustainable development objectives of the CPA requires a comparable long term commitment from the Cotonou Partners. An Investment Fund can create a framework for articulating many of the investment goals of the CPA.

12.1. Governance of the Cotonou Investment Fund must include all Partners

Governance is critical for investment, and this must begin with the funding envelope that is designed to support the investment provisions of the CPA and the Cotonou Investment Agreement.

12.2 The Cotonou Investment Fund must learn from the experience of recently established institutions.

Special attention needs to be given to the experience of institutions such as the European Bank for Reconstruction and Development (EBRD) that was explicitly designed to support private investment and has evolved a number of new procedures to reach SMEs in its target region.

12.3. The Cotonou Investment Fund must be able to support all the objectives and provisions of the Cotonou Investment Agreement.

One of the benefits of an investment fund that enjoys institutional support from all Partners is that it can give concrete meaning to the permanence of their commitment to the investment dimension of the CPA.

12.4. The Cotonou Investment Fund must have a special emphasis on SVE countries

The ACP countries include a significant number of SVE countries whose special needs require institutional recognition. See “Lowering the Threshold.”

12.5. The Cotonou Investment Fund must be able to support small and medium enterprises

SMEs are likely to represent the most important source of economic growth in ACP countries, just as they have in developed economies. Yet supporting SMEs has proven particularly difficult. It requires the kind of sustained commitment that only a properly institutionalized Fund can provide..

Annex 1: Possible Criteria for Assessing the Success of an Investment Agreement

- 1.1. Change in total long term foreign investment into ACP countries, individually and collectively
- 1.2. Change in total long term foreign investment into ACP countries relative to global economic growth
- 1.3. Total long term foreign investment into ACP countries relative to these countries' economic growth
- 1.4. Total long term foreign investment into ACP countries relative to global long term foreign investment
- 1.5. Total long term foreign investment into ACP countries relative to long term foreign investment into developing countries.
- 1.6. Number of top ten projects for sustainable development funded
- 1.7. Royalties paid by foreign investors
- 1.8. Taxes paid by foreign investors
- 1.9. Foreign investment by sector and country
- 1.10. Size of firm receiving foreign investment
- 1.11. Number of jobs related in foreign investment
- 1.12. Housing supported by foreign investors

Annex 2: Possible Criteria for Good Governance

- 2.1. Standing under ACP good governance review
- 2.2. Existence of WTO trade policy review
- 2.3. Number of building permits issued
- 2.4. Average time for issuance of permits
- 2.5. Number of civil servants employed per permit
- 2.6. Average time for judgment in first instance in civil court cases
- 2.7. Average time for review of judgments in civil court cases
- 2.8. Position on internationally recognized corruption index
- 2.9. Position on internationally recognized transparency index
- 2.10. Freedom of information legislation—and statistics on its use
- 2.11. Existence of publicly accessible toxic release inventory
- 2.12. Publication of royalty receipts
- 2.13. Adherence to specified international environmental agreements
- 2.14. Adherence to specified international labour standards
- 2.15. Adherence to specified international human rights standards
- 2.16. Existence of infrastructure for ISO certification
- 2.17. Percentage of large enterprises with ISO certification