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Research Report

Lessons from South Africa's BITs review

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Lessons from South Africa's BITs review

by

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Proponents tend to argue that bilateral investment treaties (BITs) encourage investment and strengthen the rule of law particularly in jurisdictions where court systems are weak or biased against foreigners. This premise is contested. First, studies on BITs and FDI suggest the relationship is, at best, ambiguous and that BITs are neither necessary nor sufficient to attract FDI.¹ Indeed, South Africa receives FDI from investors in countries with whom it has no BIT and often little or no FDI from others where a BIT was in place.

Second, one may legitimately ask whether the rule of law is adequately upheld in the investor-state dispute settlement (ISDS) system or in the BITs that underpin it. BITs, particularly early generation treaties, contain provisions that are imprecise and when subjected to international arbitration, leave wide scope for inconsistent and unpredictable outcomes. There is also growing awareness of deficiencies in ISDS, including with respect to its *ad hoc* nature, its fragmentation and a perceived lack of transparency and legitimacy. The problems appear deep-seated as jurisprudence in this area continues to diverge and, in the absence of an appellate process, often falls short of meeting the standards of legal correctness and consistency.² Imprecise treaty provisions, inconsistent arbitration awards, combined with a growing number of investor claims that are challenging a widening ambit of government public policy measures, are cause for growing concern.³

In 2010 the South African government concluded a three-year review of its BITs. The review assessed the role of foreign investment in South Africa, the levels of protection afforded to investment, and the risks and benefits of BITs. Overall, the review confirmed the observations above, and suggested that the current system open the door for narrow commercial interests to subject matters of vital national interest to unpredictable international arbitration that may constitute direct challenges to legitimate, constitutional and democratic policy-making.⁴

The review observed that FDI has been central to South Africa's economic development. Today, foreign firms are present in all sectors of the economy and FDI continues to grow. South Africa ranks amongst the most open jurisdictions in the

world and it provides investment protection through domestic law that is consistent with the highest international standards. Horizontal protection established in the constitution and legislation is complemented by sectoral regimes that cover, among other things, finance and banking, communications and mining. Foreign investors are treated in the same way as domestic investors are, and all have equal access to administrative justice. South Africa's legal framework provides that property may be expropriated only in accordance with the law of general application and for a public purpose. Expropriation is subject to compensation, the time and manner of which must be just and equitable, and must reflect an equitable balance between the public interest and the interests of those affected.

Taking all this into account, the South African Cabinet assessed the country's BITs and decided in July 2010 that South Africa would: refrain from entering into BITs unless there are compelling political or economic reasons to do so; terminate existing BITs and offer partners the possibility to re-negotiate BITs on the basis of a new model; develop a new Foreign Investment Act that is aligned with the constitution and clarifies typical BIT provisions under South African law; and establish an Investment Ministerial Committee to oversee this work.

A new Investment Bill was presented for public comment in November 2013.⁵ The Bill does not introduce any new restrictions on investment but clarifies the non-discriminatory protections offered to all investors from all countries. It confirms that South Africa remains open to FDI, providing effective protection while preserving the sovereign right of the government to pursue legitimate public policy objectives in line with constitutional requirements. While the process of terminating early generation BITs has been initiated in consultation with partners, South Africa has not ruled out the possibility of entering into new agreements if there are compelling reasons to do so. This will be subject to a decision by the Inter-Ministerial Committee, and treaties will need to be consistent with the new model that has been adopted at the regional level in Southern Africa.⁶

South Africa envisions a legal and policy framework for investment that learns from the lessons of the past and is better attuned to the challenges of sustainable development and inclusive growth. Equitable relationships between investors and government, based on respect for human rights, the rule of law and due process, and security of tenure and property rights, will continue to be pursued within the framework established by the constitution. The South African government's approach offers one route to addressing growing concerns with outdated BITs.

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¹ Mary Hallward-Dreimeier, "Do bilateral investment treaties attract FDI? Only a bit... and they could bite," in Karl Sauvant and Lisa Sachs, eds., *The Effect of Treaties on Foreign Direct Investment* (New York: OUP, 2009).

² UNCTAD, *World Investment Report 2012* (New York/Geneva: United Nations, 2012); UNCTAD, "Recent developments in investor-state dispute settlement", *IIA Issues Note*, No. 1 (May 2013).

³ *Ibid.*

⁴ South Africa Department of Trade and Industry, Bilateral Investment Treaty Policy Framework Review (2009), <http://www.pmg.org.za/policy-documents/2009/06/25/bilateral-investment-treaty-policy-framework-review>.

⁵ For a copy of the draft Bill, see <http://www.tralac.org/files/2013/11/Promotion-and-protection-of-investment-bill-2013-Invitation-for-public-comment.pdf>.

⁶ See Southern African Development Community, Investment Portal, <http://investment.sadc.int>.

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