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Perspectives on topical foreign direct investment issues

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FDI contracts should include investor obligations on sustainable development

by

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FDI contracts may be concluded by states and/or state-owned enterprises and MNEs, and they are usually regulated by the law of the host state. Unlike international investment treaties, through which states undertake obligations about the treatment of FDI in their territories, FDI contracts detail the commitments and economic benefits of states and investors for specific FDI projects.

FDI contracts, especially in the natural resources and energy industries, increasingly feature provisions committing investors to undertake tailor-made activities toward sustainable FDI. These "investor obligations regarding sustainable development", which sometimes may be based on domestic legislation, reflect states' efforts to maximize the contribution of FDI projects to local development and attenuate the negative environmental and social impacts of such projects.

Investor obligations may relate to:

- The employment and training of local workers, requiring investors to contribute financial and other means to reach given targets of employment and/or for the training of local workers.

  For example, the Philippines' FDI contracts establish that: "[t]he Contractor … shall, in consultation and with consent of the Government, prepare and undertake an extensive training programme suitable to Filipino nationals in all levels of employment". The program requires investors to reach specific targets of domestic employment, e. g., that, in Year 1, 75% of professional and management workers engaged in investment operations shall be Filipinos.

- The development of the local community, requiring investors to provide financial support, infrastructure and/or key services to the population affected by FDI and engage in stakeholder consultations.

  For example, Guinea's contracts oblige investors to pay a yearly amount corresponding to 0.5% of their turnover for the benefit of local communities and to conclude local development agreements. These agreements must establish, *inter alia*, procedures for the realization of social projects.

- Respect of human rights and the environment, obliging investors to perform impact assessments and create monitoring, management and/or recovering plans, and grievance mechanisms.

  For example, Brazil's model concession contract establishes that "[i]t is the duty of the operator company to continuously monitor all the activities that involve operational, environmental or human health risks, through a monitoring center, necessarily located in Brazil". Some contracts, e. g., Cameroon's contracts, may spell out what continuous monitoring consists of.

In addition, some FDI contracts affirm the state's right to adopt regulatory measures to protect health, safety and the environment. These provisions aim to prevent investor claims—under contractual stabilization clauses and treaty standards, such as fair and equitable treatment—rather than to impose obligations upon investors. For example, the Republic of Congo's and Mozambique's FDI contracts establish that stabilization clauses are not applicable to changes in legislation pertaining to health, safety, labor, social security, or the environment.

There are at least three benefits of including this type of clauses in FDI contracts:

- They commit foreign investors to contribute—through activities and finances—to host states' efforts to achieve sustainable development, considering the specificities of projects and the host communities involved. In this regard, FDI contracts go beyond the new generation of investment treaties that broadly prohibit investors to take actions that may endanger the enjoyment of human rights and/or the environment, or ask them to strive to comply with domestic rules or advance sustainable development.

- Violations of contractual obligations by investors may entitle host states to file claims against investors before arbitral tribunals, including ICSID tribunals (Art. 36). Moreover, FDI contracts may provide the basis for states' counterclaims and defenses in investor-state treaty arbitrations.

- They ensure the state's right to regulate. FDI contracts may prevent investors' claims (both under contracts and investment treaties) or offer defense arguments to states.

The above makes FDI contracts potentially effective in raising the bar of FDI governance toward sustainability in host states: the specific and proactive nature of obligations and the threat of states' claims and counterclaims may encourage compliance by investors. This, in turn, may help rebalancing the one-sided structure of the current investment law regime.

Yet, the benefit may be less than it seems due to the hesitancy of states—especially least developed ones—to initiate arbitration against investors under FDI contracts. States still face the costs, risks and negative publicity associated with arbitration. However, hesitancy may decline when contractual clauses are spelled out in clear and specific language, accompanied by effective monitoring, reporting and enforcement.

Overall, FDI contracts are more likely to advance sustainable development when they:

- Contain obligations for investors to conclude agreements with the local community (rather than to "make efforts", or to "negotiate").
- Identify local community representatives or set procedures for their identification.
- Clearly identify resources to be committed by the investor for training, local development, etc.
- Provide for monitoring and reporting, to ensure the community (and the state) remains abreast of developments through the life of investment projects, and mechanisms for accountability.
- Feature broad arbitration clauses to cover any breach of contract by investors.
- Safeguard states' right to regulate in the public interest.

One of the key challenges is to strengthen the negotiating capacity of host states (or to obtain international assistance available for FDI contract negotiations), with a view to improving host states' ability to maximize benefits and minimize negative effects derived from FDI projects.

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