EU CHAMBER OF COMMERCE AND INDUSTRY IN SOUTHERN AFRICA

PPIP comments, September 15. 2015

Speaker : Stefan Sakoschek, Chairman

EUCCISA, est. 2015, NPC.

- EU companies in SA
  - Long-term and substantive contributor to South Africa's economic growth, development and transformation.
  - 2,000 EU companies invested in South Africa – representing 77% of total FDI stock in the country. These companies have created over 300,000 direct jobs and approximately 150,000 indirect jobs.
  - Widespread provision of vocational and educational training, up-skilling, and management development.
  - EU investors have played an important part in technology transfer, with many high-tech, high skill companies located in South Africa. They also play a
  - Key role in export development, by operating African regional headquarters in South Africa to service operations throughout the African continent.
  - EU investment thus contributes significantly to the achievement of the objectives of broad-based Black Economic Empowerment.

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- **Macroeconomic Context**
- South Africa's present growth rate is far below the targeted 2019 growth rate of at least 5% growth rate as per NDP requirements of the NDP.
- With ZAR 460bn annual trade, the EU investment community considers itself a key partner in meeting this challenge through, *inter alia*:
  - creating more jobs; increasing exports; beneficiating more products in South Africa; and, through that, also managing the South Africa's trade deficit.
- With gradually increasing barriers to trade, and in a slumping global commodities market, SA exports natural resources *(transfer pricing..)*, and reimports consumer goods, often substandard, counterfeit, or "dangerous" for the consumer, and eroding the economy, creating an uneven playing field, for both EU and SA industrialists. *(E,g, WTO/GATT Art VII, emphasis on quality)*

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- Both the 2014 and 2015 SONA's, emphasised the need for:
  - removing obstacles to investment, improving private sector confidence in South Africa, and encouraging private sector investment.
  - As indicated previously, this Bill, as presently drafted, does not do that.

It also comes at a time when investors are concerned about the cumulative effect of several recent pieces of recent legislation on South Africa's investment climate.

Within the context of deteriorating external demand conditions, including the recently reported slowdown in China, it is crucial to retain certainty regarding the domestic investment climate, allowing business and government to collaborate on interventions to reduce domestic constraints.

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- Our comments

- General broad observations;
- Section-by-section highlighting of a number of salient issues, with proposals for redrafting (Annex 1);
- Conclusion.

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- GENERAL OBSERVATIONS
- The substance and detail of the Bill, viewed against its purpose**, does not provide for sufficient certainty or clarity regarding the substance and content of the domestic investment protection regime**.
- The Bill could invariably attract short-term investors, who do not pay much attention to investment frameworks, either because of the short turnaround time of their investments, or because they enjoy other preferential arrangements. We strongly believe that these kinds of investments are not of the character targeted by South Africa, and will not contribute to the country's transformation objectives pursued.

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- GENERAL OBSERVATIONS - Contd

- At this very moment we are aware of a number of projects that are pending due to the degree of **uncertainty** related to the investment framework. As we speak, some of our members are actively investigating other African destinations.
- **The current Bill sustains this discomfort** leading to discouragement related to new investments by a number of aspects discussed below.

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- GENERAL OBSERVATIONS Contd
- **Standard of Treatment**: In general, the Bill does not appear to EU investors to provide sufficient substantive protection – both absolutely and relative to other categories investors (both local and foreign). In fact, it appears, in parts, to even lock-in less favourable treatment for certain groups of investors.
- Even though the Bill "seeks to provide "**adequate and equal protection to [all classes of investor]**", as the explanatory memorandum to the Bill states (both *de facto* and *de jure*), it does not in fact do so. The review process has created quite a differentiated system of protection for different categories of investors. That is *vis-à-vis* domestic investors, and foreign investors whose BITs have not been terminated (or have been renegotiated).

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- GENERAL OBSERVATIONS Contd
- **Investment Promotion**: The EU Chamber is of the view that the Bill is lacking in substantive "promotion of investment" aspects.
- **Uncertainty over the Value of Treatment Offered by the Bill**: It is extremely difficult to determine scope and content of many of the sections of the Bill. Several sections in the Bill are still drafted in broad language or in an open-ended manner. Most investor rights contained in the Bill are subject to exceptions – and these, in turn, are by and large designated as non-exhaustive. Additionally, several of the provisions of the Bill rely on other pieces of legislation (many of which are in the process of review, or require review), to give shape and content to them.

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- GENERAL OBSERVATIONS Contd
- **Clear, transparent, and predictable investment rules** are critical factors influencing individual investors' long-term decisions to invest or reinvest, and at what levels. It is our opinion that the substance and detail of investment protections in this Bill do not covey the message of security and predictability to investors. It is our view, that this reduced certainty could not have been an intended consequence of this Bill.

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- Specific comments
- Measure
- It is not clear to the EU Chamber why the definition of ‘‘measure’’ ascribes the term to only administrative action. This definition is unduly limited, and does not cover the full gamut of measures as they are envisaged in this Bill. In the various references to measures contained in the Bill, it is clear that policy, legislation, and regulations are also included in the definition.
- *We propose the following definition be considered;*
- *“measure refers to binding governmental action directly affecting an investor or its investment, and includes laws, regulations, and administrative action …”*
- This definition is more consistent with the rest of the Bill; and is also in line with its commonly understood variations in investment protection nomenclature.

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- Specific comments Contd
- Investment
- The definition of “investment” does not comprehensively clarify whether minority equity investments by investors, i.e. portfolio or venture capital investments for example, who may or may not have established a corporation in South Africa, fall under the definition stipulated in the Bill and the memorandum. However, these financial investors provide relevant capital transfers into growth sectors, such as renewable energy projects and SMME’s in general. Further to that point, does the sole fact of being incorporated in South Africa constitute “a physical presence” as mentioned in the Memorandum?
- *We propose the wording amendments contained in Annex 1*.
- We are of the view that the proposed rewording still leaves the government at ease since hedge funds would not meet the "reasonable period of time” criteria.

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- Specific comments Contd.
- **Section 7: National treatment**
- The inclusion of the phrase “subject to national legislation” in the context of a national treatment section feels overly-broad, all-encompassing qualification.
- It is also inherently contradictory for a national treatment section to be given content to by national legislation. In a typical BIT, the national treatment clause is intended to influence national legislation in order that that legislation is not used discriminatorily (not the other way round)
- This national treatment section gives no such assurance. Currently drafted, in fact, gives the impression that foreign investors are *not* entitled to national treatment protection.
- The section is more appropriately subject to the constitution, than to legislation; which indeed it already is under s11 of the Bill.
- Additionally, there is already a “like circumstances” limitation within the section. This is intended (presumably) to cover the situations for which “subject to national legislation” was inserted.

- Specific comments
- *… For these reasons, we propose the removal of the phrase "subject to national legislation"*.
- For its part, the wording of the "like circumstances" qualification still leaves the scope and content of the national treatment protection unclear. Like circumstances is a built in limitation to national treatment clauses; even in BITs. But if it is overly-broad, such as is the case with this one, then there is no substantive national treatment protection offered by the section.
- *We request the use of clearer, and less open-ended or vague language*.
- Given that this Bill does not contain any complementary absolute standards of treatment (such as a form of "fair and equitable treatment" section), recourse for EU investors who perceive that they have been treated unfairly may well be limited. Several other foreign investors (from countries whose BITS remain active) have, as a result, avenues of protection, and substantive rights, additional to what the Bill is said to provide.

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- Specific comments
- **Section 8: Security of Investment**
- In general, the section is overly broadly worded, and does not make clear the nature of protections investors will be entitled to. Earlier versions of the Bill contained more detail. The wording "subject to available resources and capacity" indicates a caveat that may have far-ranging administrative and financial ramifications.
- *We suggest omitting this constraint, as it detracts from the intended purpose of the Bill; that is, to provide assurance and clarity*.
- We note, further, a specific change in the wording in this version. The original section in the first draft Bill read; "The Republic must accord foreign investors and their investments *and returns*, *equal* level of security as may be generally provided to other investors and subject to available resources and capacity." In the present version, the terms "and returns" and "equal" have been deleted. It would appear that this dilutes the content of this protection for foreign investors.
- *We propose that the two deleted words be reinserted into the Bill*.

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- Specific comments
- **Section 9: Protection of Property**
- Section 9 of the Bill refers to the constitutional right to property - without elaboration. It is trite that issues regarding principles relating to *expropriation* are inherent to this section. What is worrisome is that there is no current (up-to-date) legal framework for expropriation. The law of general application envisaged in the Constitution is presently in the form of two bills not yet assented into law - the Valuation Bill and the Expropriation Bill – which are still the subject of public consultations in the national assembly.
- Without reference to the actual final acts that will govern expropriation it is not possible to know how the detail of the procedural and substantive elements of expropriation will be handled.
- **Other specific concerns include:**
- the standard value of compensation in many of the BITs to which EU member states were party with South Africa was “full market value”;
- there are divergent views (even among academics and property rights practitioners) on the content of constitutional jurisprudence on the matter of compensation; and the Expropriation Bill is still the subject of intense debate, and there remain a number of issues of contention surrounding that Bill.

- Specific comments
- **Section 11: Sovereign Right to regulate**
- We note that it is a stated purpose of the Bill to promote and protect investment and ensure a *balance* of rights and obligations. The nature of this balance, and thus the inherent value of protections contained in the entire Bill can only be assessed against how precisely the public policy exceptions contained in the Bill are defined. We note that, depending on how expansive the exceptions are drafted and how expansively they may eventually be interpreted, the value of any protections in this Bill could be obviated.
- *There is a need for the inclusion of more precise language*.
- The revised version of the Bill has made the exceptions even more expansive and open-ended, which has only served to magnify the Chamber's initial concerns:
- "notwithstanding anything to the contrary in this Act";
- "and applicable legislation";
- "which may include".
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- *We propose that these additional open-ended limitations be removed, and that the wording reverts to that used in the original version of the Bill*.

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- Specific comments
- **Sections 12 and 13: Dispute Resolution and Regulations**
- It is not clear why the qualification "subject to applicable legislation" has been added here. In our view, what this section was intended to relay is that investors "*are not precluded*" by anything in the Bill from pursuing litigation in the courts or from referring a matter for review (or similar).
- *We, accordingly propose the replacement of the current wording with wording from the original version of the Bill:*
- *"Subsection (1) does not preclude an investor from approaching any court, competent, independent tribunal or statutory body for the resolution of a dispute relating to an investment"*.
- <u>Mediation; sections 12(2) and 12(2))</u>
- In the current version of the Bill, dispute settlement options such as mediation and arbitration, are supported in so far as they are suited to commercial exigencies. The EU Chamber, however, infers from the wording of s12(1) that the Bill is non-committal on the issue of mediation. Under the current wording of ss12(1) and 12(2); the Department can decline to accede to the request for mediation by an investor; and the Minister can also elect to not define criteria for the appointment of mediators. …

- Specific comments
- **Sections 12 and 13 Contd: Dispute Resolution and Regulations**

- *We propose the return of the wording in the original Bill, which read as follows:*
- *"The Minister must make regulations on the processes and procedures relating to the settlement of disputes …"*

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- Specific comments Contd
- Arbitration (State-State Arbitration s12(5))
- There is a gap in the law governing international and domestic arbitration in South Africa, so it will not be possible to comment fully. However, with the presently available information, the EU Chamber makes the observation that:
- it is not guaranteed that the home state government will agree to embark on the arbitration;
- the use of the word “may” in s12(5) suggests that the process, from the side of the South African government, is voluntary to begin with;
- Presumably, issues around: how consent to arbitration occurs; which arbitration centre will be designated; the procedures and rules that will be followed; and which arbitration rules will apply, will all be given effect-to in new arbitration legislation.

- Contd…

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- Specific comments
- In view of the introduction of this Bill and, in particular, some of the unanswered questions concerning articles 12 and 13, *we would urge the government to oversee re-engagement on the modernisation of the Arbitration Act*.
- It has been suggested by some commentators that, through the new Arbitration Bill(s), *government should consider consenting to investor-state international arbitration - with appropriate caveats "such as requiring the seat of arbitration to be in South Africa and the law governing the international arbitration to be South African law"*. This is in line with our own proposal for an appropriate ring-fencing.

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- Specific comments
- **Section 13 (read with ss12(1) to 12(3)): Regulations**
- Generally
- It appears that it is peremptory for the Minister to issue regulations under sections 12(3) and s13(2) while, under sections 12(2) and 13(1) it is not. We further note that this represents a *change* from the original Bill (from "must" to "may"), which had directed the Minister to issue regulations, under each of all these subsections.
- The EU Chamber would, nevertheless, like to make some comments in that regard:
- *the default should be that mediation should be available*, particularly because it is an effort at dispute avoidance; where a party is, for good cause, unwilling or unable to submit to mediation, *the regulations should be able to make provision for this*.
- Even if is mediation is not considered mandatory, *the defining the criteria for the appointment of a mediator of the rules and procedures governing mediation should not be optional*.
  - the rules and procedures must exist so that they govern it when it does take place. Furthermore, the general investor community would need to know the full gamut rules and procedures are in case they should need to take the route in the future.
  - the rules and procedures, and criteria for the appointment of the mediators would, in any case, be standard ones that would apply to every case.

- Specific comments
- **Section 14: Transitional Arrangements**
- The EU Chamber notes the inclusion of this section. The matters contained therein are already taken by the Chamber as implied. However, as at the present time, the contents of this section relate most perceptibly to EU investors, it would be apt to make a few specific remarks.
- It is acknowledged that existing investment retains the protection of the terminated BITs for a further 10 - 20 years. But we would like to reiterate that the issues raised in this submission concern old investment, as much as they do new investment. These developments have been viewed, by both categories of investor, as altering the investment environment. EU investment is, in general, long-term in nature. And investment planning extends beyond the lifespan of the BIT survival clauses. So without adequate certainty from any replacement regime - in this case, this Bill - investors could still consider recalibrating their investments.

- Specific comments
- **Section 14: Transitional Arrangements Contd.**

- The investment regime overhaul comes at a time when South Africa needs to record significantly larger numbers of inward FDI (than it is presently) whilst protecting existing investments - and to position itself as "open to business". However, as indicated in our previous written and oral submissions, investors are comparatively more guarded at the moment about South Africa as an investment destination.
- Because: 1) all the BITs that have been terminated were BITs with EU member states; 2) South Africa's BITs with a number of other parties remain active (with a number of them in force), or are being renegotiated.

- Conclusion
- The EU business community plays a key role in the creation of sustainable jobs, and economic growth and development in South Africa. We remain committed to a mutually advantageous long-term relationship with the South African government and the South African people. In playing a constructive role in the economy, we underscore the importance of a secure and predictable investment regime, which offers adequate protections to investors. It is our firm belief that a number of aspects would be better dealt with directly on constitutional level than by way of this Bill.
- The contributions made in this submission are provided in the light of our partnership, and we look forward to further engagement on the issues raised in this supplementary submission.

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- # Questions and Answers
- **QUESTION**
- Now, you made precise mentions to the phrases that you have challenged with regards to section 11, but you do not indicate the challenge as such, you indicate that the section is even more expansive and open ended. It would be helpful if you could indicate precisely what it is you are concerned with when you mention:
- "notwithstanding to the contrary"
- "and applicable legislation" all the legislation? Any one in particular? What is your specific concern
- "which may include"
- If you were able to give that to us?
- **ANSWER**
- It is a stated purpose of the Bill to balance between the government's right to regulate and the maintenance of an open and transparent environment for foreign investors. Our concern is that the section does not support such balance, and that the Bill could end up providing no protections to foreign investors. The challenge is specifically around the inclusion of the three qualifications (which were not contained in the first version of the Bill) into the current s11.
- These three qualifications make the exceptions in s11 even more expansive, vague, and open-ended, and consequently, represent further limitations to the protections contained in the Bill. Their addition adds to the general unease with regards to overall value of protection contained in the Bill as a whole.
- We would, accordingly, like to see the inclusion of more precise language in the section as a whole.
- We are further specifically proposing that the three phrases be removed, and that the wording reverts to that used in the original version of the Bill.

- **QUESTION**
- You say that the Bill does not (as currently drafted), adequately protect EU investors in South Africa. If passed as is, what would be the effect on EU investment? What would the impact be on EU investors' perceptions?
-
- **ANSWER**
- Based on a combination of anecdotal evidence, snap surveys conducted by bilateral chambers, and reports from individual companies, some investors (or prospective investors) are already:
- Recalibrating their investments;
- Adopting a "wait and see" approach before investing or reinvesting;
- Considering other destinations in neighbouring countries or the rest of the continent; or
- Considering other destinations further afield.

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- **QUESTION**
- What impact to credit ratings have on investors?
- **ANSWER**
- The Chamber has not specifically addressed this question with members or with bilateral chambers.
-
- **QUESTION**
- You say that the Bill does not offer enough / adequate treatment. Why?
- **ANSWER**
- Because it does not provide certainty and predictability to the investor community.
- There are a number of substantive, interpretative, and drafting aspects of the Bill that cause the EU business community to be uncertain of the protections available to their investments.
- The Bill also contains extensive limitations and exceptions.
- The Bill states that its purposes to adequate and equal protection to [all investors]". However, the review process has created quite a differentiated system of protection for different categories of investors. Among foreign investor, for example, many are still protected by BITs.
- Read as a whole, and viewed with due consideration of all of the Bill's stated purposes, it is our view that its current format does not find the balance it seeks to achieve.

- **QUESTION**
- Please clarity your input on National Treatment. What is the difference between domestic investment and foreign direct investment?
- **ANSWER**
- The national treatment section is a BIT-type section that has been included into this Bill. And according to s4, one of the purposes of the Bill is to "confirm the protection of an investment in respect of national treatment". However, for the reasons stated in our original submission, this national treatment section does not do this.
- Subjecting national treatment protection to national legislation (apart from being open-ended), is a digression from its typical formulation in BITs. In that formulation, national treatment protection is envisaged as a precaution against discriminatory national legislation. In the present Bill, content of national treatment protection is *subjected* to national legislation (current or future): effectively its content is unknown; and it does not operate as a precaution against legislation being used discriminatorily.
- The EU Chamber is fully aware that, there may be instances of legitimate differentiation by government between domestic and foreign investors, and note the comments in 2.4 of the explanatory memorandum to the Bill in this regard.
- We are of the view that the "like circumstances" limitation (if defined better), is a legally more suitable limitation to national treatment protection than "subject to national legislation. Otherwise there is no clear point to the section.
- Also, as it is suggested in the explanatory memorandum itself, the national treatment section should be subject to the Constitution; not, in our view, to *other legislation*.
- We also reiterate that it is, in any case, already subject to the Constitution through section 11 of the Bill.

- **QUESTION**
- Are you a regional or a national (South Africa focussed) chamber?
-
- **ANSWER**
- We are principally a South Africa focussed chamber of commerce.
- We are, however, cognisant that many EU companies operating in, or headquartered in South Africa also service operations in SADC.
- The region itself has become increasingly economically (trade and investment) integrated, so we were of the view that it would be important to introduce a regional aspect to our work.
- We are aware that there are no EU Chambers of Commerce in the other individual SADC members, and so in that sense we can be in a position to service any relevant needs gaps in those countries.

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- **QUESTION**
- Expand on what you understand to be inclusive growth in South Africa.
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- **ANSWER**
- Inclusive growth, as a preferred internationally concept still does not have a universally agreed definition. In our view, however, in the South African context (in the context of the NDP and SONA 2014/2015), the concept reflects growth, that; effectively tackles job creation, reduces poverty, reduces inequality, and contributes to transformation. It includes issues such as:
- Supply-chain development and supplier diversification;
- Skills transfer, and transfer of technology;
- Levelling the playing field, through enforcing rules to tackle substandard and illicit imports;
- The creation of black industrialists.
- European investors take a long-term perspective when it comes to FDI. Whilst they strive for reliability and predictability in terms of investment frameworks, they invest heavily in transformational change and societal programmes. This balanced economic and socially conscious approach works best on the basis of risk-aversion.

- **QUESTION**
- You have indicated in various places in your submission that the Bill requires different wording or redrafting. Please state where, in each case, with your proposals for alternative wording.
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- **ANSWER**
- Please refer to summarised submission, together with individual drafting proposals contained in this presentation (Promotion and Protection of Investment Bill: Template of EU Chamber Proposals to Parliament).

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- **QUESTION**
- How do you want the Bill to treat minority shareholders?
- **ANSWER**
- We are of the view that the definition of “investment” does not sufficiently acknowledge the contribution of minority equity investments (i.e. portfolio or venture capital investments for example, who may or may not have established a corporation in South Africa) to growth sectors, such as renewable energy projects, and SMME’s in general. This is evident from 2.2 of the explanatory memorandum.
- We would like to get clarity on the status of protections of the above kinds of investment. They are often significant, contribute to job creation and economic growth, and involve a level of risk-taking on the part of investors. If they are not to be protected in this Bill, where are they to be protected? Further to that point, does the sole fact of being incorporated in South Africa constitute “a physical presence” as mentioned in the memorandum?
- We would like to see substance over form here. Where large-scale financial investors provide relevant capital transfers into enterprises with a physical presence in South Africa, and which produce economic activity and create jobs in South Africa, then it is our view that they should not be overtly excluded from this Bill, as it is the case right now.
- We believe that our proposed rewording, in this presentation, still leaves the government at ease since hedge funds would not typically meet the "reasonable period of time” criteria.

- **QUESTION**
- Has the chamber consulted its own bilateral chambers?
-
- **ANSWER**
- The EU Chamber has discussed the Bill with a number of stakeholders including, but not limited to:
- European multinationals invested in South Africa for a considerable period of time by way of significant investments in manufacturing operations and regional headquarter operations;
- New European market entrants who are currently considering capital investments in manufacturing, distribution and research facilities in South Africa; and
- EU Bilateral Chambers of Commerce in South Africa (who themselves have, over the course of the last two years, continuously consulted with their members and with prospective investors on matters surrounding the Bill).

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