

Labour and Employment Issues
in Foreign Direct Investment:
Public Support Conditionalities

by

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List of acronyms and abbreviations

| | |
|---------|--|
| ADB | Asian Development Bank |
| ASEAN | Association of Southeast Asian Nations |
| BIMSTEC | Bangladesh, India, Myanmar, Sri Lanka, Thailand Economic Co-operation Agreement |
| BITs | Bilateral Investment Treaties |
| CDC | Commonwealth Development Corporation |
| CEMAC | Communauté Économique et Monétaire de l'Afrique Centrale |
| CESRU | Environmental and social impacts analysis unit |
| COMESA | Common Market for Eastern and Southern Africa |
| DBSA | Development Bank of South Africa |
| DFIs | Development finance institutions |
| EAC | East African Community |
| ECA | Export Credit Agency |
| ECGD | Export Credit Guarantee Department (British ECA) |
| EDC | Export Development Corporation (Canada) |
| EFIC | Export Finance and Insurance Corporation (Australia) |
| EKF | Eksport Kredit Fonden (Denmark) |
| EU | European Union |
| FDI | Foreign direct investment |
| FMO | Netherlands Development Finance Company |
| FTAA | Free Trade Area of the Americas |
| FTAs | Free trade agreements |
| ICSID | International Centre for the Settlement of Investment Disputes of the World Bank |
| IDB | Inter-American Development Bank |
| IFC | International Finance Corporation |
| IFTRIC | Israel Foreign Trade Risks Insurance Company |
| IFV | Danish International Investment Funds |

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|----------------|---|
| IAs | International Investment Agreements |
| IIC | Inter-American Investment Corporation |
| ILO | International Labour Organization/Office |
| IOR-ARC | Indian Ocean Rim - Association for Regional Cooperation |
| IPAP | Asia-Europe Investment Promotion Action Plan |
| KfW/DEG Invest | German development finance institutions |
| MIF | Multilateral Investment Fund |
| MIGA | Multilateral Investment Guarantee Agency |
| NAALC | North American Agreement on Labour Co-operation |
| NAFTA | North America Free Trade Agreement |
| NEXI | Nippon Export and Investment Insurance Company |
| NGO | Non-governmental organization |
| Norfund | Norwegian development finance institution |
| OECD | Organization for Economic Cooperation and Development |
| OPIC | Overseas Private Investment Corporation |
| SADC | Southern Africa Development Community |
| UEMOA | Union Economique et Monétaire Ouest Africaine |
| UK | United Kingdom |
| UN | United Nations |
| UNCTAD | United Nations Conference on Trade and Development |
| US | United States |
| WTO | World Trade Organization |

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Executive Summary

This paper explores the issue of public support for foreign direct investment (FDI) and its conditionality with respect to labour and employment issues. Three areas are examined, with the following general results:

International investment agreements: as these are agreements between States, they do not create direct obligations for investors. Some bilateral agreements suggest respect for internationally recognized human rights, but these are not binding obligations. Free trade agreements that include investment chapters may include a “no lowering of standards” provision, especially in the Americas, to avoid a “race to the bottom” to attract FDI. Others include a side deal on labour or environment matters, but remedies are applied mainly to trade-related disputes. Otherwise, these agreements leave investor behaviour to the regulation of host states.

Overseas investment insurance: public export credit agencies widely provide insurance for domestic investors going abroad to cover political risks. As this is a domestic transaction between the ECA and the investor, home state social standards can and often do apply to these contracts. Many states apply an OECD-sponsored environmental screening process to this. A few states review projects for labour and employment conditionalities. Only the U.S., the U.K. and MIGA (the World Bank) attach any core labour rights to their overseas investment insurance, though they approach this in different ways.

Development Finance: public support for foreign investment is at its strongest with the direct provision of finance. As this is also a domestic transaction, public actors are freer to attach social conditionalities. Many states follow the World Bank’s lead on environmental and social reviews, but the social review here consists of three policies that do not address labour issues directly. Those policies areas are on indigenous peoples, involuntary resettlement and cultural property. Ten development finance institutions do include labour conditionalities in their eligibility criteria. These are discussed to describe their different methods and standards. A note on FDI procurement is also included, which suggests that these conditionalities apply *only* to direct applications for finance and *not* to their procurement practices.

Introduction

Along with international trade, foreign direct investment (FDI) is a key driver of economic globalization. Governments are beginning to link international trade with the social responsibilities of business, mostly with labour and environmental standards.¹ The central question this paper explores is whether foreign investment support has similarly been connected to social conditions. FDI is highly sought after by developing and developed countries alike, and has been growing by double digits annually since the mid-1980s, reaching a record high of \$1.3 trillion in 2000.² While the flow of investment from North to South is estimated by UNCTAD to be a small fraction of global FDI, its impact in many developing countries is considerable. Therefore, it is important to consider how public actors, especially in *home* countries, link FDI to *international* social standards. This paper describes instances where the public sector links foreign investors' rights, insurance and financing to obligations to respect labour conditionalities. Environmental obligations in these areas will also be reviewed, as they are possible models for labour conditionalities.

There are at least three specific areas of public support for FDI:

1. Bilateral and multilateral investment agreements;
2. Government Export Credit Agencies offering overseas investment insurance;
3. Regional and National Development Finance Institutions offering private sector financing (as distinct from procurement policies).

These three groups of institutions provide a series of services to foreign direct investors.³ The first are framework legal rights. International investment agreements provide guarantees from states to investors against political risks (such as discrimination or expropriation) and currency transfer risks. Bilateral agreements often support these rights with a remedy for investors against host states. The goal of these agreements is for States to guarantee an atmosphere conducive to safe private investment. Investment agreements aim to guarantee certain property rights in foreign nations, not to condition those rights against obligations beyond obeying the law.

Governments often offer insurance for overseas investment through their export credit agencies. This transaction is a second publicly supported service to investors after core

¹ See for example, The U.S. *Trade Act 2002*, which obliges any new American free trade agreements to protect fundamental workers rights and the environment; the United States' 2003 Trade Policy Agenda at www.ustr.gov/reports/2003.html; the North American Agreement on Labour Co-operation (a NAFTA side agreement on the upward harmonization of labour standards) at www.naalc.org; European Commission commitment to conducting social impact assessments of all major new trade agreements (see europa.eu.int/comm/trade/sia/background.htm).

² UNCTAD *World Investment Report 2001*, Overview at 1. (available at www.unctad.org). The Report notes though that a slowing world economy showed a 40 per cent decline in FDI flows in 2001, to \$760 billion.

³ The paper is intended to look only at the formal rules in these areas. There is no comment made on the actual experience of FDI, in terms of the real effects on social standards (labour or the environment). Some studies have found a positive (if weak) relationship here, but the literature is mixed and often anecdotal. For a broad study of actual impacts in this area, see OECD, *Foreign Direct Investment for Development, Maximising Benefits, Minimising Costs* (2002), available from www.oecd.org/bookshop.

legal rights are in place. Overseas investment insurance often covers the same risks as the investment agreements, although some export credit agencies go further by insuring commercial risks. If an investment is both insured and protected by an investment agreement, there are two remedies in case these risks materialize. The investor may file a claim on the insurance, which involves minimal additional cost but will compensate only limited damages. Alternatively, the investor may pursue arbitration under the investment agreement, which will mean high costs but may end in a much larger settlement. (Investors may not pursue both avenues on the facts of one incident).

Neither an investment agreement nor overseas investment insurance will provide any money unless the investment goes disastrously wrong. The third service deals with how public money is provided to companies to finance investments ahead of time. In instances where private investments have some public policy benefit, there are agencies that provide funds for investment and assist in securing further private financing, sometimes attaching social conditionalities to their service.

All three of these regimes are examined to see if the public agency providing framework legal rights, investment insurance or financing ever requires social responsibility obligations, mandatory or voluntary. The institutions and agencies discussed in this paper were not contacted directly. The majority of them maintain extensive websites, including policies, procedures and annual reports. For the most part, except where otherwise noted, the information referred to herein is publicly available online. The three regimes are examined primarily for support of the four core principles identified in the ILO's 1998 *Declaration on Fundamental Principles and Rights at Work*: freedom of association and the right to collective bargaining; elimination of forced labour, abolition of child labour and the elimination of discrimination employment. Other work-related and environmental conditionalities are discussed, but these four principles are the core of the research.

PART I: International Investment Agreements (IIAs) – Framework Rights and Social Obligations

International investment agreements do not address social matters such as labour or environmental issues often. They aim only to produce a liberal atmosphere conducive to flows of investment. This narrow mandate leaves social issues aside. As will be seen below, social clauses are mostly only declaratory, not legally binding. Side deals to free trade agreements that deal with social issues provide remedies mainly for trade-related disputes, not for substandard *investor* behaviour. The most important social clause in international investment agreements appears in a series of bilateral free trade agreements that Mexico signed in the 1990s where the investment chapters are qualified by an agreement between states not to lower their standards in core social areas. A future *Free Trade Area of the Americas* may reproduce this model. The following section examines bilateral and multilateral investment treaties, investment promotion agreements, and investment provisions in trade agreements to identify social conditionalities.

Bilateral Investment Treaties – declaratory language

The Bilateral Investment Treaties (“BITs”) that the World Bank has compiled do not include social obligations for investors.⁴ BITs are states agreeing to a reciprocal standard of treatment of “aliens.” States, as parties to the agreements, place these obligations only on each other. Investors accrue rights (as aliens) but the agreements do not burden them with any obligations. The general range of State obligations in BITs is well described in the literature, so it will not be repeated here.⁵

The United States, Canada and Australia are the only nations that address labour and employment issues in their bilateral investment treaties. All three include a provision to permit top managerial staff to enter into the territory of the other Party for investment-related purposes. The wording the United States uses is generally this:

1. (a) Subject to its laws relating to the entry and sojourn of aliens, each Party shall permit to enter and to remain in its territory nationals of the other Party for the purpose of establishing, developing, administering or advising on the operation of an investment to which they or a company of the other Party that employs them, have committed or are in the process of committing a substantial amount of capital or other resources.

(b) Neither Party shall, in granting entry under paragraph 1(a), require a labor certification test or other procedures of similar effect, or apply any numerical restriction.

2. Each Party shall permit covered investment under this treaty to engage top managerial personnel of their choice, regardless of nationality.⁶

Between 1991 and 2001, some form of this clause (easing regulations on entry and work permits for key personnel) shows up in thirteen Australian BITs,⁷ in fourteen Canadian BITs⁸ and in twenty-nine American BITs.⁹

⁴ All of the Bilateral Investment Treaties reviewed here are compiled by ICSID (The International Centre for the Settlement of Investment Disputes, of the World Bank) in Investment Promotion and Protection Treaties. (New York: Oceana, 1983 - continually updated). Germany and Pakistan signed the first BIT in 1959; they are still signed today. The ICSID compilation is not entirely comprehensive, and updates are ongoing, but it is the most extensive collective available. The only BITs currently available online are ones agreed in the Western hemisphere, compiled by the Organisation of American States. See www.sice.org.

⁵ ICSID has posted an extensive bibliography on the subject at www.worldbank.org/icsid/pubs/treatbibl/main.htm.

⁶ Mozambique / United States, 1998, Article VII. (Author’s emphasis.)

⁷ *Ibid.*, with Egypt, 2001; India, 1999; Lithuania, 1998; Argentina, 1995; Peru, 1995; Philippines, 1995; Laos, 1994; Czech Republic, 1993; Indonesia, 1992; Czechoslovakia, 1991; Hungary, 1991; Poland, 1991; and Vietnam, 1991. Note that the only two BITs Australia signed in this period that did not include this provision were with Hong Kong, 1993 and Romania, 1993.

⁸ *Ibid.*, with El Salvador, 1999; Costa Rica, 1998; Lebanon, 1997; Uruguay, 1997; Barbados, 1996; Ecuador, 1996; Egypt, 1996; Panama, 1996; Romania, 1996; Venezuela, 1996; Latvia, 1995; South Africa, 1995; Trinidad and Tobago, 1995 and Ukraine, 1994. Note that the only two BITs Canada signed in this period that did not include this provision were with Argentina, 1991 and Hungary, 1991.

Only the United States inserts any wording relating to labour provisions for rank-and-file employees in their BITs. All this language is located in the non-binding preamble portions and is not subject to any remedy. Beginning in the early 1990s, the United States inserted first one preamble clause, and later in 1994 a second one, along these lines:

Recognizing that the development of economic and business ties can promote respect for internationally recognized worker rights;

Agreeing that these objectives can be achieved without relaxing health, safety and environmental measures of general application;¹⁰

The earlier preamble stated:

Recognizing that the development of economic and business ties can contribute to the well-being of workers in both Parties and promote respect for internationally recognized worker rights.¹¹

The bodies of the United States' BITs do not address either internationally recognized labour rights or general health and safety laws as raised in these preambles. The only employment issue treated in the legally binding text is the easing of immigration and work permit legislation for the top managerial personnel of investors. Core labour rights matters are left to host state regulation alone. (Even the obligation on investors to follow local law – perhaps a self-evident one – goes unstated in these BITs).

Regional Investment Treaties and Multilateral Investment Promotion

Most multilateral investment agreements do not contain any provisions on social conditionality, or create any obligations for investors in the host country for social matters. This is true, for example, of the Framework Agreement on ASEAN Investment Area;¹² the Bangladesh, India, Myanmar, Sri Lanka, Thailand Economic Co-operation Agreement (BIMSTEC);¹³ and the Indian Ocean Rim - Association for Regional Cooperation (IOR-ARC).¹⁴

⁹ *Ibid.*, with Bahrain, 1999; El Salvador, 1999; Mozambique, 1998; Bolivia, 1998; Azerbaijan, 1997; Jordan, 1997; Croatian, 1996; Honduras, 1995; Latvia, 1995; Nicaragua, 1995; Albania, 1995; Georgia, 1994; Uzbekistan, 1994; Estonia, 1994; Jamaica, 1994; Mongolia, 1994; Ukraine, 1994; Moldova, 1993; Kyrgyz Rep., 1993; Armenia, 1992; Kazakhstan, 1992; Romania, 1992; Bulgaria, 1992; Russia, 1992 (subject to a significantly different preamble); Argentina, 1991; Sri Lanka, 1991; Czechoslovakia, 1991; Poland, 1990 and Congo, 1990. While the preamble the United States used in its BITs evolved over the 1990s, they consistently used the same key personnel provision.

¹⁰ *Ibid.*, Mozambique / United States, 1998, preamble.

¹¹ *Ibid.*, Moldova / United States, 1993, preamble.

¹² Signed 7 October 1998, with members Brunei Darussalam, Cambodia, Indonesia, Laos, Malaysia, Myanmar, Philippines, Singapore, Thailand and Vietnam, at www.aseansec.org/7664.htm.

¹³ See <http://230.150.20.1/bimstec/index.html>.

¹⁴ See www.iornet.org/newiornet/index.htm.

In the current round of WTO negotiations, there are talks about creating a multilateral agreement to promote and protect foreign direct investment, similar to current BITs, picking up where the Multilateral Agreement on Investment failed in 1998. The EU is a leading proponent of the idea. One of their key points is that

[e]ach government should ... preserve the right to regulate the economic activity within its territory, including in the fields of development, environment and social conditions.¹⁵

This position is interesting for separating international rules on investment from social conditionalities. Europe is committed to leaving such regulation to host states, rather than creating or “imposing” international standards in these areas.

In Africa, there are two investment agreements that do suggest social goals and conditionalities, at least in a declaratory sense. The Southern Africa Development Community (SADC), a trade and investment area, lists these objectives in its founding treaty:

a) achieve development and economic growth, alleviate poverty, enhance the standard and quality of life of the people of Southern Africa and support the socially disadvantaged through regional integration;

...f) promote and maximise productive employment and utilisation of resources of the Region;¹⁶

In addition, the West African Monetary Union¹⁷ was studying a proposal in 2001 for a “*Code Communautaire des Investissements*” which would regulate investor’s social obligations. However, the proposal comes from the Commission and the member states are reluctant to move it forward.¹⁸

There are other agreements between nations that deal with promoting investment (rather than with States making formal commitments on the treatment of foreign investment). Two examples are the Asia-Europe Investment Promotion Action Plan (IPAP) and the Stability Pact for South East Europe. IPAP does not link investment and employment directly, nor does it address other social matters.¹⁹ Like most investment promotion agreements, it deals with non-discrimination and liberalisation rather than any direct social content. However, the Stability Pact, a framework agreement for international co-operation on “reform, investment, integrity and growth” underlines its commitments with this final paragraph:

¹⁵ European Union, DG Trade, at europa.eu.int/comm/trade/issues/sectoral/investment/conswoag_inv.htm. (Author’s emphasis).

¹⁶ Treaty of SADC, 17 August 1992, with members Angola, Botswana, Lesotho, Malawi, Mozambique, Namibia, Swaziland, Tanzania, Zambia, Zimbabwe at Article V.1.a and V.1.f, available online at www.sadc.int.

¹⁷ “Union Économique et Monétaire Ouest Africaine” (UEMOA) with members Benin, Burkina Faso, Ivory Coast, Guinea Bissau, Mali, Niger, Senegal and Togo – see www.uemoa.int.

¹⁸ See “Le rapport d’activités de l’année 2002 de la Commission l’UEMOA.” Available on-line at www.uemoa.int/Publication/2003/RapportCom2002.pdf.

¹⁹ See http://europa.eu.int/comm/external_relations/asem_ipap_vie/ipap_text/ipap_text.htm.

Participants will pursue these objectives and commitments in a manner consistent with their commitments to sustainable development, protection of the environment and the observance of internationally recognized core labour standards.²⁰

It is not clear whether this is legally binding; it appears to be only declaratory.

Table 1: Labour Conditionalities in International Investment Agreements

| Type | International Investment Agreement | Labour Rights Clause? |
|---------------------------------|--|--|
| Bilateral investment guarantees | U.S. BITs Canada/Australia BITs Other BITs | No <i>Exception:</i> preambles in the U.S. Bilateral Investment Treaties |
| Regional investment guarantees | ASEAN BIMSTEC IOR-ARC SADC UEMOA | No <i>Exception:</i> goals of job creation in SADC; pending code of conduct in UEMOA |
| Investment Promotion | IPAP South Eastern Europe Stability Pact | No <i>Exception:</i> a declaration of commitment to workers rights in the Stability Pact |

Investment Provisions in Trade Agreements

There are a number of regional free trade agreements (“FTAs”), particularly in the Americas, which include a chapter on investment that detail the rights of a Party’s investors when hosted by any other Party to the agreement. These chapters often do not contain any social conditionalities.²¹ Where they do exist, they are mostly in one of two formats.

²⁰ The text of the agreement as between 29 members is available online at www.stabilitypact.org.

²¹ See Cameroon, Gabon, Chad, Equatorial Guinea, Centrafrique, Congo Brazzaville Economic Association (CEMAC); The Common Market for Eastern and Southern Africa (COMESA); the Cartagena Area (see *Decision 291 of the Commission of the Cartagena Agreement. Common Code for the Treatment of Foreign Capital, Trademarks, Patents, Licenses, and Royalties, March 21, 1991*); and the East African Community (EAC). While no labour obligations are placed on the parties or investors in the EAC, the members do agree to the following in Article 80 (1) of the founding treaty: “For purposes of Article 79 of this Treaty [industrial development], the Partner States shall take measures to: (f) harmonise and rationalise investment incentives including those relating to taxation of industries particularly those that use local materials *and labour* with a view to promoting the Community as a single investment area.”

Mexican Model: The first, commonly used by Mexico, is a “no lowering of standards” clause.²² It consists of an agreement between the Parties that it is inappropriate to attract investment by eroding health, safety or environmental standards. Signatories are then free to enact any legislation on these matters without infringing the FTA. Such a model aims to prevent a “race to the bottom” rather than provide a remedy to those who feel it is already underway. The only remedy provided is State-to-State diplomacy. That is, a Party may “request consultations” if they feel another has lowered these standards to attract investors.

Canadian Model: The second format, used several times by Canada, involves creating a side deal to a free trade agreement where both the trade and investment provisions are linked to co-operation on social issues. In the NAFTA example, the side deal on labour covers eleven principles where parties retain sovereignty but they agree to promote the upward harmonization of standards. (These principles do not refer to ILO Conventions or other international standards). In addition to the upward harmonization, the side deal format often includes a set of remedies for individuals, corporations and unions should they believe that an investor or an exporter is infringing one of the eleven principles.

In the NAFTA case, there are three levels of remedy set out in the side agreement (the North American Agreement on Labour Co-operation). Only the first is available for allegations about *investors*. All three are available for *trade-related disputes*:

1. **National Administrative Officer Complaints:** a unit in each Party’s labour ministry can review “public communications” against an entity in another Party’s territory. (See Article 16(3)). This is a purely domestic procedure, and while the results of the review are public, there is no State-to-State comment or responsibility when it is released, and no further recourse for infringed labour standards connected to foreign investment.
2. **Expert Committee Evaluation:** for trade-related disputes, if the Complaints review does not satisfy the aggrieved party, they can request a panel of disinterested international experts to review the situation and issue a report (See Article 23). This puts pressure on the “guilty” Party to correct the matter.
3. **Arbitration Panels:** the final remedy, following an ECE, is binding arbitration (See *Part 5: Resolution of Disputes*). Again, this is only available for trade-related disputes.²³

²² This format shows up in at least six Free Trade Agreements: *Free Trade Agreement between Bolivia and Mexico* (Sept 10, 1994, www.sice.oas.org/Trade/mexbo_s/mbind.asp) in Article 15-14; *Free Trade Agreement between Costa Rica and Mexico* (April 5, 1994, www.sice.oas.org/Trade/mexcr_s/mcrind.asp) in Article 13-15; *Free Trade Agreement between Mexico and Nicaragua* (December 18, 1997, www.sice.oas.org/Trade/menifta/indice.asp) in Article 16-14; *Free Trade Agreement between Chile and Mexico* (April 17, 1998, www.sice.oas.org/Trade/chmefta/indice.asp) in Article 9-15; *Free Trade Agreement of the Group of Three among Mexico, Colombia and Venezuela* (June 13, 1994, www.sice.oas.org/Trade/G3_E/G3E_TOC.asp) in Article 17-13; and *Free Trade Agreement etween entral American Countries and the Dominican Republic* (April 18, 1998, www.sice.oas.org/Trade/camdrep/indice.asp).

²³ The *North American Agreement on Labour Co-operation* is available online at www.naalc.org.

The Canada-Costa Rica FTA and the Canada-Chile FTA both use a very similar side agreement model for labour co-operation.²⁴

Negotiations are in progress on a draft *Free Trade Area of the Americas (FTAA)*.²⁵ This will be a trade and investment area covering the Western Hemisphere. The draft preamble contains some interesting language that aims to:

- ✓ protect “fundamental human rights and the security of persons”;
- ✓ promote “social development, within a framework of equity”;
- ✓ observe and promote “worker rights, consistent with their commitment to internationally recognized core labour standards, to acknowledge the ILO is the competent body to set and deal with those core labour standards”;
- ✓ improve “working conditions [in the Americas]”; and
- ✓ ensure all this is done in “a manner consistent with international human rights norms and principles.”

The ILO reference in the draft preamble is interesting, as the United States tends to reference these rights generically rather than against specific international standards. This is their practice with bilateral investment treaties as well as their approach to overseas investment insurance and the provision of development finance (outlined below).

The *FTAA* currently contains a draft chapter on investment. Article 8 deals with provisions on how to treat key personnel of foreign investors (regarding immigration and work permits) which looks similar to the clause noted with the BITs above. Article 18 creates a “Commitment not to relax domestic labour laws to attract investment” (see box 2). This is very similar to the Mexican model in the free trade agreements noted above, with the clear distinction that a dispute in this area does not explicitly open diplomatic channels.

Box 1

Draft FTAA Article 18

[1. The Parties recognize that it is inappropriate to encourage investment by relaxing domestic labour laws. Accordingly, each Party shall strive to ensure that it does not waive or otherwise derogate from, or offer to waive or otherwise derogate from, such laws as encouragement for the establishment, acquisition, expansion or retention of an investment of an investor in its territory.]

[2. For smaller economies, a commitment not to relax domestic labour laws should be allied with compensating access to the Regional Integration Fund for the training of workers to make them more productive and the associated enterprises more competitive.]

²⁴ The *Canada-Costa Rica Agreement on Labour Co-operation* (entry into force January 1, 2002) is available online at www.sice.oas.org/trade/cancr/english/labore.asp; the *Canada-Chile Agreement on Labour Co-operation* (entry into force June 2, 1997) is available online at www.sice.oas.org/trade/chican%5Fe/labor1e.asp.

²⁵ The second draft of the text (dated November 1, 2002) is available at www.ftaa-alca.org. There has been a ministerial declaration that a final agreement should enter into force no later than December 31, 2005.

In summary, international investment agreements do not currently involve any social conditionalities for investors. The regime does not trade favourable treatment from states for positive investor behaviour; it only sets up a relationship between states for the reciprocal good treatment of foreign investors. The obligations rest entirely on States, though the rights and remedies accrue to the investors. The most progressive standard that can emerge from this framework is the inter-state agreement not to lower social standards to attract investment. Otherwise, language in agreement preambles about workers rights has no impact or remedy. The structure of these agreements is such that they cannot create legal obligations for the conduct of investors.

Table 2: Labour Conditionalities and Investment in Free Trade Agreements

| Type | International Investment Agreement | Labour Rights Clause? |
|---------------------------------|--|---|
| Trade and Investment Agreements | <ul style="list-style-type: none"> ✓ CEMAC ✓ COMESA ✓ EAC ✓ Cartagena Area | No |
| Mexican Model | <ul style="list-style-type: none"> ✓ Bolivia-Mexico ✓ Costa Rica-Mexico ✓ Nicaragua-Mexico ✓ Chile-Mexico ✓ Group of Three ✓ Central American Countries-Dominican Republic ✓ Draft FTAA | Yes No lowering of standards clause attached to investment provisions – (Diplomatic channels opened in case of dispute) |
| Canadian Model | <ul style="list-style-type: none"> ✓ NAFTA ✓ Canada-Costa Rica ✓ Canada-Chile | Yes Side Deal on upward harmonization of labour standards – National complaints procedure in case of dispute |

See Footnotes 21 to 24 for details on these Free Trade Agreements.

PART II: Export Credit Agencies – Overseas Investment Insurance

The main task of public export credit agencies is to facilitate international trade by extending financing and credit instruments to firms that export goods. Most of these agencies also facilitate foreign direct investment by providing investors with overseas investment *insurance*.²⁶ Table 3 shows how much this insurance is used. It displays the total coverage provided by Berne Union members (51 export credit agencies from 42 countries).²⁷

Table 3: Berne Union Members - Total Investment Insurance Commitments at Year End

| Year | US\$ Bn |
|------|---------|
| 1993 | 26 |
| 1994 | 32 |
| 1995 | 36 |
| 1996 | 43 |
| 1997 | 40 |
| 1998 | 43 |
| 1999 | 61 |
| 2000 | 57 |
| 2001 | 72 |

Export credit agencies vary in the type of risk they will insure, with each country defining *political risks* differently and limiting their insurance of currency transfer and commercial risks. Table 4 gives a few examples of how they define political violence and expropriation. Importantly, the overseas investment insurance contract is a domestic transaction between the publicly funded ECA and the private investor. Therefore, this insurance can be conditioned on the investor abiding by the *home* state's labour or environmental standards. This is significantly different from the investment agreements that rely on *host* state regulation.

²⁶ KPMG conducted a study on the economic rationale of public export credit, and to a lesser degree investment insurance, for the British ECA (the Export Credit Guarantee Department). It attempts to assess whether the products amount to a subsidy, contrary to the WTO goal that these agencies work on a break-even basis. (This goal is assisted by an OECD Consensus arrangement on Export Credit (at www.oecd.org.) The study is available online at www.ecgd.gov.uk/kpmg.pdf.

²⁷ The table is adapted from the *Berne Union Yearbook*, 2003 at 190. Available online at www.berneunion.org.uk. While the figure for 2001 looks significant, total FDI for that year came to more than ten times that amount. See UNCTAD *World Investment Report 2001*, op. cit., note 2.

Table 4: Export Credit Agencies - Risk Definitions Examples

| ECA | Political Violence | Expropriation |
|-----------------------|---|--|
| MIGA – World Bank | Protects against loss from damage to, or the destruction or disappearance of, tangible assets caused by politically-motivated acts of war or civil disturbance in the host country, including revolution | Protects against loss of the insured investment as a result of acts by the host government that may reduce or eliminate ownership of, control over, or rights to the insured investment. |
| OPIC – United States | Loss of assets or income due to war, revolution, insurrection, or politically motivated civil strife, terrorism, or sabotage. | Loss of an investment due to expropriation, nationalization, or confiscation by the host government. |
| ECGD – United Kingdom | War in which the host government is a participant; Revolution; Insurrection involving Political Violence in the host country; The investor is insured not only against damage to the property of the overseas enterprise but also against the inability of the overseas enterprise to operate the project to which the investment relates because of war. | Indirect forms of expropriation (creeping expropriation) brought about by the host government with the intention of discriminating against the investor or the overseas enterprise. |
| NEXI – Japan | The said losses may be incurred when the relevant subsidiary or the joint venture is forced to discontinue its business due to war, revolution, or force majeure such as natural disaster, etc. | N/A |
| IFTRIC – Israel | Risks connected to war, civil war, political upheaval, riots or similar events in the buyer's country. | Risks connected to nationalization, expropriation or other discriminatory acts carried out by the authorities in the buyer's country, over which the buyer has no control. |

All language taken directly from websites.

Fifty-four export credit agencies were reviewed for social eligibility criteria. Only twenty-five agencies are publicly held and offer overseas investment insurance. Of these twenty-five agencies eligible for the analysis:

- Four agencies require labour or employment-related standards of their clients
 - Each of these also requires environmental standards
- Seven require environmental standards only in terms of social conditionality
- Fourteen indicate their eligibility criteria online, but they do not include social conditionalities.

Table 5 shows the breakdown of these social conditions.

Table 5: Export Credit Agencies and Social Conditionalities

| Export Credit Agency (Nation: website) | Labour | Environment | No social Criteria |
|---|--------|-------------|--------------------|
| Overseas Protection Investment Corporation (USA: www.opic.gov) | √ | √ | |
| Export Credit Guarantees Department (UK: www.ecgd.gov.uk) | √ | √ | |
| Multilateral Investment Guarantee Agency (World Bank: www.miga.org) | √ | √ | |
| Nippon Export and Investment Insurance (Japan: nexi.go.jp) | √ | √ | |
| Eksport Kredit Fonden (Denmark: www.ekf.dk) | | √ | |
| Finnvera Plc. (Finland: www.finnvera.fi) | | √ | |
| Export Finance and Insurance Corporation (Australia: www.efic.gov.au) | | √ | |
| Hungarian Export Credit Insurance Ltd. (Hungary: www.mehib.hu) | | √ | |
| Export Guarantee and Insurance Corporation (Czech Republic: www.egap.cz) | | √ | |
| Export Development Corporation (Canada: www.edc.ca). | | √ | |
| Investment Risk Guarantee (Switzerland: www.swiss-irg.com/e) | | √ | |
| Export Credit Bank of Turkey (Turkey: www.eximbank.gov.tr/eng/index.htm) | | | √ |
| SACE (Italy: www.isace.it/portale/home.asp?l=eng) | | | √ |
| ECICS (Singapore: www.ecics.com.sg) | | | √ |
| The Israel Foreign Trade Risks Insurance Corporation Ltd (Israel: www.iftric.co.il/english/english.HTM) | | | √ |
| Office National du Ducroire (Belgium: www.ducroire.be) | | | √ |
| Export Credit Insurance Corporation (Poland: www.kuke.com.pl) | | | √ |
| Slovene Export Corporation Inc. (Slovenia: www.sid.si) | | | √ |
| Garanti-Instituttet for Eksportkreditt (Norway: www.giek.no) | | | √ |
| Malaysia Export Credit Insurance Berhad (Malaysia: www.mecib.com) | | | √ |
| The Investment Bank of the Federation of Bosnia & Herzegovina (Bosnia: www.ibf-bih.com) | | | √ |
| Export Credit Insurance Organisation (Greece: www.oaep.gr) | | | √ |
| Export Credit Guarantee Corporation of India Limited (India: www.ecgindia.com) | | | √ |
| Exportkreditnämnden (Sweden: www.ekn.se) | | | √ |
| China Export & Credit Insurance Corporation (China: www.sinosure.com.cn). | | | √ |

The remainder of this section will describe the labour and employment policies of the four agencies that do use labour conditionalities. A short note is also included on the general format of the environmental standards to suggest possible models for labour conditionalities. (Table 6 describes why twenty-nine of the fifty-four export credit agencies originally examined were excluded from the analysis).

Table 6: Excluded Export Credit Agencies

| Export Credit Agency (Nation: Website) | Privately Held | Only Trade Support | Inadequate Online Information |
|---|----------------|--------------------|-------------------------------|
| AIG Global Trade & Political Risk (USA: www.aigglobal.aig.com) | √ | | |
| Zurich Emerging Markets Solutions (USA: www.zurichna.com/politicalrisk) | √ | | |
| OEKB (Austria: www.oekb.at) | √ | | |
| Compania Argentina de Seguros de Crédito a la Exportacion (Argentina: www.casc.com.ar) | √ | | |
| Sovereign Risk Insurance Ltd. (Bermuda: www.sovereignbermuda.com) | √ | | |
| Companhia de Seguro de Créditos, S.A. (Portugal: www.cosec.pt) | √ | | |
| Società Italiana Assicurazione Crediti S.p.A. (Italy: www.eulergroup.com) | √ | | |
| Gerling NCM (Netherlands/Germany merger: www.gerlingncm.com) | √ | | |
| Credit Guarantee Insurance Corporation of Africa Limited (South Africa: www.creditguarantee.co.za) | √ | | |
| COFACE (France: www.coface.com) | | √ | |
| National Export-Import Bank of Jamaica Limited (Jamaica: www.eximbankja.com) | | √ | |
| Croatian Bank for Reconstruction and Development (Croatia: www.hbor.hr) | | √ | |
| Hermes (Germany: www.hermes-kredit.com/indexeng.html) | | √ | |
| Export Risk Guarantee (Switzerland: www.swiss-erg.com/e) | | √ | |
| Taipei Export-Import Bank of China (Chinese Taipei: www.eximbank.com.tw/english/default.html) | | √ | |
| Hong Kong Export Credit Insurance Corporation (Hong Kong: www.hkeic.com) | | √ | |
| Korea Export Insurance Corporation (Korea: www.keic.or.kr) | | √ | |
| Sri Lanka Export Credit Insurance Corporation (Sri Lanka: www.tradenetsl.lk/slecic/index.html) | | √ | |
| Export Import Bank (United States: www.exim.gov) | | √ | |
| Compania Espanola de Seguros de Crédito y Caucion S.A. (Spain: www.creditoycaucion.com) | √ | √ | |
| EULER Trade Indemnity plc (UK: www.eulergroup.com) | √ | √ | |
| FCIA Management Company Inc. (USA: www.fcia.com) | √ | √ | |
| Seguradora Brasileira de Crédito à Exportação S/A (Brazil: www.sbce.com.br) | √ | √ | |
| PwC Deutsche Revision AG (Germany: www.pwc.de/investitions Garantien) | | | √ |
| Asuransi Ekspor Indonesia (Indonesia: www.asei.co.id) | | | √ |
| Banco Nacional de Comercio Exterior S.N.C. (Mexico: www.bancomext.gob.mx) | | | √ |
| Compania Espanola de Seguros de Credito a la Exportacion (Spain: www.cesce.es) | | | √ |
| Credit Insurance Zimbabwe Limited (Zimbabwe: Tel: (263 4) 738 944-7 / 706 101-4) | | | √ |
| Export Credit Insurance Service (Cyprus: Tel: (357 2) 86 71 00 x). | | | √ |

None of the excluded agencies in Table 6 had any labour or employment conditionalities attached to their export credit products or private overseas investment insurance. Two agencies, excluded for being privately held, linked their overseas investment insurance product to environmental standards.²⁸ (Note that some major western European economies rely on the private provision of overseas investment insurance – in particular, Germany, France and Italy. The public export credit agencies in these nations restrict themselves to trade-support only.)

Labour and Employment Conditionalities at Export Credit Agencies

The four export credit agencies that link overseas investment insurance with labour conditions are from the United States, the United Kingdom, the World Bank (MIGA) and Japan. The first three refer to internationally recognized core labour rights. The United States agency is the only one to attach the mandatory obligation to follow all core labour rights to its investment insurance products, and subjects this to ongoing monitoring. The United Kingdom has a more conciliatory approach, and requires clients to warrant against the ill treatment or exploitation of labour, but it does not directly address freedom of association or collective bargaining. The Multilateral Investment Guarantee Agency has a policy preventing it from supporting investments that rely on forced or child labour. The Japanese agency does not address labour rights directly, but it does evaluate broad social considerations that are likely to affect workers' lives.

i) *United States*

In the United States, the Overseas Protection Investment Corporation (OPIC) is in a league of its own in terms of social conditionality. With investment insurance topping US \$600 million and exposure to claims at \$5.3 billion in 2002 it is an important player.²⁹ OPIC provides insurance against currency inconvertibility, expropriation and political violence risks.³⁰ Eligibility criteria for this insurance include *contributing to development, enhancing the environment, supporting worker rights, and discouraging corrupt practices* as well as financial and technical soundness. OPIC's policy on supporting worker rights is as follows:

OPIC does not support projects that contribute to violations of internationally recognized human and worker rights. OPIC Insurance agreements require the investor to agree to respect these rights, including the rights of association, collective bargaining, and acceptable working conditions with respect to wages, hours of work, occupational health and safety, and minimum age requirements.³¹

The process for receiving insurance coverage involves two forms from the applicant – a project registration with OPIC and a detailed application form. (OPIC separates the

²⁸ Oesterreichische Kontrollbank Aktiengesellschaft Export Guarantee Department (Austria; www.oekb.at); Credit Guarantee Insurance Corporation of Africa Limited (South Africa; www.creditguarantee.co.za).

²⁹ See 2002 Annual Report at www.opic.gov.

³⁰ See www.opic.gov/Insurance.

³¹ See www.opic.gov/Insurance: Eligibility: Supporting Workers Rights. The Statute referred to is Title 22 (Foreign Relations and Intercourse), 22 U.S.C. §2191. (Emphasis in the original.)

forms this way apparently to ensure they are aware of the project first and can get the evaluation process underway before requiring the very detailed application.) All applicants must fill in Part five, where they indicate the number of new employees required for construction and an estimate for the fifth year of project operation. Applicants are also asked to

[d]escribe employee training, including which categories of employees will receive training and whether there will be any training outside the host country and to [d]escribe any ancillary employee and community benefits of the project.³²

All applicants also reply to part six, which deals with worker rights (see box 2). Three of the four core labour rights are addressed (there is no mention of discrimination), and there is mention of higher standards, with the phrase “acceptable conditions of work”.

Box 2

OPIC Insurance Application Form Part 6

OPIC is required by statute to ensure that the project will not contribute to violations of internationally recognized worker rights. These rights are defined to include:

- (a) freedom of association;
- (b) the right to organize and bargain collectively;
- (c) prohibition of forced or compulsory labor;
- (d) minimum age for employment; and
- (e) acceptable conditions of work with respect to minimum wages, hours of work and occupational health and safety.

All OPIC political risk insurance contracts include language to ensure that the project is operated in accordance with internationally recognized worker rights. Since host country labour laws and practices vary, this language may be supplemented on a case-by-case basis as necessary to ensure that the project does not contribute to worker rights violations in the host country.

29. Will the Investor have sufficient control over labour-management relations to ensure that the project does not contribute to violations of worker rights as defined above? pYes/No

If No, please explain.

30A. If investing in, lending to, or acquiring an existing enterprise, is the work force organized in a trade union? Yes/No

30B. If you answered Yes to 30A, is the trade union recognized by the management: Yes/No

If you answered Yes to 30A, is the trade union recognized by the host government: Yes/No

31. If investing in a new enterprise or existing enterprise with a non-unionized workforce, does the Investor anticipate that the work force will be unionized? Yes/No. Please explain.

Finally, Part 14 (Additional Information) states

OPIC must ensure that projects receiving its support do not have a major or unreasonable adverse effect on worker safety and may request information regarding training, equipment, and applicable health and safety standards at the project.

³² See www.opic.gov/Insurance: Applying for Insurance: Form 52 – Application for Political Risk Insurance. These questions are located in Part five, questions 27 and 28 (A) and (G).

The application instructions indicate that “[m]isrepresentations or failure to disclose relevant information may result in the cancellation of insurance”. Thus, the penalty appears to be disengagement, in contrast to the UK approach set out below.

There is no information online about how these answers affect decision-making when insurance officers evaluate applications, but the policy statement forbidding OPIC from supporting projects that infringe worker’s rights seems definitive.

ii) **United Kingdom**

The Export Credit Guarantee Department in the United Kingdom offers a number of trade and investment support products. Their overseas investment insurance protects against political risks (including expropriation and war), currency transfer risks and, remarkably, the commercial risk of breach of contract. The ECGD promotes the *OECD Guidelines for Multinational Enterprises* to its corporate clients.

The ECGD appears to have a much closer working relationship with its clients than OPIC does. The application and evaluation process is very transparent after a “Case Handling Note” dated April 2003.³³ According to that document, investors wishing to take out coverage typically go through the following steps:

- They approach the Department for a preliminary assessment of whether insurance is available for the type of work or host State, and an estimate of the premiums.
- With this non-binding information in hand, the investor is then invited to fill in an application.³⁴
- The application provides ECGD’s Business Principles Unit with the information necessary to categorize the project as low-, medium- or high-risk. The Business Principles Unit is responsible for reviewing social standards as follows:
 - Low-risk investments receive no further social evaluation;
 - Medium-risk investments require an impact analysis questionnaire from the investor warranting that major adverse impacts are avoided; and
 - High-risk investments require full-blown environmental and social impact assessments based on international standards.

The impact analysis questions in the application are mostly environmental. In fact, the only social impact question upfront requires the investor to describe the *beneficial* aspects of the investment:

Please ensure that all environmental, health and safety, and social impact benefits are clearly identified and quantified where possible. Benefits could include reduction in pollution, improved efficiency of energy usage, generation of electricity from renewable

³³ *Case Handling Note*, April 2003, available at 62.239.5.9/casehandlinginfoapril2003.doc.

³⁴ The application is available online at www.ecgd.gov.uk: All Products & Services: Application Forms: New OII Application.

resources, technology transfer, skills transfer and training, opportunities for local entrepreneurs such as micro-credit schemes and other associated community projects.³⁵

These questions get the client to describe the type of activity involved in the project. The Business Principles Unit analyses this description and puts the investment into one of these three categories. This suggests that the ECGD engages in ongoing relationships with clients applying for coverage. Already the applicants have met with an ECGD official for a preliminary review, and submitted an application. Unless it is a low-impact project, they will have ongoing contact while the Department assures itself that environmental and social risks are mitigated or minimized.

At the medium-risk level, this is done through an impact analysis questionnaire. Investors are asked to give details on a series of environmental and social issues related to their project. The two key labour questions asked at this stage are:

QUESTION 8

Will the goods or project cause, require, bring about or stimulate any of the following?

- Resettlement of the local population
- Compulsory acquisition of land
- Displacement of or damage to existing industry or agriculture
- Job losses among the local population
- Child labour
- Bonded or forced labour
- Large-scale influx of workers
- Damage to sites of cultural, historic or scientific interest
- Impact on minority or vulnerable communities
- Use of armed personnel
- Social benefits

QUESTION 9

Will the benefits of the goods/project (including employment opportunities for local people) be open to all, regardless of race, religion, gender, social grouping, etc.?³⁶

Thus, the ECGD assures itself under warranty from its clients that it will not support child labour, forced labour or discrimination. The detailed notes explaining these questions not only refer to ILO conventions but also to World Bank policies and other relevant

³⁵ *Ibid.*, at 9.

³⁶ Impact Questionnaire, Form IQ2, available online at www.ecgd.gov.uk. (Author's emphasis).

international standards.³⁷ The analysis notably does not address freedom of association or collective bargaining.

The approach taken with high-impact (greenfield) projects has three interesting characteristics. Firstly, the ECGD requires the client to bear the cost of full-blown environmental and social impact assessments. Secondly, it publishes project details on its website and receives public comments, which are then taken into consideration. Thirdly, the project may be dealt with under a ‘sensitive cases’ procedure that involves consultations with other government departments to ensure that ECGD support does not undermine other goals and priorities of the UK government.

Finally, the Department suggests that its coverage may be conditional on conducting the business in a certain manner, especially avoiding risks identified in the impact analysis process, and it reserves the right to monitor implementation. The Case Handling Note states:

It is ECGD policy to constructively engage with the exporter/investor to improve exports/projects to bring support of the export/investment into conformance with the Business Principles. However if this were not possible then support would not be provided.³⁸

Constructive engagement is distinct from the United States’ policy to block insurance from any project that does not conform to its standards.

iii) The World Bank (MIGA)

The Multilateral Investment Guarantee Agency (MIGA), one of the five World Bank Group institutions, provides a product similar to national export credit agencies, called an “investment risk guarantee”, focusing in particular on transfer restrictions, expropriation, breach of contract, war and civil disturbance. The MIGA was

created in 1988 as a member of the World Bank Group to promote foreign direct investment into emerging economies to improve people's lives and reduce poverty...Since its inception, MIGA has issued more than 500 guarantees for projects in 78 developing countries. As of June 2001, total coverage issued exceeded \$9 billion, bringing the estimated amount of foreign direct investment facilitated since inception to more than \$41 billion.³⁹

MIGA coverage is conditioned against environmental and social standards similar to those of the World Bank Group in general, but modified for the particular investment context. This means that there is a heavier emphasis on abiding by host country laws than on imposing restrictions directly in the guarantee contract. The social standards include the three World Bank policies (indigenous peoples, involuntary resettlement and cultural property), which regulate the impact of the investment on the broader community. The labour conditions relate to harmful child and forced labour.

The initial application form posted on the website does not have any social issues questions. Guarantee decisions are made using a series of social policies and procedures.

³⁷ See notes on Form IQ2 (Impact Questionnaire), at 62.239.5.9/impactanalysisguidancenotesapril2003.doc.

³⁸ *Case Handling Note, op. cit.*, note 34.

³⁹ See www.miga.org: About MIGA

The two clauses relevant to labour conditionality are from the *Environmental and Social Procedures* document, and their *Operational Regulations*.⁴⁰ These are set out in box 3. There is no specific reference to the ILO, nor is there reference to discrimination or freedom of association. These policies were adopted in 1998.

Box 3

MIGA Environmental and Social Procedures

15. MIGA's Operational Regulations (paragraph 3.08) explicitly state that "Investments of a military or highly speculative nature or in legally prohibited activities such as narcotics production shall not be covered." Consistent with practices among the other Bank Group members, MIGA will not provide guarantees for certain other types of business activities. These include: "...enterprises whose primary sources of income are gambling, prostitution, or involving forced labour or child labour inconsistent with internationally recognized norms.

MIGA Operational Regulations

- 3.08 Investment of a military or highly speculative nature or in legally prohibited activities such as narcotics production shall not be covered. MIGA shall not cover investments that do not comply with the national laws of the Host Country, including those that protect core labour standards and related treaties ratified by the Host Country; nor shall it cover investments that use Forced Labour or hire Harmful Child Labour.

iv) Japan

The Nippon Export and Investment Insurance company (NEXI) provides overseas investment insurance which

covers losses suffered by a Japanese company who establishes a subsidiary or a joint venture in a foreign country. The said losses may be incurred when the relevant subsidiary or the joint venture is forced to discontinue its business due to war, revolution, or force *majeure* such as natural disaster, etc. Insurance also covers losses incurred when a Japanese company is unable to remit dividend to Japan due to prohibition of foreign currency conversion into currency such as the yen or dollar or suspension of remittance.⁴¹

Political, natural disaster and currency transfer risks are thus mitigated for Japanese corporations investing abroad.

NEXI's Guidelines on Environmental and Social Considerations in Trade Insurance (April 2002, "Guidelines") governs all their insurance products, for both investment and trade.⁴² The Guidelines set out the environmental and social "considerations" which NEXI

⁴⁰ Their social policies are at www.miga.org/screens/policies/disclose/soc_rev.htm (See article 15 for their position on harmful child and forced labour). Their *Operations Regulations* are available at www.miga.org/screens/about/regulations/Operations-Regulations.pdf. (See paragraph 3.08 in particular on this topic).

⁴¹ See nexi.go.jp/e/02.html for various insurance instruments, including a description of NEXI's OII product. (Author's emphasis.)

⁴² Available online at nexi.go.jp/e/pdf/ins_kankyoku_gl-e.pdf.

uses to “contribute to [the] sound development of Japan’s external transactions”.⁴³ They encourage applicants to

undertake appropriate environmental and social considerations in accordance with the nature of the project, based on the principles listed in Exhibit 1 of the Guidelines.⁴⁴

Exhibit 1 sets out a few guiding principles, including the core idea that environmental and social impacts should be discussed early in the project cycle while it is still possible to propose alternatives. The agency clearly prefers to mitigate impacts than to compensate for them. The Exhibit then describes the scope of impacts to be examined:

Environmental impacts to be investigated and examined include factors that impact human health and safety as well as the natural environment, such as air, water, soil, waste, accidents, water usage and ecosystems and organisms; social concerns (e.g. involuntary resettlement, indigenous peoples, cultural heritage, landscape, gender, children’s rights and communicable diseases such as HIV/AIDS); and impacts that may lead to trans-boundary and global environmental problems.⁴⁵

These concerns do not directly address labour rights or employment conditions. In addressing health and safety and gender concerns though, the agency may indirectly address those matters.

The Guidelines contain detailed policies on involuntary resettlement (including compensation for loss of livelihood) and indigenous peoples, but neither contains direct comment on labour or employment matters. The closest we come to this is in the following sections:

Projects must be adequately coordinated so that the projects are accepted in a manner that is socially appropriate to the country and locality in which the project is planned. For projects with potentially large environmental impacts in particular, sufficient consultations with stakeholders, such as local residents, must be conducted via disclosure of information from an early stage when alternative proposals for the project plans may be examined. The outcomes of such consultations must be incorporated into the contents of the project plan;

and

Appropriate consideration must be given to vulnerable social groups, such as women, children, the elderly, the poor, and ethnic minorities, all of whom are susceptible to various environmental and social impacts and who may have little access, within society, to decision-making processes.⁴⁶

⁴³ *Ibid.*, section 1.

⁴⁴ *Ibid.*, section 2.

⁴⁵ *Ibid.*, Exhibit 1. (Author’s emphasis.)

⁴⁶ *Ibid.*, Exhibit 1. (Author’s emphasis.)

These considerations will likely lead to investment that improves the lives of workers, but again, their particular situation is not directly addressed in NEXI's guidelines.⁴⁷

NEXI implements these Guidelines throughout the project cycle, starting with the application for insurance, through a screening and categorization mechanism. It conducts a full environmental (and social) review of high-risk projects, which is incorporated into the decision-making process. Even after a commitment is made, NEXI "judges" monitor investments they have underwritten to ensure compliance, as well as accepting and investigating objections from third parties. Poor conformity may lead to a rejection of coverage, or a withdrawal later on.⁴⁸

The models used by export credit agencies in the United States, the United Kingdom, the World Bank and Japan demonstrate a range of options for the scope and method of linking support for foreign investment with social responsibility. The first two are especially important for demonstrating that a wide range of human rights and labour standards can be attached to foreign direct investment in a way that is enforceable with financial penalties, but which does not produce too great a burden for the private sector. Even between agencies with these high standards, there are different approaches with regard to implementation as strict rules or a policy of engagement to improve social responsibility. The United Kingdom's "sensitive cases" process, which involves other government priorities, is an important contribution to this discussion. MIGA's policy of refusing support for investments that rely on the worst forms of labour exploitation is a solid first step. Japan's holistic approach also offers an interesting model for social conditionalities.

Table 7: Export Credit Agencies: Labour, Environment and Process

| ECA | Current Exposure | Amount Underwritten | Labour Matters | Environment Matters | Process |
|------|---------------------|----------------------|--|-------------------------|-------------------------------|
| OPIC | US\$5.3 bn | US\$600 mn | Core labour rights plus wages, hours and health and safety | Yes OECD model | Penalties |
| ECGD | £821 mn (US\$1.4bn) | £126 mn (US\$215 mn) | Child labour, forced labour, discrimination | Yes OECD model | Constructive Engagement |
| MIGA | US\$5.2 bn | US\$2 bn | Child labour, forced labour | Yes World Bank model | Internal screening |
| NEXI | US\$5.6 bn | US\$418 mn | Health and safety, gender, children's rights, HIV/AIDS | Yes OECD Model | Integrates into project cycle |

Financial information from annual reports online (2001). See below for OECD environment model.

Environmental Conditionalities at Export Credit Agencies

Where ECAs have connected their investment products to environmental conditions, the model comes almost universally from an OECD agreement entitled *Common*

⁴⁷ Interestingly, NEXI reported against these guidelines in its 2001 Annual report, available online at nexi.go.jp.

⁴⁸ These procedures are paraphrased from the *Guidelines, op. cit.*, note 43, sections 3-7.

Approaches to the Environment and Officially Supported Export Credit. Twenty-five OECD countries agreed to this model, which was adopted in January 2002. Most of these nations use the agreement only with their trade-support products (export credit) rather than the overseas investment insurance under scrutiny here. Ten export credit agencies do analyse environmental impacts on this model: Australia, Canada, Czech Republic, Denmark, Finland, Hungary, Japan, the United Kingdom and the United States⁴⁹ and the World Bank's Multilateral Investment Guarantee Agency.⁵⁰

The *Common Approaches* Agreement deals almost exclusively with natural environment impacts. It does not include labour standards or any comment on employment conditions. However, at the outset it defines environmental impacts to include "impact on resettlement, indigenous or vulnerable groups and cultural heritage." These three areas are informed by social standards set at the World Bank (especially by the MIGA noted above, and the IFC, noted below). Otherwise, the Agreement works by categorizing projects for which export credit is supplied into three groups of descending risk:

Category A: a project is classified as Category A if it has the potential to have significant adverse environmental impacts. These impacts may affect an area broader than the sites or facilities subject to physical works. Category A should, in principle, include projects in sensitive sectors or located in or near sensitive areas. An illustrative list of sensitive sectors and sensitive areas is set out in Annex I.

Category B: a project is classified as Category B if its potential environmental impacts are less adverse than those of Category A projects. Typically, these impacts are site-specific; few if any of them are irreversible; and mitigatory measures are more readily available.

Category C: a project is classified as Category C if it is likely to have minimal or no adverse environmental impacts.⁵¹

These categories are subject to either a full-blown environmental and social impact assessment (cat. A), a detailed negotiation with the client (cat. B) or little further social review (cat. C). The regime calls for each member to report on their activities in this regard, a provision that has produced some interesting data.⁵²

Three characteristics of the *Common Approaches* framework make it a success. Firstly, it comes out of a multilateral setting, so member states (export credit agencies) feel that they are not losing a competitive advantage by raising social standards. Secondly, the

⁴⁹ See Australia: Export Finance and Insurance Corporation (www.efic.gov.au); Canada: Export Development Corporation (www.edc.ca); Czech Republic: Export Guarantee and Insurance Corporation (www.egap.cz); Denmark: Eksport Kredit Fonden (www.ekf.dk); Finland: Finnvera Plc. (www.finnvera.fi); Hungary: Hungarian Export Credit Insurance Ltd. (www.mehib.hu); Japan: Nippon Export and Investment Insurance (nexi.go.jp); United Kingdom: Export Credit Guarantees Department (www.ecgd.gov.uk); United States: Overseas Protection Investment Corporation (www.opic.gov) and Multilateral Investment Guarantee Agency (www.miga.org).

⁵⁰ MIGA's Environmental Policies are very similar to the OECD *Common Approaches* Agreement (see note 53 below), but based directly on the World Bank Group's standards.

⁵¹ *Draft Recommendations on Common Approaches to the Environment, Revision 6*. OECD Document TD/ECG(2000)11/REV6, available from www.oecd.org.

⁵² See for example "*Environment and Export Credits: 2002 Revised Coverage Matrix (Situation as at 2 April 2003)*", available from www.oecd.org.

reliance on national reporting rather than alternate dispute resolution mechanisms is a very positive way to meet the goal of the upward harmonization of environmental standards. Thirdly, the OECD has significant credibility among its members.

PART III: Development Finance Institutions – Private Sector Financing

The strongest expression of public support for foreign direct investment is to provide the financing for it. For the most part, investment finance comes from commercial financial institutions. Public financial institutions are limited to advancing specific public policy goals, like development in targeted countries, growth in small and medium-sized enterprises or promoting national exports abroad. Although public development finance institutions (“DFIs”) direct most of their funds towards the public sector, this section deals with the funds that go directly to the private sector. The section also includes a few remarks on public procurement, especially as sponsored by the development bank. Here, the processes of DFIs’ providing funding to the private sector are examined to see whether and how they oblige their corporate clients to respect labour or environmental standards.

Finance from DFIs comes in three main forms: loans, equity investments and guarantees. *Loans* may be secured against collateral or unsecured, syndicated by the DFI such that several financial institutions share the risk or subordinated to other loans taken by the company (sub-debt or mezzanine finance), and are given on various terms, but usually at market rates. *Equity investments* and quasi-equity loans involve the DFI taking a certain percentage of ownership in the firm, usually not more than a pre-determined limit in the 30-49 per cent range. *Guarantees* are instruments that assist the corporation in securing finance from private financial institutions. Most institutions offer these products on a ‘project finance’ basis, in order to accomplish a certain task. Many DFIs also provide this as ‘corporate finance’ to firms operating on an ongoing basis in the developing world. The following discussion is an examination of ten DFIs’ eligibility criteria and how they evaluate applications to describe their different approach to social obligations.

Forty-six regional and national development finance institutions were examined. Of these, nine did not indicate any eligibility criteria or related information at all, so their social conditionalities are unknown.⁵³ The 37 remaining DFIs were categorized as follows:

- Nine DFIs linked their private sector finance to core labour rights in some manner,⁵⁴
 - and a tenth has very high social standards that do not directly implicate labour;⁵⁵
- Seven DFIs had mainly environmental clauses, but also placed emphasis on job creation and training, as well as other social goals short of labour rights;⁵⁶

⁵³ Industrial Development Bank of Turkey; Sabah Development Bank; Industrial Development Bank of Pakistan; Development Bank of Mauritius Ltd; Arab Fund for Economic and Social Development; SIMEST – Italy; APAD – Portugal; COFIDES – Spain; FGG – Austria.

⁵⁴ International Finance Corporation (IFC-World Bank Group); Inter-American Development Bank (IDB); OPIC US; CDC Capital Partners – UK; KfW - The German Development Bank; FMO – Netherlands; IFU, IO, IFV (Danish International Investment Funds); Norfund – Norway; Development Bank of South Africa.

⁵⁵ Asian Development Bank.

-
- Twelve DFIs attached environmental clauses but no further social conditions;⁵⁷ and
 - Eight DFIs attached no social conditionality at all to their private sector finance;⁵⁸

Labour and Employment Conditionalities and Development Finance

Nine development finance institutions included some or all of the core labour rights identified in the ILO 1998 *Declaration on Fundamental Principles and Rights at Work* in qualifying investment projects for their involvement. They are: the World Bank Group (through the International Finance Corporation), the Asian Development Bank, the Inter-American Development Bank, the Overseas Protection Investment Corporation (United States), CDC Capital Partners (United Kingdom), KfW (Germany), FMO (Netherlands), IFU, IO and IFV (Danish International Investment Funds), Norfund (Norway), and the Development Bank of South Africa.

i) World Bank Group

One of the World Bank Group institutions, the International Finance Corporation is charged with providing finance to *private corporations* in the *developing world*. The IFC shares the World Bank's mission to "reduce poverty and improve people's lives." Their work is set out as follows:

IFC provides affordable capital and global experience to businesses in high-risk, developing countries to improve the long-term viability of markets in these nations. IFC's mandate essentially is to further economic development through the private sector.⁵⁹

The IFC can provide loans, equity and guarantees. Access to this capital depends on the investment meeting five criteria. It must:

- be located in a developing country that is a member of IFC
- be in the private sector
- be technically sound

⁵⁶ Central American Bank for Economic Integration; Brazilian Development Bank; Caribbean Development Bank; Bahamas Development Bank; Hellenic Industrial Development Bank; Andean Development Corporation; FinnFund – Finnish Industrial Co-op fund.

⁵⁷ North American Development Bank; European Bank for Reconstruction and Development; Council of Europe Development Bank; Black Sea Trade and Development Corporation; Development Bank of the Philippines; African Development Bank Group; France Development Agency; Development Bank of Japan; Islamic Development Bank Group; Swiss Development Finance Corporation; OPEC Fund for International Development; Swedfund International AB.

⁵⁸ Korea Development Bank; National Development Bank of Sri Lanka; Economic Development Corporation of Goa, Daman, and Diu Ltd; Qatar Industrial Development Bank; Eastern and Southern Africa Trade and Development Bank; East African Development Bank; Industrial Development Bank of Kenya; SBI-BMI – Belgium.

⁵⁹ See www.ifc.org: About IFC.

- have good prospects of being profitable
- benefit the local economy and it must be environmentally and socially sound, satisfying IFC environmental and social standards as well as those of the host country.⁶⁰

The environmental and social standards are evaluated by CESRU, the IFC's environmental and social impacts analysis unit. CESRU has promulgated a series of standards for the private sector, including draft recommendations on occupational health and safety. It analyses a series of environmental impacts, as well as the three social policies shared with the other World Bank institutions: *involuntary resettlement*, *indigenous peoples* and the protection of *cultural property*.

Box 4

IFC 2002 Annual Report

"The business case is at the heart of our new approach to sustainability. A growing body of evidence suggests that improving projects' impact beyond the financial bottom line can in many cases also make good business sense. ...Even where the business case is not apparent today, we find that the changing business landscape is likely to reveal new risks from ignoring sustainability and new opportunities for high-impact sustainability practices that offer commercial benefit in new places for more firms."

Source: www.ifc.org/ar2002/investing/introduction.html: Investing in a Sustainable Private Sector.

More recently, CESRU has been focusing on forced and harmful child labour. This policy refers to ILO standards. As it was promulgated in 1998,⁶¹ it only refers to Convention 138 (of 1979), not the *Convention 182 concerning the Prohibition and Immediate Action for the Elimination of the Worst Forms of Child Labour (1999)*. The policy makes allowance for 'non-harmful' child labour. The definitions are as follows:

'*Forced Labour*' consists of all work or service, not voluntarily performed, that is exacted from an individual under threat of force or penalty.

'*Harmful Child Labour*' consists of the employment of children that is economically exploitative, or is likely to be hazardous to, or interfere with, the child's education, or to be harmful to the child's health, or physical, mental, spiritual, moral, or social development.⁶²

The labour standards analysis deals only with the worst forms of exploitation. The policy is exclusionary though: no finance is permitted to go to investors using these practices. The IFC does not yet address freedom of association and the right to collective bargaining or non-discrimination or any further employment conditionalities, except the draft occupational health and safety guidelines.⁶³

⁶⁰ See www.ifc.org: Applying for Financing.

⁶¹ This is the same year that MIGA implemented their child and forced labour policy. See Operations Regulations, op.cit., note 41.

⁶² See CESRU at www.ifc.org/enviro. The *Harmful Child and Forced Labour* policy is at www.ifc.org/enviro/EnvSoc/childlabor/Child_and_Forced_Labor.pdf

⁶³ Available online at www.ifc.org/enviro/EnvSoc/pollution/occupation/DraftOHS.pdf.

ii) **Asian Development Bank**

The Asian Development Bank replicates the World Bank's three social policies – indigenous peoples, involuntary resettlement and cultural property – in its private sector financing. However, the ADB does not follow the World Bank's lead on forced and harmful child labour. The ADB's private sector operations department requires applicants to submit detailed proposals for financing, including an independently prepared environmental impact assessment.⁶⁴ The ADB then clears the concept, establishes the facts, appraises the project and negotiates any difficult points before submitting it to the Board of Directors for approval and closing the financial arrangements.⁶⁵ In establishing the facts, the bank runs the project through their environmental and social guidelines, including the three social policies.⁶⁶ While the ADB does not apply core labour standards to its project evaluations, it is committed to promoting respect for these standards (especially with child labour) through a series of dialogues and engagement with its member states.⁶⁷

iii) **Inter-American Development Bank (IDB)**

Within the IDB the Inter-American Investment Corporation (IIC) provides private sector financing for development goals. The IIC's primary development goal is *job creation*. Its mission is to

promote and support the development of the private sector and the capital markets in its Latin American and Caribbean member countries by investing, lending, innovating and leveraging resources as the institution charged with fostering the development of small and medium-sized enterprises to further sustainable economic development.⁶⁸

Loans (and syndication), equity investments and guarantees are all available to IIC clients.

In addition, the IDB itself has a department that lends to the private sector, primarily for infrastructure projects, while its Multilateral Investment Fund (MIF) aims to mobilize capital for small and medium-sized enterprises by lending to financial intermediaries who

⁶⁴ See www.adb.org/PrivateSector/Operations/procedures.asp.

⁶⁵ See www.adb.org/PrivateSector/Operations/process.asp.

⁶⁶ The three policies are available respectively at:
www.adb.org/Documents/Policies/Indigenous_Peoples/ipp-001.asp;
www.adb.org/Documents/Policies/Involuntary_Resettlement/involuntary_resettlement.pdf; and
www.adb.org/Documents/Guidelines/Environmental_Assessment/Cultural_Heritage.pdf.

⁶⁷ See for example “*Strengthening the role of labour standards in selected DMCs*,” by Frank Hagemann, ILO and Joseph Lim, UNDP/RETA Consultant. Main recommendations at: www.adb.org/Documents/Events/2002/Core_Labor_Standards/hagemann.PDF; “*Combating Child Labour in the Philippines*,” www.adb.org/Documents/Events/2002/SocialProtection/sardana_presentation.pdf; Hawaii seminar 2001 “*Child Labour and Poverty*,” www.adb.org/AnnualMeeting/2001/seminars/child_labor.html. According to an IFBWW press release, “in September 2001 the ADB adopted a policy stating that the ADB will take all necessary and appropriate steps to ensure that contractors, subcontractors and consultants comply with the country's labour legislation and Core Labour Standards in ADB financed procurement of goods and services.” See IFBWW News 34 – 9 May 2003 at www.ifbww.org/index.cfm?n=44&l=2&c=940. This policy is not indicated on the ADB's website.

⁶⁸ See www.iic.int. (Author's emphasis).

on-lend under MIF conditionalities. All three IDB institutions share a common environmental and social analysis framework. The MIF has one further policy, which aims to ensure that when it lends to local banks, these intermediaries will lend under the same social obligations that the Bank would impose directly.

The IDB analyses projects in terms of their impact on labour rights and working conditions, but their policy relies on compliance with local regulation rather than with international standards. In the application process, clients are informed that:

All projects must include a description of potential environmental impacts, including an assessment of compliance with environmental, worker safety and labour regulations, and specific mitigation measures to be taken if required.⁶⁹

The Inter-American Investment Corporation's *Environmental and Labour Standard* directly forbids forced and child labour, but relies on national law to deal with "core labour rights" (identified as (1) freedom of association; (2) right to organize and collective bargaining; (3) abolition of forced labour; (4) elimination of exploitative/harmful child labour; and (5) non-discrimination in employment and occupation.)⁷⁰ In this way, the institution commits itself to refusing finance to projects that engage in the worst forms of exploitation, but approaches non-discrimination, free association and collective bargaining in a normative, evolutionary manner.

iv) OPIC (United States)

OPIC is the same organization that provides overseas investment insurance in the United States. Their labour conditionalities are similarly high when granting financing. Since 1971, the Overseas Protection Insurance Corporation "has made \$145 billion worth of investments, generated \$65 billion in U.S. exports and created more than 254,000 jobs in the United States."⁷¹ OPIC's mission is

to promote and facilitate U.S. investment in emerging market economies by providing medium- to long-term loans and guaranties to projects involving significant equity or management participation.

The Corporation provides both project and corporate finance, in the form of loans and guarantees, mostly with an equity investment of some degree. Eligibility for this financing is strictly controlled by social obligations:

OPIC is prohibited by statute from supporting projects that contribute to violations of internationally recognized worker rights. OPIC's finance agreement requires the investor to agree to respect these rights, including the rights of association, collective bargaining, and acceptable working conditions with respect to wages, hours of work, occupational health and safety, and minimum age requirements.⁷²

⁶⁹ See www.iic.int/apply/financing_envirion.asp.

⁷⁰ See "Procedure for Environmental and Labor Review of IIC Projects", dated 04/27/1999, at www.iic.int/policies/042799_projectreview.ASP, section 26 and footnote 2.

⁷¹ See www.opic.gov: About Us.

⁷² See www.opic.gov: Insurance, finance and funds: OPIC Finance: Eligibility: Supporting Workers Right. (Author's emphasis).

There is no specific international standard attached to this policy, nor any reference to the ILO. Their environmental policy is similarly strict:

OPIC is required by statute to conduct an environmental assessment of every project proposed for financing and to decline support for investment projects that, in OPIC's judgment, would have an unreasonable or major adverse impact on the environment, health, or safety in the host country.⁷³

OPIC aims to ensure not only that it avoids adverse social impacts but also that its funds contribute to positive development. To that end, they seek to maximize job creation, develop skills in host States through training, transfer technology where possible and stimulate local enterprises.⁷⁴

The process of applying for finance is much more involved than with OPIC's overseas investment insurance product. The wording of the Worker Safety and Worker Rights section in the initial application is much shortened, though:

WORKER SAFETY AND WORKER RIGHTS

- a) If there is an existing project company, does it permit its workers to form or join a labour union?
- b) If the project company is an existing project company, are the workers unionized?
- c) Is a collective bargaining agreement in effect?
- d) What is the legal minimum age for employment in the project country? Age:
- e) What is the legal minimum age for employment in hazardous activities? Age:
- f) What are the legal maximum hours of work without payment of overtime? Hours: With overtime? Hours:
- g) Will employees at the project be employed by contractors or subcontractors or will they be employed by the project company?⁷⁵

The initial application form is generally supplemented with a more formal proposal, and goes through a series of screening and due diligence mechanisms before reaching approval.

OPIC monitors the projects it supports for a number of purposes, one of which is compliance with social guidelines. One method of monitoring is a *Self-Monitoring Questionnaire for Insurance & Finance Projects*. The opening instructions on this form state:

⁷³ See www.opic.gov: Insurance, finance and funds: OPIC Finance: Eligibility: Enhancing the Environment. (Author's emphasis).

⁷⁴ See www.opic.gov: Insurance, finance and funds: OPIC Finance: Eligibility: Contributing to Development.

⁷⁵ The application form is available at <http://www.opic.gov/forms/FORMS.HTM>. See especially Form 115, Parts D and E for questions regarding "*Social Effects (Good Corporate Citizenship)*", *Worker Safety* and *Worker Rights*.

This form requests information from OPIC clients which is required by OPIC's governing legislation. The information provided in this questionnaire will allow OPIC to better assess the effects that OPIC-assisted projects have on the U.S. economy and employment, as well as the environment and economic development abroad. Complete responses to the collection of information in this form are mandatory, per the Foreign Assistance Act of 1961, as amended, Section 231(k)(2).⁷⁶

The questionnaire requires investors (project sponsors) to detail the impacts of the new investment that OPIC was involved with. There is only one labour question in this questionnaire (see box 5). The consequence for non-compliance with labour and environmental standards is the withdrawal of support.⁷⁷

Thus, OPIC is committed to the mandatory application of high social standards on all its investment finance. These are reviewed in the application process and on an ongoing basis to ensure that resources are not used in violation of international standards on labour rights or the environment.

| | | | | | | | | |
|---|-----------------|-------------------------------|-------------------------------|---------------|-----------|---------------|--------------------|---------------|
| <p>Box 5</p> <p>Self-Monitoring Questionnaire for Insurance & Finance Projects</p> <p>9 a. Have there been any changes in the Project or the environment which have created new environmental, or occupational health & safety issues? No/Yes</p> <p>(If so, please attach a brief description of the changes and the measures taken to address them.)</p> <p>b. Labour conditions -- please check any that applied within the last 12 months:</p> <table><tr><td>1. Labour Union</td><td>No/Yes</td><td>2. Collective Labor Agreement</td><td>No/Yes</td></tr><tr><td>3. Strike</td><td>No/Yes</td><td>4. Hazardous labor</td><td>No/Yes</td></tr></table> <p>5. Does the project employ anyone under 18? No/Yes</p> <p>(If yes, attach a description of duties and age of youngest worker)</p> <p>6. <i>Maximum Workweek Without Overtime:</i></p> <p style="text-align: center;">40-44 Hrs. ___ 45-48 Hrs. ___ more than 48 Hrs. ___</p> <p>Source: www.opic.gov/forms/Form%20162%20-%20selfmon.doc</p> | 1. Labour Union | No/Yes | 2. Collective Labor Agreement | No/Yes | 3. Strike | No/Yes | 4. Hazardous labor | No/Yes |
| 1. Labour Union | No/Yes | 2. Collective Labor Agreement | No/Yes | | | | | |
| 3. Strike | No/Yes | 4. Hazardous labor | No/Yes | | | | | |

v) **CDC Capital Partners (United Kingdom)**

CDC Capital Partners is a new incarnation of the Commonwealth Development Corporation, which has been investing in the private sector in developing countries for fifty years. It offers only equity investments, not loans or guarantees. It grounds its work in five key investing principles:

- ✓ To be open and honest in all our dealings, while respecting commercial and personal confidentiality;

⁷⁶ See www.opic.gov/forms/FORMS.HTM.

⁷⁷ "OPIC systematically monitors investor compliance with U.S. economic, environmental, worker rights, and corrupt practices representations through questionnaires, investor reporting, and site visits. **Non-compliance may constitute a default under OPIC loan agreements.**" See www.opic.gov: Insurance, finance and funds: OPIC Finance: Eligibility: Monitoring for Compliance. (Author's emphasis).

-
- ✓ To be objective, consistent and fair with all our stakeholders;
 - ✓ To be a good corporate citizen, demonstrating integrity in each business and community in which we operate;
 - ✓ To respect the dignity and well-being of all our people and those with whom we are involved;
 - ✓ To operate professionally in a performance-orientated culture and be committed to continuous improvement.⁷⁸

CDC Capital Partners employs a Human Rights Framework to assess the *countries* where their clients will invest against social criteria. This feature is rare among DFIs, which tend only to assess the investment at hand rather than the broader context.⁷⁹ The Framework is a balance of avoiding the worst forms of human rights abuses and engaging with the least developed countries, which often have such records, in an effort to raise standards there. It is used to identify which areas of human rights and labour standards are likely to be most at risk in the investment, and thus subject to the most due diligence and monitoring by the CDC. The policy addresses all the core labour rights as well as certain working conditions by investigating the following:

Does the country lack fair labour regulations? In particular

- ✓ Are there records of forced labour?
- ✓ Are there records of child labour?
- ✓ Are there records of discrimination in employment?
- ✓ Are working hours excessive?
- ✓ Is the current remuneration policy insufficient for an adequate standard of living?
- ✓ Are trade unions and other employee associations prohibited / restricted in any way?
- ✓ Does the country fail to provide acceptable health and safety conditions for the employees and their families or our company representatives?⁸⁰

In addition to the human rights framework, CDC Capital Partners maintains a health and safety and a social issues policy, each of which concerns investors' social obligations for labour and employment matters.⁸¹ The broadest objective of the health and safety policy is

⁷⁸ See www.cdcgroup.com.

⁷⁹ See the FMO (Netherlands DFI) description below for another, less rigorous use of this method.

⁸⁰ Human Rights Framework: Country Assessment Guidelines. See www.cdcgroup.com/how_we_can_help/investing_responsibly.asp at 1. (Author's emphasis).

⁸¹ These are available at www.cdcgroup.com/how_we_can_help/investing_responsibly/business_policies.asp: health and safety; social issues. The human rights policy is within the social issues page.

to seek to ensure that businesses in which we invest comply with *internationally recognised standards* of good practice in order to protect the health and safety of their employees while at work.

Similarly, the social issues policy aims

to require the businesses in which we invest to treat fairly all their employees and contractors, and to respect their dignity, well-being and diversity ...[and] to work over time towards full compliance of our investments with the ILO Fundamental Conventions and with the UN Declaration of Human Rights.

CDC's bottom line is that they will not engage in countries that the UK, EU or UN have sanctioned (taking into account NGO campaigns as well). Otherwise, they will invest and monitor the situation to mitigate adverse impacts, based on the belief that such engagement is likely to improve social conditions. (This approach is similar to the UK's export credit agency, reviewed above.)

vi) KfW / DEG Invest (Germany)

KfW is the parent development finance institution in Germany. Its wholly owned subsidiary, DEG Invest, takes care of private sector financing.⁸² Both institutions have high standards on labour and environmental conditionalities. KfW stands out among its peers for its rigorous ex-post evaluation system that contributes to institutional learning and increasing best practice. They evaluate every project after five years, rating it on a scale of success from one to five (against effectiveness, efficiency, significance and relevance), and then produce a report every year evaluating the overall success rate of their strategy and adjusting themselves accordingly. DEG Invest's mandate is as follows:

DEG promotes private enterprise in developing and transition countries as a contribution to sustainable growth and a lasting improvement in the living conditions of the local population. Therefore, we provide long-term capital for private enterprises investing in those countries.

We only take on commitments in projects that make an effective development policy impact, meet environmental standards and comply with social principles. We are particularly committed to our developmental mandate and our guidelines for social and environmental compatibility: they form the decisive frame of our work.⁸³

DEG Invest offers equity finance, mezzanine finance, long-term loans and guarantees. It not only invests in the private sector of developing countries, but also aims to develop local capital markets to expand those investments sustainably. This process maximizes their development impact in the long term (captured in the idea that they seek to ensure that the investment produces "socially relevant effects."). DEG Invest ensures compliance with each of the core labour rights, with direct reference to ILO Conventions, as well as much higher standards on health and safety, hours and wages. Their *Guidelines on the Social Compatibility of DEG Business Operations*, which include these standards, state:

DEG has specialised in long-term project and corporate finance in developing and transition countries. As a development finance institution we are committed to upholding and respecting social human rights in our business activity. Apart from the fundamental labour standards of the International Labour

⁸² See www.kfw.de and www.deginvest.de.

⁸³ See www.deginvest.de.

Organisation (ILO), this involves internationally acknowledged social agreements and guidelines, as well as local regulations in DEG's partner countries.⁸⁴

By attaching both international and local standards to their social conditionalities, Germany provides a good middle ground between the Inter-American Development Bank (which relies entirely on local regulation) and countries like the United States (which rely only on international standards). This policy implies a healthy relationship of respect for countries that host DEG's supported investments.

vii) FMO (Netherlands)

The Dutch development finance institution, FMO, is mandated "to achieve the highest possible development impact and to generate a favourable return on investment".⁸⁵ It offers a particularly wide range of financial products, including loans, guarantees, syndicated loans, equity and quasi equity investment finance.

FMO requires a double set of social obligation for its investor clients.⁸⁶ Their internal obligations include mandatory rules on the treatment of the investor's employees, such as abiding by international standards on all core labour rights (especially ILO Conventions). The policy has a strong emphasis on industrial relations, but also includes provisions regarding hours, contracts, wages, consultation in case of retrenchment, and health and safety. Additionally, investors are obliged to abide by a series of external social policy rules, including World Bank policies on indigenous peoples, involuntary resettlement and cultural property, and requirements for public consultation to mitigate any impacts on the wider community. All of these policies are mandatory, and explicitly based on ILO Conventions and World Bank standards.

These social policies are intricately linked with FMO's decision-making process. FMO also accounts for host country conditions rather evaluating the investment alone, as is the case in the U.K. with CDC Capital Partners. (The process is set out in box 6).

⁸⁴ See www.deginvest.de/english/home/company/our_mandate/guidelines_social/index.html.

⁸⁵ See www.fmo.nl.

⁸⁶ See FMO's social policy at <http://www.fmo.nl/downloads/en/social-policy.doc>.

Box 6

FMO Evaluation Process

In evaluating an investment request, the project itself is looked at initially. Important aspects are:

- commercial viability.
- a sound investment plan.
- a thorough feasibility study and complete analysis of the market.
- transparency according to the principles of corporate governance.
- a respectable environmental policy.
- execution by internationally acceptable social standards.

Furthermore, the owner or sponsor of the project to be financed is considered. The important factors are that it:

- is financially healthy.
- has a proven track record.
- is being guided by an expert, experienced and ethical management.

Additionally, any intended cooperation with a partner(s) is assessed. A potential financing partner can be, for example:

A local financial party, under the conditions that it has a proven track record and a good reputation and is a party that FMO complements in terms of country knowledge, sector knowledge and/or the investment process.

A large, often internationally-operating enterprise or financial institution which is active in the sector concerned.

Finally, factors affecting the surroundings are also weighed. Namely the economic, social and political situation in the country of investment.

Source: www.fmo.nl/en/aboutfmo/criteria.php

viii) IFU, IO and IFV (Danish International Investment Funds)

Denmark participates in development finance through three investment funds. IFU addresses the private sector in developing countries with a per capita income below the World Bank's upper limit for new loans (US\$ 5,225 in 2002). IFV's clients are private firms in developing countries with a per capita income above the same World Bank limit. IO invests in the private sector in Central and Eastern Europe and administers an Environmental Investment Facility. The funds offer both equity capital and loans.⁸⁷

All three funds share a common environmental and social analysis framework. These are set out in an environmental policy⁸⁸ and a code of conduct⁸⁹ in which core labour rights are protected by reference to key ILO Conventions. Denmark attaches the Code to all projects in which the funds invest. Its stated goal is to

⁸⁷ See www.ifv.dk, www.ifu.dk and www.io.dk.

⁸⁸ See www.ifu.dk/EnvironmentalPolicy/EnvironmentalPolicy.pdf.

⁸⁹ See www.ifu.dk/common/Cc.pdf

constantly strive to enhance awareness, to heighten standards and to work for continuous improvement in all matters related to business ethics, social responsibility, human rights, occupational health and safety as well external environment.

The Code goes on to explicitly reference international standards in these areas, including all the ILO conventions related to the core labour rights.

The Funds are developing a Human Rights Compliance Assessment on the model of the environmental impact assessment. Financing decisions are made in the reciprocal, relational manner of the United Kingdom institutions: a project sponsor approaches the appropriate Fund, they receive a preliminary estimate and are asked for a fuller investment proposal (or application), which is reviewed and subjected to further environmental and social impact studies before a decision is made.

Denmark's environmental policy is based on conducting environmental assessments, with a "best judgment declaration" and an evaluation afterwards:

THE FUNDS intend to prevent or minimise possible adverse environmental effects, and to promote a positive impact. This applies to the external environment as well as to the working environment (occupational environment).

The Funds identify environmental effects in the following areas: human health and safety – including the working environment; nature and wildlife; soil; water; air; climate; landscapes.

ix) Norfund (Norway)

The Norfund is a small development finance institution that makes equity investments only, mostly for SMEs, "to create capital and employment in private enterprises in developing countries". Finance applications include a social assessment form, which deals with labour rights and working conditions in depth. Norway's policy in this area reflects a balance between belief in the power of markets to address many of these issues, and the importance of international social standards:

Norfund firmly believes that a profitable business establishment improves the standard of living in the area where it is deployed; hence, Norfund has no specific development scheme that must be fulfilled. Norfund will, nonetheless, monitor the project and report on the most obvious improvements... Norfund believes that for a project to be sustainable and profitable, it is absolutely necessary for it to follow international standards that are widely accepted by today's business community.⁹⁰

Norfund's application process includes requiring the investor to guarantee that high standards will be applied when the project is implemented. The declaration covers equal opportunities, gender equality, child labour, forced labour, reasonable working hours, voluntary overtime, living wages, freedom of association and collective bargaining. The Norfund does not refer to ILO Conventions or other international standards in this assessment process though. Additional social policies at Norfund include the World Bank policies on involuntary resettlement, indigenous peoples and cultural property, HIV/AIDS and anti-corruption.

⁹⁰ See www.norfund.no: Project Proposal: Proposal: Development Impact.

Their environmental policy also takes the form of a questionnaire/declaration, and addresses air pollution, water pollution, wastes, ambient noise, occupational health and safety, hazardous materials, major accident prevention and emergency planning.

x) Development Bank of South Africa

The Development Bank of South Africa, reconstituted in 1996 to better serve the needs of the new state, has a social policy uniquely suited to South Africa's history. The DBSA's mandate is

to invest in infrastructure and facilitate the provision of infrastructural development finance...[to] finance sustainable development in partnership with the public and private sectors...[and to] respond to development demands and act as a catalyst for investment.

Accordingly, their finance instruments for the most part go to the private sector engaged in providing infrastructure for the nation. In social terms, DBSA has two key goals: racial and gender equity and job creation. In their own words,

The DBSA's policy work aims to optimise development impact, positive economic outcomes, address socio-economic development backlogs and maximise the impact of projects in respect of gender, racial equity, sustainable job creation, appropriate technology, community participation and environmental sustainability.⁹¹

This policy stems from a vision on the DBSA to "be a leading change agent for accelerated and equitable socio-economic development in Southern Africa." Specifically, they identify sensitivity to the needs of the poor and implementation of a best-practice policy in all activities, including social and environmental practices as key areas for the institution.⁹²

Table 8 compares the preceding ten DFIs on labour rights and their financial positions. It shows that half of these institutions reference the ILO for their labour standards. It also notes that where a DFI addresses labour at all, it tends to include all four core labour rights. The biggest exception is the World Bank which deals primarily with child and forced labour.

⁹¹ See www.dbsa.org/AboutTheBank/AboutMaster.htm: DBSA Overview: Policy Work. (Author's emphasis.)

⁹² See www.dbsa.org/AboutTheBank/AboutMaster.htm: DBSA Overview: Vision.

Table 8: Private Sector Financing and Core Labour Rights Obligations

| DFI | Latest Year Data Available | New private sector financing (US '000) | Free Association/ Collective Bargaining | Ban on Child Labour | Ban on Forced Labour | Non-Discrimination | ILO Reference |
|------------------------|----------------------------|--|---|---------------------|----------------------|--------------------|---------------|
| IFC | 2002 | 2 723 550 | | √ | √ | | Yes |
| IADB (Americas) | 2002 | 1 171 700 | √ | √ | √ | √ | No |
| OPIC (U.S.) | 2002 | 844 072 | √ | √ | √ | √ | No |
| CDC (U.K.) | 2002 | 400 000 | √ | √ | √ | √ | Yes |
| KfW (Germany) | 2002 | 548 000 | √ | √ | √ | √ | Yes |
| FMO (Netherlands) | 2002 | 458 000 | √ | √ | √ | √ | Yes |
| IFU, IO, IFV (Denmark) | 2001 | 386 000 | √ | √ | √ | √ | Yes |
| NorFund (Norway) | 2001 | 1 500 000 | √ | √ | √ | √ | No |
| DBSA (S. Africa) | 2002 | 199 680 | | | | √ | No |
| ADB | 2002 | 180 000 | | (?) | | | No |
| Total | | 8 411 002 | 7/10 | 8/10 | 8/10 | 8/10 | 5/10 |

Job Creation and Training

Development finance institutions generally believe that poverty eradication will only be achieved through the creation of employment and the spread of labour skills. FDI is an important contributor to developing countries for both these reasons – in creating jobs and skill transferring. Investment projects are highly favoured when they emphasize either of these features. The ten DFIs discussed above all promote job creation and training. These criteria are also mentioned specifically by each of the following institutions: the Central American Bank for Reconstruction and Development, Brazil Development Bank, Caribbean Bank, Bahamas Development Bank, Hellenic Industrial Development Bank, Andean Development Corporation and the FinnFund.⁹³ These DFIs do however not specify the conditions of work at these new jobs, nor any related labour rights.

Environmental Standards and Development Finance

Of the 37 development finance institutions examined here, only eight did not have an environmental standard of any kind.⁹⁴ The World Bank's standards and procedures are widely replicated. Environmental standards in public investment support are more or less consistent across the board. The World Bank takes the lead in investment finance, mirroring the OECD's lead in investment insurance (and export credit). These two

⁹³ See note 58.

⁹⁴ See note 60.

institutions have promulgated very similar standards: dividing incoming projects according to their risk into three categories which then receive different screening.⁹⁵

Interestingly, for development finance, environmental policies are extremely specific in terms of risks and industries. For instance, at the IFC (World Bank), there are a series of ‘safeguard policies’ that address issues as diverse as natural habitats, pest management, forestry, safety of dams and international waterways. They also identify 28 ‘sectoral guidelines’ that deal with environmental dangers in specific industries.⁹⁶ Additionally, the World Bank’s Pollution Prevention and Abatement Handbook is a widely cited authority on specific standards.

Public procurement

Private sector investors seeking public finance *on their own initiative* face various social obligations as described above. These obligations *do not apply* to public procurement by development finance institutions. DFIs often spend far more on procurement than they do on direct finance to the private sector. For instance, at the World Bank Group, the IFC provided US\$2.7 billion financing in loans, equity investment and guarantees in 2002, but did not play any role in procurement. In the same year, two related World Bank institutions – the International Bank for Reconstruction and Development and the International Development Corporation – procured *nearly ten times* that amount (US\$11.5 billion and US\$8.1 billion respectively.)⁹⁷ Their combined *Guidelines on Procurement* not only lack the social obligations found at the IFC, but also state that procurement decisions **must** be based only on economy and efficiency, “without regard to political and other non-economic influences or considerations.”⁹⁸

The World Bank sets the standard on development procurement with very few exceptions. Their principles on economy and efficiency are complemented by a commitment to transparency and non-discrimination, and are replicated at all major regional DFIs. The World Trade Organisation’s plurilateral agreement on government procurement reaffirms the latter two principles.⁹⁹

The latter is essentially a *trade liberalisation* agreement. Its goal is to open government procurement tendering processes to all products and suppliers from each of the Party States without discrimination,¹⁰⁰ and to ensure this is happening by making tendering procedures as transparent as possible.¹⁰¹ The agreement does not provide directly for any

⁹⁵ See *OECD Common Approaches, op. cit.*, note 53, and World Bank (IFC) Environmental Policy at www.ifc.org/enviro/EnvSoc/index.html#policies.

⁹⁶ See www.ifc.org/enviro/EnvSoc/pollution/guidelines.htm.

⁹⁷ Compare annual reports at www.ifc.org and www.ibrd.org and www.ida.org.

⁹⁸ See www.worldbank.org/html/opr/procure/guidelin.html, Section 1.2, with reference to the World Bank’s Articles of Agreement.

⁹⁹ The text of the agreement, background and analysis are available at www.wto.org/english/tratop_e/gproc_e/gp_gpa_e.htm.

¹⁰⁰ See article III, *Agreement on Government Procurement* (Uruguay Round Agreement, Annex 4b), available at www.wto.org/english/docs_e/legal_e/gpr-94_01_e.htm.

¹⁰¹ *Ibid.*, article XVII.

social responsibility vetting (i.e. explicitly permitting or requiring members to procure only from those corporations with a respectable track record on labour or environmental issues.)

The question arises whether the agreement *prevents* such vetting. The Agreement governs two processes. The first is **qualifying suppliers**, that is, researching and vetting corporations to decide whether – in principle – they could supply any future demand. The second is the **tendering process** where an actual demand exists and the government seeks to fill it by asking a variety of corporations to bid on the contract.

i) Qualifying suppliers

The key passage governing this process reads as follows:

In the process of qualifying suppliers, entities shall not discriminate among suppliers of other Parties or between domestic suppliers and suppliers of other Parties. Qualification procedures shall be consistent with the following: ...

(b) any conditions for participation in tendering procedures shall be limited to those which are essential to ensure the firm's capability to fulfil the contract in question. Any conditions for participation required from suppliers, including financial guarantees, technical qualifications and information necessary for establishing the financial, commercial and technical capacity of suppliers, as well as the verification of qualifications, shall be no less favourable to suppliers of other Parties than to domestic suppliers and shall not discriminate among suppliers of other Parties. The financial, commercial and technical capacity of a supplier shall be judge on the basis both of that supplier's global business activity as well as of its activity in the territory of the procuring entity, taking due account of the legal relationship between the supply organisations.¹⁰²

The bold portion read alone seems to indicate that any capable firm (in the financial, commercial and technical sense of the word) shall be equally qualifiable as a supplier. On its face, this clause appears to exclude the possibility of social vetting, as a corporation with a poor record of social responsibility may be just as 'capable' as one with a strong record. However, the mischief this article is trying to avoid is discrimination based on *nationality*. In that way, the phrase "regardless of national origin" may be implied at the end of the bold portion. There is no mention of social standards anywhere here; it may reasonably be assumed that the Parties did not turn their minds to the idea of social vetting in the qualification of suppliers and thus did not block the possibility with this clause.

ii) Tendering Process

There are two basic types of tendering documents in the main forms of procurement (that is, in open or selective bidding): an "invitation to participate" and full "tender documentation". The former must provide certain information, including "any economic and technical requirements, financial guarantees and information required from suppliers."¹⁰³ The latter must give suppliers "all information necessary to permit them to submit responsive tenders" including:

(f) any economic and technical requirements, financial guarantees and information or documents required from suppliers,

¹⁰² *Ibid.*, article VIII.

¹⁰³ *Ibid.*, article IX, 6(f).

(g) a complete description of the products or services required or of any requirements including technical specifications, conformity certification to be fulfilled, necessary plans, drawings and instructional materials;

(h) the criteria for awarding the contract, including any factors other than price that are to be considered in the evaluation of tenders and the cost elements to be included in evaluating tender prices, such as transport, insurance and inspection costs, and in the case of products or services of other Parties, customs duties and other import charges, taxes and currency of payment.¹⁰⁴

Contract awards are made exclusively on terms outlined in these documents. To do otherwise would violate the core principle of transparency. If the tender or invitation does not say that the project requires environmental standards or particular respect for human rights, it would be illegitimate to later invoke those principles to judge the various bids.¹⁰⁵ This formulation leaves room for social vetting. As long as all suppliers are aware in due time, transparently, that the award will go to a supplier who has a good social track record, or that company social policies must be submitted along with the bid, then it is fair and there can be no recourse under the Challenge provisions later on.¹⁰⁶

Regardless of whether the WTO Agreement does or does not permit social vetting, no major development bank has in fact attached social conditions to their procurement practices.¹⁰⁷ Of the five major regional development banks, none derogates significantly from these four key principles – economy and efficiency, transparency and non-discrimination. The European Bank for Reconstruction and Development tends to emphasize the latter two (as a leading proponent of opening public procurement to international trade).¹⁰⁸ The Inter-American Development Bank and the North American Development Bank focus more directly on the first two principles (though all are committed to transparency, if less so to non-discrimination).¹⁰⁹ The Asian Development Bank restricts supplier eligibility to member states (diminishing the non-discrimination principle.)¹¹⁰ The African Regional Development Bank, while broadly committed to the key principles, is the only one of the five to suggest that bid evaluation may include taking

¹⁰⁴ *Ibid.*, article XII, 2 (f)-(h).

¹⁰⁵ *Ibid.*, article XII, 4 (a)-(c).

¹⁰⁶ *Ibid.*, article XX, but note that there have only been three “official” disputes taken to the WTO under these provisions in the 24 years of this Agreement’s existence, see www.wto.org/english/tratop_e/gproc_e/disput_e.htm.

¹⁰⁷ See note 69 for a news item regarding the Asian Development Bank that suggests differently.

¹⁰⁸ See the EBRD policy on procurement at www.ebrd.org/about/policies/procure/ppr.pdf. For more on the EU position on international trade and government procurement, see europa.eu.int/comm/trade/miti/gov_proc/index_en.htm.

¹⁰⁹ The IADB procurement policy is available online at www.iadb.org/ros/prm/english/docs/Policies.pdf. The NADB procurement policy is available online at www.nadb.org/Reports/Policy/eng/Procurement%20Guidelines%20Eng.pdf.

¹¹⁰ The ADB procurement policy is available online at www.adb.org/Documents/Guidelines/Procurement/default.asp?p=prcrmnt. See Article 1.03 (a): “... the proceeds of a loan can be used only for procurement of goods and works supplied from, and produced in, member countries of the Bank,...”

related training, safety and environmental benefits into consideration.¹¹¹ The Asian, African and North American Development Banks also allow affected communities to participate in the procurement process (particularly with projects that will be labour-intensive.)¹¹²

Conclusion

Public support for foreign direct investment can and does come with social conditionalities for investors. International investment agreements are the least likely to carry such conditions, as they are geared towards state obligations to create environments conducive to investment. Export credit agencies and development finance institutions often attach social conditions to their insurance and finance products as an integral part of the application and evaluation process. Such conditions are easier to formulate in these latter two institutions as the transactions involve contracts made directly with the investors, as opposed to between States. It is very common to see environmental conditionalities in this way, but core labour standards (and even job creation goals) are much more rare. Many of these institutions follow the OECD's and the World Bank's lead on environmental and social policies, and the latter focus almost exclusively on indigenous peoples, involuntary resettlement and cultural property. The World Bank is increasingly addressing forced labour and harmful child labour as well, especially since 1998.

This connection between FDI and a social agenda is likely to increase. The Free Trade Area of the Americas, if it goes ahead, will link its investment chapter to an agreement not to lower social standards to attract investment. Export credit agencies, following the OECD agreement *Common Approaches to the Environment*, may use this multilateral approach to incorporate higher social standards in overseas investment insurance products. Development finance institutions may go through a similar process, led by the World Bank at the global level. Similarly, the IFC's policy on harmful child and forced labour will likely lead to increasing pressure on DFIs to do likewise.

These models are all possibilities to overcome the structural difficulties of attaching international standards to investment. Traditionally, the treatment of investment has been a matter entirely within the sovereignty of the nation state and thus left to the regulation of the host government. While this notion remains largely true, home governments are clearly taking more responsibility for the behaviour of "their" corporations while overseas by including conditionalities where they can, particularly in overseas investment insurance and financing for development, and to a lesser degree in trade and investment agreements.

¹¹¹ See Article 3.36.2 in the African Development Bank procurement policy, available online at www.afdb.org/opportunities/procurement/pdf/Rules%20of%20procedure%20for%20procurement.pdf.

¹¹² See Article 3.13 in the ADB policy (*op.cit.*, note 112), Article 4.12 in the African Development Bank policy (*ibid.*) and Article 2.7 in the NADB policy (*op. cit.*, note 111).