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Stabilisation Clauses in Investment Agreements – a Human Rights and Development Perspective

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SUMMARY

When making a long-term investment investors need to be able to ensure a certain degree of legal and financial predictability. Since the investment is subject to the jurisdiction of the host state, investment agreements between the host state and the investor are commonly used. Such investment agreements may include stabilisation clauses, ensuring that arbitrary changes in law do not apply to the investment or that compensation will be rewarded where the changes lead to increased costs for the investor.

However, in recent years, a debate on the negative human rights impacts of stabilisation clauses has surfaced. In cases where a stabilisation clause is written to hinder changes in law also concerning human rights, it may have detrimental effects on the development of human rights in the host state. When the host state is a developing country, the issue becomes especially prominent.

In March 2011 the United Nations published the Guiding Principles on Business and Human Rights, establishing a corporate responsibility to respect human rights and human rights due diligence to be an incorporated part of businesses. Although voluntary in character, the UN Guiding Principles changes the way business and human rights are looked at. This paper is intended to analyse the impacts of the UN Guiding Principles on the future use of stabilisation clauses and provides a description of stabilisation clauses in relation to human rights in developing countries.

By looking into aspects of foreign direct investment, human rights, the business and human rights debate and the recent changes on corporate responsibilities this paper is meant to raise questions concerning the use of stabilisation clauses as a means to secure foreign investments. The different forces and interests behind the use of stabilisation clauses are considered, and focus lies upon why the use of stabilisation clauses is especially problematic where the host state is a developing country. The often-confidential character of stabilisation clauses, or rather the investment agreements in which they are included, poses a true challenge. The number of cases available for research is comparatively low, and cases of corporate-related human rights abuses are most often referred to arbitration.

Nevertheless, it becomes evident that stabilisation clauses, if drafted to include changes in human rights law, may have detrimental effects on human rights. In this sense, the inclusion of stabilisation clauses in investment contracts directly contradicts the entire concept of a corporate responsibility to respect human rights and the purpose of human rights due diligence as set forth by the UN Guiding Principles.

ABBREVIATIONS

BIT	Bilateral investment treaties
CSR	Corporate social responsibility
FDI	Foreign direct investment
FTA	Free Trade Agreements
HGA	Host Government Agreements
ICSID	International Centre for Settlement of Investment Disputes
IFC	International Finance Corporation
IIA	International investment agreements
ISDS	investor-State dispute settlement
MNC	Multinational Corporations
TNC	Transnational corporations
SGSR	United Nations Secretary General Special Representative for business and human rights
UN	United Nations
UNGC	United Nations Global Compact

1 INTRODUCTION

1.1 The Debate on Stabilisation Clauses

The debate on stabilisation clauses “began in earnest in 2003” following the publication of agreements governing a cross-border pipeline investment.¹ The agreements included stabilisation clauses claimed to undermine the ability, and even willingness, of the host states to fulfil their human rights obligations pursuant to international law.² The argument was based on the very nature of stabilisation clauses: in aiming to ensure a certain degree of legal and financial predictability stabilisation clauses may freeze or limit which laws are to be applicable to a specific project. Needless to say, the use of stabilisation clauses covering also changes in human rights law may have detrimental impacts on the human rights development in the host country.

Still, the debate surrounding stabilisation clauses is a relatively silent one. Due to the confidential nature of most investment contracts there is “no public repository of private contracts that would allow practitioners, host states, investors, civil society, and academics to view modern practice for all sectors.”³ Rather, the debate has been limited to instances where corporations more or less voluntarily have published agreements containing such clauses.⁴ When the United Nations and International Finance Corporation published a report on Stabilisation Clauses and Human Rights in 2008, therefore, it was the first one of its kind.⁵ The report not only concluded that stabilisation clauses may have negative effects on human rights unless carefully drafted and applied, but also that the risks were higher where the host state is a developing country. Indeed, it is also in these countries stabilisation clauses covering human rights are most often included in investment contracts.

Much of the debate surrounding foreign direct investment and human rights has circled around the lack of a focal point from which legal instruments can develop, and great uncertainty has surrounded to what extent corporations have a responsibility with regards to human rights. The introduction of the United Nations Guiding Principles on Business and Human Rights in March 2011 was, therefore, a significant step toward the full integration of business and human rights whereby a “common global platform for action” was established.⁶ The UN Guiding Principles not only clarifies that a corporate responsibility to respect human rights indeed does exist, but also suggests for corporations to integrate

¹ Schemberg, Andrea, *Stabilization Clauses and Human Rights – a research project conducted for the IFC and the UN Special Representative to the Secretary General on Business and Human Rights*, March 11 2008, p. 1. See below for details on the BP Oil cross-border pipeline investment.

² Ibid.

³ Ibid., see Executive Summary.

⁴ See for example Amnesty International, *Contracting out of Human Rights – The Chad-Cameroon Pipeline Project*, Amnesty International UK, September 2005.

⁵ Schemberg, Andrea, *Stabilization Clauses and Human Rights – a research project conducted for the IFC and the UN Special Representative to the Secretary General on Business and Human Rights*, March 11 2008, see Executive Summary.

⁶ United Nations, *Guiding Principles*, 21 March 2011, p. 5 (introduction).

human rights due diligence in processes for investments.⁷ It seems only reasonable to assume the implications of the UN Guiding Principles will require significant changes for the manner in which foreign direct investments are being made, including the use of stabilisation clauses.

1.2 Purpose and Research Question

The following text is intended to provide a description and analysis of stabilisation clauses in relation to human rights in developing countries. By looking into aspects of foreign direct investment, human rights, the business and human rights debate and the recent changes on corporate responsibilities this paper is meant to raise questions concerning the use of stabilisation clauses as a means to secure foreign investments. The intention is to consider the different forces and interests behind the use of stabilisation clauses and explain why they are part of state-investor contracts, but also to reflect on why the use of stabilisation clauses is especially problematic where the host state is a developing country.

The research question relates to an extensive spectrum of issues, but focuses on whether the use of stabilisation clauses in state-investor agreements poses a threat to human rights, including the right to development, when they limit the application of new laws in developing countries. Under circumstances where this indeed is the case, this paper questions whether the use of stabilisation clauses is compatible with the corporate responsibility to respect human rights and human rights due diligence as established in the UN Guiding Principles on Business and Human Rights.⁸

1.3 Approach, Materials and Methodology

The research has been conducted with the intent to provide an insight into issues relating to the above-stated question, but to entirely isolate this dilemma from others relating to foreign direct investment and human rights has, however, been neither desirable nor necessary. The approach has thus been a broad one, looking at historical factors as well as current developments to provide for an objective view on related issues.

The concepts of human development and social laws, although often referred to in materials on the topic, have not been used and will not be explained in this paper. Instead, focus remains on human rights in relation to development.

⁷ United Nations, *Guiding Principles*, 21 March 2011, p. 5 (introduction).

⁸ United Nations Human Rights Council, *Report of the Special Representative of the Secretary-General on the issue of human rights and transnational corporations and other business enterprises, John Ruggie, Guiding Principles on Business and Human Rights: Implementing the United Nations "Protect, Respect and Remedy" Framework*, UN doc. A/HRC/17/31, Human Rights Council Seventeenth Session, United Nations, 21 March 2011. Hereafter referred to as: UN, *Guiding Principles*, 21 March 2011 in footnotes and simply the UN Guiding Principles in the text.

Publications from the UN have been a major source of information on matters strictly concerning human rights and investment rights respectively, but even more so on matters concerning areas where the integration of business and human rights is investigated. Unsurprisingly, reports from the UN Secretary General Special Representative on Business and Human Rights, as well as the actual UN Guiding Principles and the UN “Protect, Respect and Remedy” Framework have been of great use. However, the UN and IFC research project on Stabilisation Clauses and Human Rights⁹ has made out the basis of investigations, along with a newly published book on Foreign Direct Investment and Human Development¹⁰. Also, the UN Global Compact Human Rights and Business Dilemmas Forum¹¹ on stabilisation clauses have been an inspiring source of information.

A majority of the materials used in this paper stem from subjective sources.¹² Also, a large portion of the materials is either written by the UN, or related to the work of the UN. However, the intention with this paper is to provide an unbiased insight into the dilemma surrounding stabilisation clauses and the debate surrounding foreign direct investment and human rights at large. A number of cases where stabilisation clauses have had detrimental effects on human rights are considered, but no case study of a specific country or corporation is provided for. This is an active choice, but also a choice that stems from the often-confidential nature of agreements where stabilisation clauses can be found. The fact that most cases on related issues are referred to international arbitration also further impedes research on the topic.

A typical legal research method has thus not been possible, but neither would it suit the topic very well. Foreign direct investment and human rights are legal topics, but also highly political ones. The legal realms are not limited to a single instrument or body of law, but rely on international, regional and domestic influences. In order to provide the reader with the means necessary to grasp the controversy surrounding the use of stabilisation clauses, therefore, a descriptive analytical method has been applied.

⁹ Schemberg, Andrea, *Stabilization Clauses and Human Rights – a research project conducted for the IFC and the UN Special Representative to the Secretary General on Business and Human Rights*, March 11 2008.

¹⁰ De Schutter, Olivier, et. al., *Foreign Direct Investment and Human Development – the Law and Economics of International Investment Agreements*, Routledge, New York, 2013.

¹¹ United Nations Global Compact, *the Human Rights and Business Dilemmas Forum, Dilemmas and Case Studies: Stabilisation Clauses*, Retrieved 2011-11-23, <http://human-rights.unglobalcompact.org/dilemmas/stabilisation-clauses/>

¹² An excellent example of this are the two Amnesty reports used in the research for this project, see for example Amnesty International, *Contracting out of Human Rights – The Chad-Cameroon Pipeline Project*, Amnesty International UK, September 2005 and Amnesty International, *Human Rights on the Line – the Baku-Tbilisi-Ceyhan Pipeline Project*, Amnesty International, London, May 2003.

1.4 Delimitations and Implications

Due to the nature of the topic a large amount of delimitations have been necessary to make. A thorough investigation of the legal framework on investment rights and human rights has been neither possible nor necessary, and only an introduction to the basics is thus provided for. This is true also for areas where business and human rights overlap, including areas such as corporate social responsibility and policies for sustainable investments. Rule of law, democracy, good governance and similar areas related to the topic are of relevance for the discussion and should be kept in mind, but have been excluded from a more thorough description and analysis. The work within the UN is described and analysed, but a complete coverage of all the work on business and human rights is by no means included in this paper. Rather, the research has been limited to work relevant to the UN Guiding Principles, stabilisation clauses as well as the corporate responsibility to respect human rights and human rights due diligence.

Although certain human rights are referred to as more at risk for the impacts of stabilisation clauses, the list is not exhaustive. Certain rights, such as the right to development and the right to access to effective remedies, are considered in more detail, but this should not be interpreted as limiting the scope of possible impacts of foreign direct investment and stabilisation clauses on human rights to these specific areas. Rather, it should be recalled that corporate activity might have an impact on virtually any human rights but that a complete coverage of this spectrum has not been possible.

Furthermore, focus lies upon the impact of foreign direct investment on human rights in developing countries only. This should not be interpreted in the sense that corporate-related human rights issues arise only in developing countries, but is due to the unique situation provided by the state-investor relationship, and the inevitable connection created between domestic, regional and international law concerning human rights and investment rights in these countries.

Moreover, the confidential nature of state-investor agreements combined with the use of arbitration for disputes concerning these agreements makes it nearly impossible to gain insight into certain aspects of stabilisation clauses. As mentioned with regard to materials above, the research is thus limited to reports and research on case law as well as state-investor agreements. Also, the debate on stabilisation clauses is a rather new one – not the least from a legal perspective – and only a limited amount of time has passed since the introduction of the corporate responsibility to respect human rights as set forth by the UN Guiding Principles in March last year. From a research perspective, this has posed a true challenge since the actual impacts and results of the recent changes on the business-human rights relationships are not yet evident.

1.5 Disposition

Following the background provided in Chapter 2, Chapter 3 considers the legal framework for international investment law and international human rights law. Special attention is being paid to definitions, actors, and basic regulation as well as how this relates to human rights and developing countries. In Chapter 4 areas where business and human rights overlap are described, looking specifically at the history underpinning the debate, the work carried out within the United Nations as well as the role and impact of the UN Guiding Principles.

Chapter 5 moves on to consider the very core of this essay: the relationship between stabilisation clauses and human rights. A few specific case studies of potential adverse human rights impacts resulting from the application of stabilisation clauses are looked at. Furthermore, how the use of stabilisation clauses in investment agreements relates to the UN Guiding Principles and the corporate responsibility to respect human rights thereby established is taken into consideration, paying special attention to human rights due diligence. Chapter 6 provides a different perspective on the topic, as well as an analysis. Finally, in Chapter 7, a few concluding statements are made.

2 BACKGROUND

2.1 Globalisation and International Investment Agreements

In the late nineteenth century a universally recognized set of principles on foreign investment had developed, and customary international law allowed foreign investors to receive the same protection of rights as nationals.¹³ Until the early twentieth century the “international consensus on those principles was quite solid...” but rather soon policies of nationalization and expropriation created a disparity as to what regulations should apply to foreign investments, combined with an increased demand from investors to secure the investments being made.¹⁴

What followed was a period of great uncertainty, and in the 1964 Sabbatiano judgement the US Federal Supreme Court expressed there are “few if any issues in international law today on which opinion seems to be so divided as the limitations on a State’s power to expropriate the property of aliens”.¹⁵ Efforts were made within the UN to establish a consensus on the matter, but progress was halted by the increase of developing countries participating in the negotiations. In the 1960’s, much due to the role of developing countries within the UN, the division on how to regulate became even larger than it had previously been despite efforts made in the opposite direction.

Meanwhile, a global market where foreign direct investment was considered a significant force grew rapidly, and States became increasingly aware to regulate their relations. As a consequence, “capital-exporting states started...to intensify a practice consisting in agreeing with host countries on protective terms for their national investors...”¹⁶ These International Investment Agreements (IIAs) were intended to create a greater legal and financial certainty for an investment, and since no multilateral agreement could be reached, IIAs – and even more so Bilateral Investment Treaties (BITs) – were essential for the further expansion of a global climate in which foreign direct investment could thrive.¹⁷

A few attempts on multinational agreements had been made, including the OECD Multilateral Investment Agreement (MAI). Its failure, however, only further demonstrated the insurmountable divisions on how to regulate foreign direct investment, and although the International Centre for the Settlement of Investment Disputes (ICSID) Convention was agreed upon in 1965 it did not “entail any substantive norms nor a regime for FDI.”¹⁸ For this very reason, IIAs and BITs dominated the latter part of the twentieth century and from the

¹³ De Schutter, Olivier, et. al., *Foreign Direct Investment and Human Development – the Law and Economics of International Investment Agreements*, Routledge, New York, 2013, p. 27.

¹⁴ *Ibid.*, p. 28. The USSR and Mexico are mentioned as especially dominant states of this time with regard to expropriation and nationalisation.

¹⁵ *Ibid.*, p. 29.

¹⁶ *Ibid.*, p. 33.

¹⁷ *Ibid.*

¹⁸ *Ibid.*, p. 34.

introduction of these types of agreements their use increased steadily until, in the 1990s, it “literally exploded”.¹⁹

As of today, IIAs are a main instrument in the regulation of foreign investment, and there are over 2,800 BITs signalling a positive attitude to foreign direct investment and the regulation thereof.²⁰ Recent years have, however, seen a decline in the use of IIAs and BITs. This can be explained by the increased use of regional trade agreements, but a more interesting cause is “the fact that IIAs are becoming increasingly controversial and politically sensitive.”²¹

2.2 A New Approach to Foreign Direct Investment

The controversy stems, in large, from the attitude surrounding foreign direct investment as such. The regulation on foreign direct investment has, until very recently, been dominated by an investor-friendly attitude where the protection of investor rights has been allowed to intrude on the sovereignty of the host state.²² However, following several incidents of corporate-related human rights abuses in the 1990s a different approach has grown strong.²³

Indeed, “the issue of business and human rights became permanently implanted on the global policy agenda in the 1990s” as a result of the expansion of private actors on the global market and the further growth of transnational activities, and the scrutiny of foreign direct investment in relation to foreign direct investment remains a strong force as of today.²⁴ A new generation of investment policies is thus emerging, where sovereignty and associated development perspectives are allowed to take place alongside investor-friendly policies.

However, whilst IIAs and BITs are increasingly scrutinized in relation to their potential human rights impacts, private contracts between the investor and the host state remain an area of concern. In 2003, the debate on the use of stabilisation clauses surfaced as Amnesty International published a report on the potential adverse human rights impacts of the inclusion of such clauses in state-investor agreements governing foreign direct investment.²⁵ Stabilisation clauses, much like IIAs and BITs, had for long been an integrated part of contracts between the investor and the host state to ensure a certain degree of stability for

¹⁹ De Schutter, Olivier, et. al., *Foreign Direct Investment and Human Development – the Law and Economics of International Investment Agreements*, Routledge, New York, 2013, p. 34.

²⁰ *Ibid.*, p. 38.

²¹ UNCTAD, *World Investment Report 2012: Toward a New Generation on Investment Policies*, New York & Geneva, 2012, see Overview.

²² De Schutter, Olivier, et. al., *Foreign Direct Investment and Human Development – the Law and Economics of International Investment Agreements*, Routledge, New York, 2013, p. 47.

²³ United Nations, *Guiding Principles*, 21 March 2011, p. 3 (introduction).

²⁴ *Ibid.*

²⁵ Schemberg, Andrea, *Stabilization Clauses and Human Rights – a research project conducted for the IFC and the UN Special Representative to the Secretary General on Business and Human Rights*, March 11 2008, p. 1.

long-term investments, but were in the report argued to pose a threat to human rights.²⁶

2.3 A Call for a Change

The incidents and surrounding discussions created a strong public demand for legislation and regulation concerning human rights and the business-sector. For corporations, terminology such as sustainability and corporate responsibility became essential for the establishment of a successful business, and in 1999 then UN Secretary General Kofi Annan called for business leaders of the world to take on the challenge of a Global Compact, incorporating labour, environment, human rights and anti-corruption in the “corporate sphere”.²⁷

In 2000, the UN General expressed the necessity of change to ensure the effects of continuing rapid globalisation and increase of foreign direct investments to be beneficial also for developing parts of the world:

We believe that the central challenge we face today is to ensure that globalization becomes a positive force for all the world's people. For while globalization offers great opportunities, at present its benefits are very unevenly shared, while its costs are unevenly distributed. We recognize that developing countries and countries with economies in transition face special difficulties in responding to this central challenge.²⁸

Not until March 2011, however, the UN Guiding Principles, following several previous attempts and years of work in the area, established a globally recognised corporate responsibility to respect human rights.²⁹ Following the adoption of the UN Guiding Principles, corporations, through human rights due diligence, are responsible to ensure they are not, directly or indirectly, contributing to any violation of human rights.³⁰ The UN Guiding Principles, although not legally binding, thereby establishes a closer connection between business and human rights than have ever previously existed.

Nevertheless, corporate related human rights abuses remain an issue, and the report on the Top 10 Business and Human Rights Issues 2013³¹ from the Institute for Human Rights and Business includes a number of issues closely related to foreign direct investment and human rights. Indeed, a voluntary

²⁶ Schemberg, Andrea, *Stabilization Clauses and Human Rights – a research project conducted for the IFC and the UN Special Representative to the Secretary General on Business and Human Rights*, March 11 2008, p. 1.

²⁷ United Nations World Economic Forum, *Secretary General Proposes Global Compact on Human Rights, Labour, Environment, in Address to World Economic Forum in Davos*, Press release SG/SM/6881, United Nations, Davos, 1 February 1999.

²⁸ United Nations General Assembly, *United Nations Millennium Declaration*, UN doc. A/RES/55/2, Adopted in New York, 18 September 2000, p. 2.

²⁹ United Nations, *Guiding Principles*, 21 March 2011.

³⁰ Ibid.

³¹ Institute for Human Rights and Business, *Top 10 Business and Human Rights Issues 2013*, 10 December 2012, retrieved 2012-12-12,

http://www.ihrb.org/top10/business_human_rights_issues/2013.html.

measure such as the UN Guiding Principles does not seem enough to encounter the problem.

2.4 Stabilisation Clauses

The use of stabilisation clauses began in the 1960s and 1970s following “a wave of nationalizations of foreign investments in oil and mining”. Today, stabilisation clauses are a well-established risk-mitigation tool used on a global level in all types of industries used to “deal with the risk of arbitrary or discriminatory legislation against the investor, nationalization, or expropriation, but they also are likely to guard against physical or creeping expropriation by the host state...”³².

The critique put forward by civil society groups in 2003 especially concerned the use of stabilisation clauses claimed to “undermine the willingness and ability” of the host states to fulfil obligations under international human rights law.³³ In ensuring the legal parameters of an investment stabilisation clauses were criticised to encumber the development of human rights within the host state - due to the limitations they imposed on the implementation of new laws as well as the compensation required to be paid by the host state to the investor for additional costs resulting from the implementation of new laws.³⁴

As part of the work behind the UN Framework and the UN Guiding Principles the SGSR, having noticed greatly differing views amongst consulted stakeholders on the issue, requested a report on the use of stabilisation clauses in foreign direct investment. In a joint effort between the UN SGSR and the International Finance Corporation (IFC) a report on Stabilisation Clauses and Human Rights was published in March 2008.³⁵ The report was the first empirical study of its kind and a unique contribution to the understandings of an otherwise rarely discussed topic.

The study found that “stabilization clauses are sometimes drafted so as to insulate investors from having to implement new...laws, or to provide investors with an opportunity to be compensated for compliance with such laws”, including human rights.³⁶ It was also concluded that the use of stabilisation clauses was especially problematic when the host state was a developing country, and that the risk for detrimental effects human rights standards in these countries was significantly larger.³⁷ Despite these findings, stabilisation clauses continue to be a component of a large amount of state-investor agreements – especially for foreign direct investments in developing countries concerning

³² Schemberg, Andrea, *Stabilization Clauses and Human Rights – a research project conducted for the IFC and the UN Special Representative to the Secretary General on Business and Human Rights*, March 11 2008, p. 4.

³³ *Ibid.*, p. 1.

³⁴ *Ibid.*

³⁵ *Ibid.*

³⁶ *Ibid.*

³⁷ *Ibid.*, p. 10.

changes in legislation concerning human rights.³⁸

³⁸ Ibid., p. 4.

3 THE LEGAL FRAMEWORK

This essay is intended not to provide for a detailed description on the international law on foreign direct investment, nor to consider international human rights law in detail. However, an introduction to the legal framework is necessary.

3.1 The Legal Framework Governing Foreign Direct Investment

In the following section a definition of foreign direct investment will be provided. The actors typically involved will be looked at, and furthermore the international law on foreign direct investment and the instruments used will be considered. Last, foreign direct investment and stabilisation clauses will be described, followed by a section on why developing countries are of certain interest in relation to foreign direct investment.

3.1.1 Defining Foreign Investment

The OECD defines foreign direct investment as “the objective of establishing a lasting interest by a resident enterprise in one economy...in an enterprise...that is resident in an economy other than that of the direct investor”, requiring a long-lasting relationship as well as significant influence on the management of the enterprise.³⁹ For the purpose of this essay this definition is used. However, a number of definitions are available and may contribute to the understanding of foreign direct investment.

Several definitions are provided for also in treaties concerning international investment. Countries with a strong position in exporting capital, such as the United States, have promoted a broad definition of foreign investment in treaty-making processes, often supported by the opinions of arbitral tribunals.⁴⁰ Such definitions are, however, influenced by the purpose of the treaty or, in the case of arbitral tribunals, limited to the definition provided for in the treaty. A common technique to define foreign investment is to look to “distinct criteria such as commitment of assets into a project with the object of profit and permanence and with a view to the risks arising from legal, political and economic changes”.⁴¹ However, foreign investment can also be defined as “the transfer of tangible or intangible assets from one country to another for the purpose of their use in that country to generate wealth under total or partial control of the owner of the assets”.⁴² Physical property, such as equipment or a bought manufacturing plant, are thus considered foreign investments.⁴³

Foreign investment should not be confused, however, with portfolio investment. Portfolio investment concerns the “movement of money for the purpose of buying shares in a company formed or functioning in another country” or “other

³⁹ OECD, *OECD Benchmark Definition of Foreign Direct Investment*, p. 48.

⁴⁰ M. Sornarajah, *The International Law on Foreign Investment*, p. 10.

⁴¹ *Ibid.*, p. 10.

⁴² *Ibid.*, p. 8.

⁴³ *Ibid.*, p. 8.

security instruments through which capital is raised for ventures”.⁴⁴ In essence, the main difference is that foreign direct investment is done with the intention to exercise control over the enterprise.⁴⁵

The distinction between foreign direct investment and portfolio investment is necessary due to how the two types of investments are dealt with under international law. Foreign direct investment, in bringing assets to a host-state which otherwise had been beneficial to the economy of the home state, is considered necessary to protect whereas portfolio investment, which can be made on stock exchanges globally, are not.⁴⁶ Although opinions differ, it appears as if the ruling saying is that portfolio investments are not protected under international customary law in the same sense as foreign direct investments, unless specifically expressed to be in treaties. The distinction between the two allows for an insight into the general view of foreign investment as an important issue in international law to be protected and cared for to a larger extent than other forms of investment.

3.1.2 The Actors

To grasp the dilemma surrounding stabilisation clauses, a definition with regards to the actors typically involved is necessary. Here, the host- and the home state are of significance.

The host state is understood to be the recipient of the investment being made, whilst the home state is the state in which the investing corporation is registered.⁴⁷ Foreign investment, in addition to the overall contribution to development of international trade, is considered to contribute to the economies of both the host- and the home state and is often an important source of capital for both.⁴⁸ Furthermore, although the investor can be a natural person, significant for the topic at hand is when the investor is a corporation operating in several jurisdictions.⁴⁹

When operating in several countries most corporations adopt a network-based model in which several corporate entities work within and across jurisdictions in a hierarchical structure. This provides economic efficiency, but poses problems for the corporations in controlling their global value chains and as to which national legal system is to be applied.⁵⁰

3.1.3 Regulating Foreign Direct Investment

The very nature of corporations operating across borders poses “a regulatory challenge to the international legal system”.⁵¹ Economies worldwide have

⁴⁴M. Sornarajah, *The International Law on Foreign Investment*, p. 8.

⁴⁵ UNCTAD, *Investment and Enterprise – FDI Statistics – Definitions and sources*, Retrieved 2012-11-20, [http://unctad.org/en/Pages/DIAE/Foreign-Direct-Investment-\(FDI\).aspx](http://unctad.org/en/Pages/DIAE/Foreign-Direct-Investment-(FDI).aspx).

⁴⁶ M. Sornarajah, *The International Law on Foreign Investment*, p. 9.

⁴⁷ OECD, *OECD Benchmark Definition of Foreign Direct Investment*, p. 14.

⁴⁸ Ibid.

⁴⁹ Such corporate actors are often referred to as transnational or multinational corporations.

⁵⁰ Ruggie, John Gerard, *Business and Human Rights: The evolving international agenda*, p. 7.

⁵¹ Ibid.

become increasingly integrated, creating a need for functioning international regulation on foreign investment for all actors involved. If regulated properly, foreign direct investment may be highly beneficial to all actors involved, as it “assists host countries in developing local enterprises, promotes international trade through access to markets and contributes to the transfer of technology and know-how” and, indirectly, also have “an impact on the development of labour and financial markets, and influences other aspects of economic performance through its other spill-over effects”.⁵² Indeed, it is important foreign direct investment is regulated accordingly.

When corporations operate in the hierarchical structure mentioned above the parent company and its subsidiaries are considered separate legal entities. Wrongdoings carried out by the subsidiaries do not result in legal liability for the parent company following to the doctrine of limited liability, unless a close operational control can be established as to the subsidiary merely acting as an agent.⁵³ The subsidiaries are legally responsible under the national laws of the country in which they operate, but the main issue with transnational corporations has been that they as such are not governed under international law.⁵⁴ As we shall see below this has, at least to a certain extent, changed. Fact remains, however, that foreign direct investment is regulated not by a single body of law but rather several types of instruments.

These will be discussed below. First, however, it must be noted that they all have in common to have been created in an investor-friendly atmosphere with a primary intent to protect the investor from arbitrary changes in law posing a potential threat to the investment.⁵⁵ In addition to the friendly attitude toward investment most regulatory bodies are permeated with the main purpose to mitigate the risk involved with a long-term investment. Since “...investments are subject to a host government's jurisdiction, there is potential for arbitrary state interference at a time when the balance of negotiating power shifts”, and incidents of expropriation – direct or indirect – have caused corporations to take precautionary steps in ensuring a reliable ground for the investment.⁵⁶

3.1.3.1 International Investment Agreements and Bilateral Investment Treaties

With these intentions, a large body of international law on foreign investments has developed, and there a several means by which a corporation can secure an investment. One option is to rely on the protection provided through International Investment Agreements (IIAs). IIAs are treaties entered into by states, covering foreign directs investments and in certain cases also portfolio investments. IIAs are intended to clarify standards on foreign direct investments, and in being part to such an agreement the home and host states agree to adhere to these standards. Often, a further intention with the conclusion of IIAs is to

⁵² OECD, *OECD Benchmark Definition of Foreign Direct Investment*, p. 20.

⁵³ Ruggie, John Gerard, *Business and Human Rights: The evolving international agenda*, p. 7.

⁵⁴ *Ibid.*, p. 8.

⁵⁵ United Nations Global Compact, *the Human Rights and Business Dilemmas Forum, Dilemmas and Case Studies: Stabilisation Clauses*, Retrieved 2011-11-23, <http://human-rights.unglobalcompact.org/dilemmas/stabilisation-clauses/>.

⁵⁶ *Ibid.*

specify dispute-resolution procedures and more specifically to make international arbitration rather than domestic courts the primary route for such dispute-resolutions.

Bilateral Investment Treaties (BITs) fulfil the same function but are, as the name suggests, entered into by two parties only. Both IIAs and BITs typically focus on providing protection for foreign direct investments, and address traditional internationally recognized standards such as fair and equitable treatment, national treatment, most-favoured nation treatment and full protection and security. Corporations also have an option of buying political risk insurance covering an investment against risks of expropriation, direct or indirect, as a result of arbitrary changes in law.⁵⁷

3.1.3.2 State-investor Agreements

Yet another option is for a corporation to regulate the terms of the investment in a contract entered directly into with the host state. Agreements between the host state and the investor are named in several different ways, but will here be referred to as state-investor agreements in order to clarify the nature of the agreement.⁵⁸ State-investor agreements often include stabilisation clauses as a means to secure the investment.⁵⁹ Following the topic for this paper, a further description of stabilisation clauses is provided for below. Further on, the relationship between stabilisation clauses and human rights will also be discussed.

3.1.4 Foreign Direct Investment and Stabilisation Clauses

3.1.4.1 Understanding Stabilisation Clauses

Stabilisation clauses are, as the name suggests, intended to ensure a certain degree of stability for the investment being made and are used in investment contracts to limit the risk-taking involved.⁶⁰ Although stabilisation clauses are by no means included in all investment contracts, they are common in long-term investment contracts in, for example, contracts concerning public infrastructure or in the extractive industries, and used on a worldwide basis for foreign direct investments.⁶¹

⁵⁷ United Nations Global Compact, *the Human Rights and Business Dilemmas Forum, Dilemmas and Case Studies: Stabilisation Clauses*, Retrieved 2011-11-23, <http://human-rights.unglobalcompact.org/dilemmas/stabilisation-clauses/>.

⁵⁸ Such agreements are also being referred to as "host government agreements" or "concession agreements", to mention a few, and the naming often depend on which type of industry the agreement concerns. For example, "concession agreement" is a common naming of an agreement in the extractive industry sector

⁵⁹ United Nations Global Compact, *the Human Rights and Business Dilemmas Forum, Dilemmas and Case Studies: Stabilisation Clauses*, Retrieved 2011-11-23, <http://human-rights.unglobalcompact.org/dilemmas/stabilisation-clauses/>.

⁶⁰ Schemberg, Andrea, *Stabilization Clauses and Human Rights – a research project conducted for the IFC and the UN Special Representative to the Secretary General on Business and Human Rights*, March 11 2008, p. 1.

⁶¹ *Ibid.*, p. 4.

For the purpose of this essay, the term stabilization clause will be considered “the contractual clauses in private contracts between investors and host states that address the issue of changes in law in the host state during the life the project”.⁶² The use of stabilisation clauses in state agreements as discussed above is, therefore, not considered further.

The “changes in law” intended to be regulated through a stabilisation clause generally refer to, to mention a few, “arbitrary or discriminatory legislation against the investor, nationalization, or expropriation...physical or creeping expropriation by the host state, nullification of the contract pursuant to national law, or more specific fiscal issues...” but may also be included in a contract with the intention to avoid future costs related to, for example, improved social or environmental legislation in the host state.⁶³

Because investments are subject to the laws of the host states there is a risk for arbitrary changes in domestic laws that may impact the investment in such a way it can be considered to amount to expropriation. Such incidents of expropriations have occurred on a global level, and caused investors to mitigate the risk of expropriation or ensure compensation for it.⁶⁴ Today, also indirect forms of expropriations are protected through investment contracts and stabilisation clauses where the value of the investment is significantly reduced, or the new laws are imposed only with the intention to increase the share of project profits for the host state.⁶⁵

In order to grasp the issue of stabilisation clauses and why they are included in investment contracts one must remember the different interests of the parties involved in the making of an investment contract. Many individuals representing investors believe that “foreign investment would not be possible in many parts of the world without stabilisation clauses”, and that clauses ensuring a certain degree of legal as well as financial stability are necessary to ensure predictability in relation to raised costs – even in cases where the increase in costs is a result of the implementation of regulation concerning improved human rights.⁶⁶

From an investor point-of-view stabilisation clauses are especially important when investing in a market that can be considered more unstable than others, such as emerging markets. Also many lenders require stabilisation clauses and consider them a necessary means to ensure that the commercial security of a project is not damaged through amendments in legislation by the host state, or

⁶² Schemberg, Andrea, *Stabilization Clauses and Human Rights – a research project conducted for the IFC and the UN Special Representative to the Secretary General on Business and Human Rights*, March 11 2008, p. 4.

⁶³ *Ibid.*, p. 4

⁶⁴ United Nations Global Compact, *the Human Rights and Business Dilemmas Forum, Dilemmas and Case Studies: Stabilisation Clauses*, United Nations, Retrieved 2011-11-23, <http://human-rights.unglobalcompact.org/dilemmas/stabilisation-clauses/>.

⁶⁵ *Ibid.*

⁶⁶ Schemberg, Andrea, *Stabilization Clauses and Human Rights – a research project conducted for the IFC and the UN Special Representative to the Secretary General on Business and Human Rights*, March 11 2008, p. 5.

that the repayment of the loan is made impossible by raised costs due to such amendments.⁶⁷ The host state, on the contrary, “see stabilization clauses as a way to encourage inward investment and provide a favourable investment climate”, and therefore tend to accept sweeping stabilization clauses – including terms that may be to the detriment of the host state and in favour of the investor.⁶⁸

According to those interviewed for the UN and IFC study of stabilisation clauses and human rights, there are three ways in which stabilisation clauses can be used; they are a part of the investment agreement “and therefore form a part of the ground rules upon which the investor operates the project”; they are used as a “reference point for informal dealings and formal negotiations between the parties to the agreement”; and they are used as a “formal protection of rights if a dispute should arise”.⁶⁹

3.1.4.2 Types of Stabilisation Clauses

Stabilization clauses may be divided into three categories, each intended to protect the investor in a certain way. The three types: freezing clauses, economic equilibrium clauses and hybrid clauses will be described below. One should note that the types of stabilisation clauses are not mutually exclusive, and that different forms of these clauses may be incorporated in an investment contract to fulfil several purposes. However, the descriptions are intended only to provide the reader with a brief insight into the basic legal realms of stabilization clauses, so as to prepare for the discussion on stabilization clauses and human rights below.

Freezing clauses are “designed to make new laws inapplicable to the investment” and “aim to freeze the law of the host state with respect to the investment project”.⁷⁰ There are two types of freezing clauses: full and limited freezing clauses. Whilst full freezing clauses “purport to freeze both fiscal and nonfiscal issues” limited freezing clauses “aim to protect the investor from a more limited set of legislative actions”.⁷¹ Some claim freezing clauses are no longer in use, and several states have prohibited the use of such clauses under domestic law making economic equilibrium clauses more commonly used in foreign direct investment contracts.⁷² In some countries, however, freezing clauses are still in use.

Economic equilibrium clauses allow for new laws to be applied to an investment but ensure the investor, in complying with the new laws, will be compensated by the host state for any additional costs it may lead to. Economic equilibrium clauses thereby intend to “maintain the economic equilibrium of the investment

⁶⁷ Schemberg, Andrea, *Stabilization Clauses and Human Rights – a research project conducted for the IFC and the UN Special Representative to the Secretary General on Business and Human Rights*, March 11 2008, p. 5.

⁶⁸ *Ibid.*

⁶⁹ *Ibid.*, p. 35.

⁷⁰ *Ibid.*, p. 5.

⁷¹ *Ibid.*, p. 6.

⁷² *Ibid.*, p. 7.

project” rather than freeze the law applicable to it.⁷³ Also economic equilibrium clauses can be divided into two categories: full economic equilibrium clauses and limited economic equilibrium clauses. Full economic equilibrium clauses “protect against the implications of all changes of law” and may require the host state to provide the investor full compensation for any economic change associated with changes in law.⁷⁴ Limited economic equilibrium clauses, on the other hand, are limited to certain types of regulatory changes (or rather, exclude certain types of regulatory changes or areas of law from the right of compensation) and may require the investor to show a certain amount of financial loss to claim a right to compensation.⁷⁵

The third and last type of stabilization clauses is hybrid clauses. Such clauses combine the other two types of clauses. Similar to economic equilibrium clauses, “hybrids do not make investors automatically exempt from new laws...” but, like freezing clauses, “explicitly include the granting of exemptions from laws as one method to ensure that the investor is not financially impacted by new laws.”⁷⁶ Much similar to the other two categories of stabilization clauses, hybrid clauses can be either full or limited hybrid clauses. A full hybrid clause carries the function to “protect against the financial implications of all changes of law, by requiring compensation or adjustments to the deal, including exemptions from new laws, to compensate the investor when any changes occur”. A limited hybrid clause is intended to function in the same manner, with the difference that it does not cover *all* changes in law or only does so in cases where a certain financial loss is incurred, and allows for compensation only for those changes explicitly covered in the contract.⁷⁷

3.1.5 Foreign Direct Investment in Developing Countries

Before moving on to the next section, a few words on why developing countries are of special interest in discussing foreign direct investment, stabilisation clauses and human rights should be made.

Transnational corporations are strong economic forces and the “most visible embodiment” of globalization.⁷⁸ In general, corporations and governments alike have maintained an investor-friendly attitude to promote the expansion of a global market. The financial crisis in 2008 and 2009, and the slow growth and financial difficulties that followed and are still evident, have not changed this. Rather, it has resulted in the opposite as “countries worldwide continued to liberalize and promote foreign investment as a means to support economic

⁷³ Schemberg, Andrea, *Stabilization Clauses and Human Rights – a research project conducted for the IFC and the UN Special Representative to the Secretary General on Business and Human Rights*, March 11 2008, p. 7.

⁷⁴ *Ibid.*, p. 7.

⁷⁵ *Ibid.*, p. 8.

⁷⁶ *Ibid.*, p. 8.

⁷⁷ *Ibid.*, p. 9.

⁷⁸ Ruggie, John Gerard, *Business and Human Rights: The evolving international agenda*, p. 6.

growth and development”.⁷⁹ Meanwhile, “the percentage of more restrictive policy measures showed a significant decrease” during the same period.⁸⁰

As has been briefly noted, and will be discussed further later on, foreign direct investment is an important source of capital and may contribute to development for the host as well as the home state.⁸¹ A host state may be a developed or a developing country, but the effects, both positive and negative, may take different shapes depending on the economy in which the investment takes place. Stabilisation clauses are an excellent example of this, as possible negative effects on development are “exacerbated in developing countries, where the need is for rapid legislative development and implementation—not for obstacles to the application of new laws”.⁸² In attracting foreign investment, governments of developing countries are typically considered weaker in negotiating the terms of the investment. The following quote presents the underlying issue:

Each legally distinct corporate entity is subject to the laws of the countries in which it is based and operates. Yet States, particularly some developing countries, may lack the institutional capacity to enforce national laws and regulations against transnational firms doing business in their territory even when the will is there, or they may feel constrained from doing so by having to compete internationally for investment.⁸³

Specific examples of such situations and a further discussion on this matter will be provided below, but one must not forget that also for the investor there is a certain challenge involved when it comes to developing countries. Although foreign direct investment poses a challenge for all parties involved, in balancing the different interests and risk-takings, it remains that “developing countries are seen by investors as offering less certainty in this respect”.⁸⁴ The risk for arbitrary changes in domestic law is simply higher in a developing country, and requires extensive precautionary steps to be taken.⁸⁵

Foreign direct investment remains the “largest component of international capital flows into developing countries” and the impacts – whether negative or positive - cannot be neglected.⁸⁶ With regards to human rights, including the right to development, no consensus has been reached. A majority seem to be of the opinion that foreign direct investment is necessary for development, and thus also the promotion of human rights. Others, however, argue the opposite.

⁷⁹ UNCTAD, *World Investment Report: Towards a New Generation of Investment Policies*, New York and Geneva, 2012, p. 21.

⁸⁰ *Ibid.*

⁸¹ OECD, *OECD Benchmark Definition of Foreign Direct Investment*, p. 14.

⁸² Schemberg, Andrea, *Stabilization Clauses and Human Rights – a research project conducted for the IFC and the UN Special Representative to the Secretary General on Business and Human Rights*, March 11 2008, p. 10.

⁸³ UN, “*Protect, Respect and Remedy*” Framework, 7 April 2008, p. 6.

⁸⁴ United Nations Global Compact, *the Human Rights and Business Dilemmas Forum, Dilemmas and Case Studies: Stabilisation Clauses*, Retrieved 2011-11-23, <http://human-rights.unglobalcompact.org/dilemmas/stabilisation-clauses/>.

⁸⁵ *Ibid.*

⁸⁶ De Schutter, Olivier, et. al., *Foreign Direct Investment and Human Development – the Law and Economics of International Investment Agreements*, Routledge, New York, 2013, p. 76.

Several factors must be considered in determining the impacts of foreign direct investment, and “depends, to a large extent, on the quality of governance in the host state.”⁸⁷

Either way, foreign direct investment in developing countries is continuing to increase rapidly, and in 2011 the OECD noted that in developing countries “multinational enterprises have diversified beyond primary production and extractive industries into manufacturing, assembly, domestic market development and services”.⁸⁸ This change in nature of foreign direct investment has “strengthened and deepened the ties that join the countries and regions of the world” but also presents a challenge to the international community to amend the regulation governing foreign direct investment accordingly.⁸⁹

3.2 The Legal Framework of Human Rights

This section is intended to provide an insight into the framework for international human rights law, looking especially at the UN Charter, the UDHR, the International Bill of Human Rights as well as the Millennium Development Goals. Special attention will be paid to the right to development, but also other specific human rights will be considered in more detail.

3.2.1 Understanding Human Rights

The very core of human rights relies on the principles of being universal and inalienable, interdependent and indivisible as well as equal and non-discriminatory.⁹⁰ This means human rights are inherent to all human beings whatever nationality, place of residence, national or ethnic origin, sex, colour, language, religion, or other status a person may hold, and that in being inalienable, human rights may not be interfered except under certain circumstances according to due process.⁹¹ Furthermore, human rights are “indivisible, interrelated and interdependent” - whether they are civil, political, economic, social, cultural or collective rights – and the principles of non-discrimination and equality permeates all areas of international human rights law.⁹²

International human rights law lays out obligations and duties – including positive actions – for states to contribute to the development of human rights and respect, protect and fulfil human rights.⁹³ Meanwhile, “at the individual level,

⁸⁷ De Schutter, Olivier, et. al., *Foreign Direct Investment and Human Development – the Law and Economics of International Investment Agreements*, Routledge, New York, 2013, p. 157.

⁸⁸ OECD, *OECD Guidelines for Multinational Enterprises*, OECD Publishing, 25 May 2011, p. 14.

⁸⁹ Ibid.

⁹⁰ Office of the High Commissioner for Human Rights, *Your Human Rights – What are human rights*, United Nations, Retrieved 2012-11-23, <http://www.ohchr.org/EN/ProfessionalInterest/Pages/InternationalLaw.aspx>.

⁹¹ Ibid.

⁹² Ibid.

⁹³ Ibid.

while we are entitled to our human rights, we should also respect the human rights of others".⁹⁴

3.2.2 Regulating Human Rights

International human rights are regulated through a number of instruments, including the UN Charter, the UDHR and the International Bill of Human Rights. In 1945 the Charter of the United Nations⁹⁵ was adopted, referring to the promotion and protection of human rights and fundamental freedoms as one of the main objectives.⁹⁶ Whilst lacking a catalogue of human rights, the Economic and Social Council were assigned to create a Commission with the specific task of creating such a catalogue.⁹⁷

In 1946 the Commission on Human Rights – since 2006 replaced by the Human Rights Council – was thus formed, and in 1948 human rights became a permanent topic on the agenda of the post-war international community as the UN, following the work of the Commission on Human Rights, adopted the Universal Declaration of Human Rights.⁹⁸ For the first time in history “basic civil, political, economic, social, and cultural rights that all human beings should enjoy” were spelled out, making human rights a universally protected area of law.⁹⁹ The UDHR was implemented through binding international treaties, open to ratification by the member states.¹⁰⁰

Since 1945 an extensive body of international human rights law has developed, and whilst treaties and customary law form the “backbone”, guidelines, declarations and principles contribute to its “understanding, implementation and development”.¹⁰¹ The UDHR was an important step in the development of international human rights, and is considered to set out fundamental norms to be accepted and implemented globally, and - together with the International Covenant on Civil and Political Rights as well as the International Covenant on

⁹⁴ Ibid.

⁹⁵ United Nations, *Charter of the United Nations and the Statute of the International Court of Justice*, signed on 26 June 1945, San Francisco, entered into force 24 October 1945. Hereafter referred to as the UN Charter.

⁹⁶ De Shutter, Olivier, *International Human Rights Law: Cases, Materials, Commentary*, Cambridge University Press, 2010, p. 12.

⁹⁷ Ibid., p. 14.

⁹⁸ United Nations, *Universal Declaration of Human Rights*, Paris, 10 December 1948, hereafter referred to as the UDHR. See also De Shutter, Olivier, *International Human Rights Law: Cases, Materials, Commentary*, Cambridge University Press, 2010, p. 15.

⁹⁹ Office of the High Commissioner for Human Rights, *Your Human Rights*, United Nations, Retrieved 2012-11-23, <http://www.ohchr.org/EN/ProfessionalInterest/Pages/InternationalLaw.aspx>. See also De Shutter, Olivier, *International Human Rights Law: Cases, Materials, Commentary*, Cambridge University Press, 2010, p. 49.

¹⁰⁰ De Shutter, Olivier, *International Human Rights Law: Cases, Materials, Commentary*, Cambridge University Press, 2010, p. 16.

¹⁰¹ Office of the High Commissioner for Human Rights, *Your Human Rights – International Human Rights Law*, United Nations, Retrieved 2012-11-23, <http://www.ohchr.org/EN/ProfessionalInterest/Pages/InternationalLaw.aspx>.

Economic, Social and Cultural Rights - the UDHR forms the International Bill of Human Rights.¹⁰²

3.2.3 Human Rights at Risk

Although foreign direct investment may affect essentially any established human right, there are certain rights that are at a larger risk of being invoked where foreign direct investment is carried out in a developing country. These include the following; the Right to Adequate Food; The Right to Water; the Right to Health, mostly in relation to the challenging of environmental impacts of an investment; and basic labour rights including the Right to Work, the Right to Adequate Standard of Living as well as the Right to Safe and Healthy Working Conditions.¹⁰³ In ensuring compliance and fulfilment of these rights procedural safeguards are important, including the Right to Self-determination, the Right to Information, the Right to Access to Effective Remedies and, at last, the Right to Development.¹⁰⁴

3.2.3.1 The Right to Development

In 1986 the UN adopted the Declaration on the Right to Development¹⁰⁵ defining the Right to Development in Article 1 as follows:

1. The right to development is an inalienable human right by virtue of which every human person and all peoples are entitled to participate in, contribute to, and enjoy economic, social, cultural and political development, in which all human rights and fundamental freedoms can be fully realized.
2. The human right to development also implies the full realization of the right of peoples to self-determination, which includes, subject to the relevant provisions of both International Covenants on Human Rights, the exercise of their inalienable right to full sovereignty over all their natural wealth and resources.¹⁰⁶

The right to development is, thereby, an inalienable human right like any other, entitling all persons not only to the right to contribute to, participate in and enjoy the right to development but also establishing sovereignty over natural resources and self-determination.¹⁰⁷ The Declaration on the Right to Development is rooted in the UN Charter, the UDHR and the two Covenants just mentioned.¹⁰⁸

¹⁰² Ibid.

¹⁰³ De Schutter, Olivier, et. al., *Foreign Direct Investment and Human Development – the Law and Economics of International Investment Agreements*, Routledge, New York, 2013, p. 164-165.

¹⁰⁴ Ibid.

¹⁰⁵ United Nations General Assembly, *Declaration on the Right to Development*, adopted through UN doc. A/RES/41/128, United Nations General Assembly 97th plenary meeting, United Nations, 4 December 1986.

¹⁰⁶ Ibid., Art. 1.

¹⁰⁷ See also: Office of the High Commissioner for Human Rights, *Development – Right to Development*, United Nations, Retrieved 2012-11-26, <http://www.ohchr.org/EN/Issues/Development/Pages/Backgroundrtd.aspx>.

¹⁰⁸ United Nations General Assembly, *Declaration on the Right to Development*, adopted through UN doc. A/RES/41/128, United Nations General Assembly 97th plenary meeting, United Nations, 4 December 1986, see p. 1. The two covenants are the International Covenant on Civil and Political Rights and the International Covenant on Economic, Social and Cultural Rights.

In recognizing the right to development, the UN especially points to the aim of the UN Charter for all member states to “achieve international co-operation in solving international problems...and in promoting and encouraging respect for human rights and for fundamental freedoms for all...”¹⁰⁹. Also the UDHR came to play a significant role in shaping the right to development as it strongly promotes “social progress and better standards of life...recognizes the right to non-discrimination, the right to participate in public affairs and the right to an adequate standard of living”, but furthermore attaches significance to “everyone’s entitlement to a social and international order in which the rights and freedoms set forth...can be fully realized”.¹¹⁰

The significance and need of development as a fundamental human right and freedom was also recognized in the Declaration on the Right to Development:

...development is a comprehensive economic, social, cultural and political process, which aims at the constant improvement of the well-being of the entire population and of all individuals on the basis of their active, free and meaningful participation in development and in the fair distribution of benefits resulting therefrom...¹¹¹

The human person is recognized as the central subject, active participant and beneficiary of the right to development.¹¹² The Declaration on the Right to Development states that the responsibility for development lies with all human beings on an individual and collective level, but that states have a primary responsibility and “the right and the duty to formulate appropriate national development policies” to promote development.¹¹³ At a national level, states are thus obliged to undertake measures to promote development.¹¹⁴

Whilst this puts extensive pressure on the national governments, the Declaration on the Right to Development requires action to be taken at the international level as well. In doing so, states are required to “formulate international development policies with a view to facilitating the full realization of the right to development”.¹¹⁵ Also, states “have a duty to co-operate with each other in ensuring development and eliminating obstacles to development...to promote a new international economic order based on sovereign equality, interdependence, mutual interest and co-operation...”¹¹⁶. Both domestic and international action is thus called upon, and the right to development should be acknowledged despite

¹⁰⁹ Ibid., p. 1. See also UN Charter art. 1(3).

¹¹⁰ Office of the High Commissioner for Human Rights, *Development – Right to Development*, United Nations, Retrieved 2012-11-26, <http://www.ohchr.org/EN/Issues/Development/Pages/Backgroundrtd.aspx>.

¹¹¹ United Nations General Assembly, *Declaration on the Right to Development*, adopted through UN doc. A/RES/41/128, United Nations General Assembly 97th plenary meeting, United Nations, 4 December 1986, p. 1.

¹¹² Ibid., Art. 2(1).

¹¹³ Ibid., Art. 2(2), Art. 2(3) and Art. 3(1).

¹¹⁴ Ibid., Art. 8(1).

¹¹⁵ Ibid., Art 4(1).

¹¹⁶ Ibid., Art. 3(3).

the level of development in a country. However, the Declaration on the Right to Development recognizes the need for special attention being paid to those countries which have reached a lower degree of development, and calls for international co-operation to promote more rapid development in these cases.¹¹⁷

For this context, the most significant aspect of the right to development and the obligations thereby imposed is “the requirement that the revenues from projects that are conducted in the name of development are used for the benefit of the local population, and that the communities affected by the project participate in shaping it.”¹¹⁸ The conclusion can be drawn from the close connection between the right to development and Millennium Development Goal eight.

3.2.3.2 Millennium Development Goal Number Eight

In 2000 the UN General Assembly adopted the Millennium Declaration¹¹⁹, and established eight goals for development. These eight include; to eradicate extreme poverty and hunger; to achieve universal primary education; to promote gender equality and empower women; to reduce child mortality; to improve maternal health; to combat HIV/AIDS, malaria and other diseases; to ensure environmental sustainability and to develop a global partnership for development.¹²⁰ The eight goals came to be referred to as the Millennium Development Goals and are to be reached by 2015.

The eighth goal – to develop a global partnership for development – is of relevance in discussing foreign direct investment. The eighth goal consists of several sub-goals, amongst which the further development of an open, rule-based, predictable, non-discriminatory trading and financial system is especially worth mentioning.¹²¹ This is especially true today as net aid disbursements in 2011 amounted to \$133.5 billion (0.31 per cent of the combined national income of developed countries), showing a 2.7 per cent drop since 2010 and remaining a far distance from the UN target of 0.7 per cent of the combined national income of developed countries going to net aid disbursements.¹²² UN Secretary General Ban Ki-Moon states that in reaching all of the eight goals set forth in 2000, “much depends on the fulfilment of MDG-8—the global partnership for development. The current economic crises besetting much of the developed world must not be allowed to decelerate or reverse the progress that has been made.”¹²³

The Millennium Development Goals must therefore not be forgotten when discussing foreign direct investment and human rights in developing countries,

¹¹⁷ Ibid., Art. 4(2).

¹¹⁸ De Schutter, Olivier, et. al., *Foreign Direct Investment and Human Development – the Law and Economics of International Investment Agreements*, Routledge, New York, 2013, p. 168.

¹¹⁹ United Nations General Assembly, *UN Millennium Declaration*, UN doc. A/RES/55/2, Adopted in New York, 18 September 2000. Hereafter referred to as the UN Millennium Declaration.

¹²⁰ Ibid. See also: UNDP, *The Millennium Development Goals*, Retrieved 2012-11-26, <http://www.undp.org/content/undp/en/home/mdgoverview.html>.

¹²¹ United Nations, *Millennium Development Goals – Global Partnership*, Retrieved 2012-11-26, <http://www.un.org/millenniumgoals/global.shtml>. See goal 8.A.

¹²² United Nations, *The Millennium Development Goals Report 2012*, New York, 2012, p. 60.

¹²³ Ibid., p. 3.

and although they do not constitute legal instruments they are important forces in the current debate on business and human rights. Furthermore, the Working Group on the Right to Development has expressed that the fulfilment of the Millennium Development Goals is dependent on the impact of the right to development on foreign direct investment. They state that the right to development:

...implies that foreign direct investment...should contribute to local and national development...The principles underlying the right to development...further imply that all parties involved...have responsibilities to ensure that profit considerations do not result in crowding out of human rights protection. The impact of FDI should, therefore, be taken into account when evaluating progress in Goal 8...¹²⁴

With regard to the use of stabilisation clauses in state-investor agreements, and the corporate responsibility to respect human rights imposed by the UN Guiding Principles, this becomes especially interesting.

3.2.3.3 The International Covenant on Economic, Social and Cultural Rights

The close relationship between the right to development, Millennium Development Goal number eight and foreign direct investment is further established in the International Covenant on Economic, Social and Cultural Rights.¹²⁵ Art. 2(1) of the Covenant calls for states to “ensure the progressive liberalization of the economic and social rights, to the maximum of all available resources”, also implying that allowing foreign direct investment revenues to crowd out human rights undertakings may be incompatible with international law.

In this context, the right to development – in the light of the Millennium Development Goals and the International Covenant as described above – implies a duty to take into consideration potential adverse human rights impacts of a project, but, the right to development also implies “something more: that the agreement serve the development of the country as a whole, rather than only the specific groups that stand to benefit from its implementation.”¹²⁶ This issue will be explored further later on.

3.2.3.4 The Right to Information and Access to Effective Remedies

Also the right to information as stated in the Covenant on Civil and Political Rights¹²⁷ should be considered before moving on to the relationship between business and human rights. Whilst the right to development focuses on the objectives of an investment, the right to information focuses on the means

¹²⁴ De Schutter, Olivier, et. al., *Foreign Direct Investment and Human Development – the Law and Economics of International Investment Agreements*, Routledge, New York, 2013, p. 169.

¹²⁵ United Nations, *International Covenant on Economic, Social and Cultural Rights*, New York, 10 December 1966.

¹²⁶ De Schutter, Olivier, et. al., *Foreign Direct Investment and Human Development – the Law and Economics of International Investment Agreements*, Routledge, New York, 2013, p. 171.

¹²⁷ United Nations, *The International Covenant on Civil and Political Rights*, New York, 16 December 1966.

through which the objective may be reached and is an important ingredient in any democratic state.¹²⁸

For foreign direct investment in developing countries, where the lack of democracy and rule of law may influence the negotiations of the investment, this may have an impact on the negotiations of investment treaties as well as state-investor agreements. For the latter, an agreement is often “concluded outside any form of public scrutiny” and both parties seem to prefer extensive confidentiality.¹²⁹ For the state, the secrecy surrounding foreign direct investment may be motivated by a “fear that too much transparency would allow groups of citizens to veto agreements that would be in the interest of the country as a whole”, but could also be a direct result of the simple fact that “they prefer to decide how to spend the revenues from the deal which is concluded.”¹³⁰

When the right to information is not fulfilled, and a close scrutiny of the investment contract prior to its conclusion is not possible, the right to access to effective remedies becomes essential. For communities affected negatively by the investment, access to remedies may indeed be the only way to gain compensation.

Access to effective remedies is recognized in general principles of international human rights law, and included in the UN Guiding Principles as an essential component for the full integration of business and human rights.¹³¹ Also this right may, however, be limited through state-investor contracts since such contracts, much like investment treaties, “protect the investor from the adoption of regulation that amount to indirect expropriation, and situations may therefore arise in which the rights of investors are pitted against those of the individuals or communities whose risks are negatively affected by the investment”.¹³² This is due to the very nature of state-investor agreements since they are typically “internationalized” in the sense that the applicable law is international law, or municipal law “frozen” with the use of stabilisation clauses as described above.¹³³ Also, state-investor agreements most often refer any disputes rising from the contract to international arbitration. Although other relevant rules of international law may be taken into account by an arbitral tribunal, this is not an efficient insurance against corporate-related human rights abuses.¹³⁴

Why this is the case will be discussed further below. In this context, also the problems arising from the above-mentioned rights and foreign direct investment will be discussed further. First, however, further regulation – or rather voluntary principles – on foreign direct investment and human rights will be looked at.

¹²⁸ De Schutter, Olivier, et. al., *Foreign Direct Investment and Human Development – the Law and Economics of International Investment Agreements*, Routledge, New York, 2013, p. 172.

¹²⁹ Ibid.

¹³⁰ De Schutter, Olivier, et. al., *Foreign Direct Investment and Human Development – the Law and Economics of International Investment Agreements*, Routledge, New York, 2013, p. 173.

¹³¹ Ibid., p. 173.

¹³² Ibid., p. 173.

¹³³ Ibid., p. 175-176.

¹³⁴ Ibid., p. 176.

4 INTEGRATING FOREIGN DIRECT INVESTMENT AND HUMAN RIGHTS

Having taken a closer look at the legal realms of foreign direct investment and international human rights, time has come to consider areas where they overlap. In the following text the concepts of Corporate Social Responsibility, sustainable investments and the so-called governance gap will be looked at. This will be followed by an introduction to the UN Guiding Principles, and the extensive work carried out within the UN to integrate foreign direct investment and human rights.

4.1 History of the Business and Human Rights Debate

4.1.1 Corporate Social Responsibility

The concept of corporate social responsibility developed already in the 1950s and 1960s, as transnational and multinational corporations became strong forces on the global market.¹³⁵ Corporate social responsibility, in embracing raised awareness and standards on business ethics and good business practice, is a solely voluntary measure applied by national and international businesses alike.¹³⁶

Whether corporate social responsibility should be part of business has, however, been debated. In 1970 Milton Friedman expressed concerns regarding the “social responsibility” of businesses, dismissing it as a matter for the state rather than the business-sector to be concerned with.¹³⁷ Instead, Friedman meant, “there is one and only one social responsibility of business – to use its resources and engage in activities designed to increase its profits”.¹³⁸

Corporate social responsibility “concerns how business enterprises relate to, and impact upon, a society’s needs and goals” and can thus take various shapes.¹³⁹ It must be noted that it “encompasses an array of meanings and intended applications that have undergone substantial modifications over time”, providing for different interpretations and meanings of the concept.¹⁴⁰ Furthermore, although corporate social responsibility is often linked to human rights, environment, labour and anti-corruption it may entail any kind of action intended to contribute to the social and cultural development of the community a corporation is operating within.¹⁴¹

¹³⁵ UNCTAD, *The Social Responsibility of Transnational Corporations*, New York and Geneva, 1999, p. 13.

¹³⁶ Ibid.

¹³⁷ Friedman, Milton, *The Social Responsibility of Business is to Increase its Profits*, New York Times Magazine, September 13, 1970.

¹³⁸ Ibid., p. 5.

¹³⁹ UNCTAD, *The Social Responsibility of Transnational Corporations*, New York and Geneva, 1999, p. 1.

¹⁴⁰ Ibid., p. 2.

¹⁴¹ UNCTAD, *The Social Responsibility of Transnational Corporations*, New York and Geneva, 1999, p. 7.

The voluntary character of corporate social responsibility has been, and still is, criticised. Since the introduction of corporate social responsibility the corporate sphere have maintained an aversion to the introduction of legally binding instruments on the matter, whilst regulation on pure investment matters have been welcomed.¹⁴² As of today, corporate social responsibility – or similar concepts - is an integrated part of most business enterprises and whilst remaining voluntary measures they have played a significant role in developing a closer connection between business and human rights.

4.1.2 The UN Global Compact

The change in attitude toward the relationship between business and human rights became significant also for developments within the UN. As has been noted, following the corporate-related human rights abuses in the 1990's, there was a call for states to act on a global level to prevent further violations. At the World Economic Forum in Davos in 1999, then Secretary-General Kofi Annan thus challenged the global business sector to take part in a global compact to give a “human face to the global market” by implementing human rights, labour standards and environmental practices in the “corporate sphere”.¹⁴³ In July 2000 the United Nations Global Compact (UNGC) was officially launched¹⁴⁴, and in 2004 extended to include also anti-corruption measures following the introduction of the UN Convention against Corruption.¹⁴⁵ The UNGC has since functioned as a guide to business and human rights, and sets out ten universally recognized principles.¹⁴⁶ Principle one and two concern human rights, stating businesses should “support and respect the protection of internationally proclaimed human rights” and “make sure they are not complicit in human rights abuses.”¹⁴⁷

The concept of a global compact has received much critique with regards to the success of implementing human rights into the business sector. Non-governmental organisations (NGOs) have argued there is a need for “legally-binding regulations to control corporate activities with respect to human rights”¹⁴⁸, indicating that a guidance tool such as the UNGC is not enough.

4.1.3 The UN Draft Norms

In 2003 the UN Sub-Commission for the Promotion and Protection of Human Rights adopted the Draft Norms on the Responsibilities of Transnational

¹⁴² Ibid., p. 9.

¹⁴³ United Nations World Economic Forum, *Secretary General Proposes Global Compact on Human Rights, Labour, Environment, in Address to World Economic Forum in Davos*, Press release SG/SM/6881, United Nations, Davos, 1 February 1999.

¹⁴⁴ United Nations Global Compact, *After the signature – A Guide to Engagement in the United Nations Global Compact*, January 2012, p. 3.

¹⁴⁵ United Nations Office on Drugs and Crime, *UN Convention Against Corruption*, New York 2004.

¹⁴⁶ United Nations Global Compact, *Overview - the UN Global Compact*, Retrieved 2012-10-14, , <http://www.unglobalcompact.org/AboutTheGC/>.

¹⁴⁷ United Nations Global Compact, *The ten principles – Human Rights*, Retrieved 2012-10-14, <http://www.unglobalcompact.org/AboutTheGC/TheTenPrinciples/humanRights.html>.

¹⁴⁸ Global Policy Forum Europe, *Speaking Notes of a hearing at the UN*, Geneva, 4 July 2007, p. 9, <http://www.scribd.com/doc/17222782/20070704-Global-Compact-Alternative-Hearing-2007>.

Corporations and other Business Enterprises with Regard to Human Rights.¹⁴⁹ Created to combat the deficiency of the UNGC's voluntary character by providing a more detailed regulatory framework, the draft Norms were intended to complement the UNGC and become a binding instrument. The increase of corporations operating in several nations was claimed to cause "economic activities beyond the actual capacities of any one national system"¹⁵⁰, and the draft Norms were drafted in awareness of the growing pressure on the international community to react to human rights abuses related to globalisation.

The draft Norms thus established that the primary responsibility for the protection of human rights was to remain with the state, but that within their respective area of activity and "sphere of influence", corporations have obligations with regards to human rights.¹⁵¹ Corporate responsibility had until this point been considered voluntary, relying on the efforts made by individual corporations, but the draft Norms reformed the previously held view within the international community that international human rights were mainly a matter of national governments to be concerned with. In 2004, however, the Commission on Human Rights concluded the draft Norms not to be legally binding, thus leaving the global community in the same state of uncertainty it had previously been with regards to business and human rights.¹⁵²

4.1.4 The Governance Gap

When there is a willingness amongst transnational corporations to incorporate policies concerning social responsibilities, amongst which human rights and the right to development may be included, one may wonder why there is a problem at all. The following quote pinpoints a major issue:

The root cause of the business and human rights predicament today lies in the governance gaps created by globalization – between the scope and impact of economic forces and actors, and the capacity of societies to manage their adverse consequences. These governance gaps provide the permissive environment for wrongful acts by companies of all kinds without adequate sanctioning or reparation. How to narrow and ultimately bridge the gaps in relation to human rights is our fundamental challenge.¹⁵³

International human rights have primarily been considered falling under the responsibility of governments, with the intention to regulate the relationship

¹⁴⁹ United Nations Economic and Social Council, *Norms on the responsibilities of transnational corporations and other business enterprises with regards to human rights*, 13 August 2003. Hereafter referred to as the UN Norms.

¹⁵⁰ Ibid., see Preamble p. 2.

¹⁵¹ Ibid. See Section A.1 p. 3. For further details on the UN Norms please refer to United Nations, *Commentary on the Norms on the Responsibilities of Transnational Corporations and Other Business Enterprises with Regard to Human Rights*, U.N. Doc. E/CN.4/Sub.2/2003/38/Rev.2 (2003), 2003.

¹⁵² Ruggie, John, *Business and Human Rights: the evolving International Agenda*, American Journal of International Law, June 2007.

¹⁵³ United Nations, *"Protect, Respect and Remedy" Framework*, 7 April 2008, p. 3.

between a state and individuals or groups.¹⁵⁴ However, “with the increased role of corporate actors, nationally and internationally, the issue of business’ impact on the enjoyment of human rights” has led to debates as to whether also corporations should be responsible under international human rights law.¹⁵⁵

4.2 The UN Guiding Principles

In recent decades the UN has carried out extensive work in the area of business and human rights, and consultations with stakeholders resulted in the endorsement of the UN Guiding Principles in 2011 which, in implementing the UN Framework, establishes “a global standard for preventing and addressing the risk of adverse impacts on human rights linked to business activity”.¹⁵⁶ The UN Guiding Principles are significant in changing the previously held view of international human rights being primarily a state-matter¹⁵⁷ and thus deserve further consideration.

4.2.1 The Mandate

Despite the rejection of the draft Norms several states recognized the importance of the issue at hand and that it required “serious attention”.¹⁵⁸ As a result, in April 2005, the UN Commission on Human Rights (since 2006 replaced by the UN Human Rights Council) requested the Secretary General to appoint a special representative to “identify and clarify” the ruling standards on corporate responsibility and find a way to implement legally binding norms acceptable to all stakeholders involved. Three days later, Harvard Professor John Ruggie was appointed UN Secretary General Special Representative (SGSR) for Business and Human Rights.¹⁵⁹

The mandate was initially intended to last for a period of two years, but was extended for yet another three until 2011. The mandate can be divided into three phases of which the first was to “identify and clarify” ruling standards and practices during the initial two year-mandate.¹⁶⁰ The second phase began as the mandate was extended in 2007, encouraging the SRSG to submit “recommendations” which in June 2008 resulted in the submission of the UN “Protect, Respect and Remedy” Framework.¹⁶¹ In June 2008 SRSG John Ruggie presented the Framework, providing for the type of authoritative focal point previously missing, and when the Human Rights Council unanimously endorsed the Framework this marked the first time in history a UN intergovernmental

¹⁵⁴ Office of the High Commissioner for Human Rights, *Your Human Rights: Human Rights Issues – Business and Human Rights*, United Nations, Retrieved 2012-11-23, <http://www.ohchr.org/EN/ProfessionalInterest/Pages/InternationalLaw.aspx>.

¹⁵⁵ Ibid.

¹⁵⁶ Ibid.

¹⁵⁷ United Nations, *Guiding Principles*, 21 March 2011, p. 5 (introduction).

¹⁵⁸ Ruggie, John, *Business and Human Rights: the evolving International Agenda*, American Journal of International Law, June 2007, p. 4.

¹⁵⁹ Ibid., p. 1.

¹⁶⁰ United Nations, *Guiding Principles*, 21 March 2011, p. 3.

¹⁶¹ United Nations, *Guiding Principles*, 21 March 2011, p. 3 (introduction).

body had taken “a substantive policy position” in the area of business and human rights.¹⁶²

The third and last phase of the mandate began as the SRSG was asked to “operationalize” the Framework, and provide “the concrete and practical recommendations for its implementation”.¹⁶³ This was very much due to the concerns expressed with regards to the problems in reaching an agreement suitable for all stakeholders. Indeed:

...one reason cumulative progress in the business and human rights area had been difficult to achieve was the lack of an authoritative focal point around which actors’ expectations could converge—a framework that clarified the relevant actors’ responsibilities, and provided the foundation on which thinking and action could build over time.¹⁶⁴

In 2011 the Guiding Principles were presented, marking the end of the mandate but even more so a new era in the area of business and human rights.

4.2.2 The Corporate Responsibility to Respect Human Rights

The Framework rests on three pillars, each presenting a core value and complementing one another to ensure sustainable progress: the State duty to protect against human rights abuses by third parties, including businesses; the corporate responsibility to respect human rights; and the need for access to effective remedies.¹⁶⁵ The UN Guiding Principles, by implementing the Framework, rests upon the same principles and construction, and are intended to provide a “common global platform for action” in the area of business and human rights.¹⁶⁶ In doing so, the Framework and the UN Guiding Principles require human rights to be incorporated in due diligence processes.

For the topic at hand, the second pillar of the Framework is of essence. The following text establishes the first foundational principle of the corporate responsibility to respect human rights: “Business enterprises should respect human rights. This means that they should avoid infringing on the human rights of others and should address adverse human rights impacts with which they are involved.”¹⁶⁷ The corporate responsibility to respect human rights is intended to function as “a global standard of expected conduct for all business enterprises wherever they operate” and requires corporations to take positive actions to do so.¹⁶⁸

Important to note is that the corporate responsibility exists independently of the state duty to protect, thereby removing the previously confusing distinction between primary and secondary obligations in relation to states, corporations

¹⁶² United Nations Introductory Description, *The UN “Protect, Respect and Remedy” Framework for Business and Human Rights*, September 2010, p. 1.

¹⁶³ United Nations, *Guiding Principles*, 21 March 2011, p. 4 (introduction).

¹⁶⁴ United Nations Introductory Description, *The UN “Protect, Respect and Remedy” Framework for Business and Human Rights*, September 2010, p. 1.

¹⁶⁵ United Nations, *“Protect, Respect and Remedy” Framework*, 7 April 2008.

¹⁶⁶ United Nations, *Guiding Principles*, 21 March 2011, p. 5 (introduction).

¹⁶⁷ *Ibid.*, p. 13.

¹⁶⁸ United Nations, *Guiding Principles*, 21 March 2011, p. 13.

and human rights. Furthermore, the responsibility “exists over and above compliance with national laws and regulations protecting human rights”.¹⁶⁹ Essentially, the Framework requires corporations to “do no harm”, establishing that a passive position is not enough, but that also active measurements must be taken when needed.¹⁷⁰

The relationship between the state and the corporate entity remains one of great focus, but the UN Guiding Principles clearly states that the corporate duty to respect “exist independently of States’ abilities and/or willingness to fulfil their own human rights obligations”.¹⁷¹ However, the actions taken by a corporation to fulfil their obligations may not under any circumstances undermine the ability of the State to fulfil theirs.¹⁷²

The second foundational principle of the corporate responsibility to respect human rights states:

The responsibility of business enterprises to respect human rights refers to internationally recognized human rights – understood, at a minimum, as those expressed in the International Bill of Human Rights and the principles concerning fundamental rights set out in the International Labour Organization’s Declaration on Fundamental Principles and Rights at Work.¹⁷³

Although some human rights may be at greater risk than others, corporations are under Guiding Principle number 12 responsible to adhere to all internationally recognized human rights. This is based on the extensive impact a corporate entity may have on “virtually the entire spectrum” of human rights.¹⁷⁴ In addition to the International Bill of Human Rights¹⁷⁵ the commentaries also refer to the ILO core convention as set out in the Declaration on Fundamental Principles and Rights at Work, but stresses that additional standards must be considered under certain circumstances.¹⁷⁶ In this respect, corporations are encouraged to adhere to the human rights of groups or populations that may require “particular attention” – such as; women; children; indigenous people; minorities; disabled and migrant workers¹⁷⁷ - where they may have adverse human rights impacts on them.¹⁷⁸

Guiding Principles 13, 14 and 15 need not be cited in their complete form. In discussing foreign direct investment and human rights it is enough to mention that Guiding Principle 13 states that a corporation is responsible for adverse human rights impacts caused through their own activities as well as those caused through business relations with other parties, including the

¹⁶⁹ United Nations, *Guiding Principles*, 21 March 2011, p. 13.

¹⁷⁰ United Nations, “*Protect, Respect and Remedy*” Framework, 7 April 2008, p. 17.

¹⁷¹ United Nations, *Guiding Principles*, 21 March 2011, p. 13.

¹⁷² Ibid.

¹⁷³ Ibid., Guiding Principle 12.

¹⁷⁴ Ibid., p. 13-14 and p. 17.

¹⁷⁵ Consisting of the UNDHR and the two Covenants further discussed below.

¹⁷⁶ United Nations, *Guiding Principles*, 21 March 2011, p. 13-14.

¹⁷⁷ This list is by no means exhaustive, but provides an example of groups or populations whose rights the UN have elaborated further.

¹⁷⁸ United Nations, *Guiding Principles*, 21 March 2011, p. 13-14 (A. Foundational Principles).

understanding of “activities”, both acts and omissions.¹⁷⁹ In addition, the responsibility encompasses corporations “regardless of their size, sector, operational context, ownership and structure”, and although these factors may impact the capacity of a corporation to adhere to adverse human rights impacts they do not excuse such impacts according to Guiding Principle 14.¹⁸⁰

Guiding Principle 15 states that certain operational principles must be in place in order for a corporate entity to be able to meet the demands as set out above, and establishes policies and processes necessary to do so. Amongst a policy commitment and processes to enable remediation, a “human rights due-diligence process to identify, prevent, mitigate and account for how they address their impacts on human rights” should be in place.¹⁸¹

4.2.3 Human Rights Due Diligence

Human rights due diligence in the context of the UN Guiding Principles is as such a new concept, introduced by the SGSR as late as in 2008.¹⁸² The following defines the parameters for human rights due diligence:

In order to identify, prevent, mitigate and account for how they address their adverse human rights impacts, business enterprises should carry out human rights due diligence. The process should include assessing actual and potential human rights impacts, integrating and acting upon the findings, tracking responses, and communicating how impacts are addressed. Human rights due diligence:

- (a) Should cover adverse human rights impacts that the business enterprise may cause or contribute to through its own activities, or which may be directly linked to its operations, products or services by its business relationships;
- (b) Will vary in complexity with the size of the business enterprise, the risk of severe human rights impacts, and the nature and context of its operations;
- (c) Should be ongoing, recognizing that the human rights risks may change over time as the business enterprise’s operations and operating context evolve.¹⁸³

The Framework thus states three factors which should be considered by corporations to fulfil the human rights due diligence-requirement; the country context and specific human rights challenges posed; their own human rights impact and; any indirect impact their activities may cause.¹⁸⁴ This requires potential adverse human rights impacts to be addressed, either through mitigation of the problem or prevention of it, as early as possible in the project but allows for the due-diligence process to be an integrated part of a larger risk-management system of a corporation.¹⁸⁵

¹⁷⁹ United Nations, *Guiding Principles*, 21 March 2011, p. 14 (Guiding Principle 13. See also Guiding Principle 19)

¹⁸⁰ *Ibid.*, see Guiding Principle 14.

¹⁸¹ *Ibid.*, p. 15 (Guiding Principle 15).

¹⁸² Institute for Human Rights and Business: *The State of Play” of Human Rights Due Diligence*, London, 2011, p. 11.

¹⁸³ United Nations, *Guiding Principles*, 21 March 2011, p. 16 (Guiding Principle 17).

¹⁸⁴ United Nations, *“Protect, Respect and Remedy” Framework*, 7 April 2008, p. 17.

¹⁸⁵ United Nations, *Guiding Principles*, 21 March 2011, p. 16 (Guiding Principle 17).

The concept of thoroughly establishing human rights due diligence and see to possible adverse human rights impacts in advance is intended to help businesses prove they took steps to prevent an abuse in cases where legal claims of corporate-related human rights abuses arise. However, the establishment of a due diligence procedure concerning human rights does not exclude the corporation from being held responsible for human rights abuses.¹⁸⁶

Whilst Guiding Principle 17, referred to above, defines the parameters of human rights due-diligence Guiding Principles 18-21 defines what this should entail. In the Commentary to Guiding Principle 18 it is stressed that the purpose of the impact assessment is to “understand the specific impacts on specific people, given a specific context of operations” and that so should be done prior to a proposed investment and with a dynamic approach to adapt to changes in international human rights law.¹⁸⁷ Business enterprises face a challenge in assessing actual and potential adverse human rights impacts in all sectors of the business and, where there is a risk of impact, to address the issue.¹⁸⁸ Extensive horizontal integration is thus required. However, in situations where the corporations cannot be directly attributed a specific impact but the cause of the impact can be associated with the products, services or operations of the corporation the responsibility may not extend to the corporation as such.¹⁸⁹ In these situations the level of responsibility – and following requirements to take action - will depend on factors such as “leverage over the entity concerned, how crucial the relationship is to the enterprise, the severity of the abuse, and whether terminating the relationship with the entity itself would have adverse human rights consequences”.¹⁹⁰

At large, the purpose of human rights due diligence is for corporations to establish and adhere to practices and policies which demonstrate an understanding and respect for international human rights “in practice”.¹⁹¹ A key to doing so is communication, transparency, consultations, reports and, in cases where there may be impact, accountability.¹⁹² The corporate responsibility to respect human rights also includes providing for effective remediation in cases where adverse impacts on human rights have been identified.¹⁹³

As a concluding note on human rights due diligence, it must be mentioned that the entire concept of a corporate responsibility to respect human rights builds upon the context that “all business enterprises have the same responsibility to respect human rights wherever they operate”, and although certain circumstances may cause non-compliance these should be assessed and avoided to the largest extent possible.¹⁹⁴

¹⁸⁶ United Nations, *Guiding Principles*, 21 March 2011, p. 16 (Guiding Principle 17).

¹⁸⁷ *Ibid.*, p. 16 (Guiding Principle 18).

¹⁸⁸ *Ibid.*, p. 18 (Guiding Principle 19).

¹⁸⁹ *Ibid.*, p. 18 (Guiding Principle 19).

¹⁹⁰ *Ibid.*, p. 18 (Guiding Principle 19).

¹⁹¹ *Ibid.*, p. 20 (Guiding Principle 21).

¹⁹² *Ibid.*, p. 20 (Guiding Principle 21).

¹⁹³ *Ibid.*, p. 20 (Guiding Principle 22).

¹⁹⁴ United Nations, *Guiding Principles*, 21 March 2011, p. 20 (See Guiding Principle 23-24).

4.3 Impact of the UN Guiding Principles

The UN Guiding Principles are a significant step toward a full integration of business and human rights, and play an important role for foreign direct investment in developing countries. In this section, the legal impacts of the Guiding Principles as well as the effects they have on foreign direct investment in developing countries will be looked at. In this context, also the UN Principles on Responsible Contracts introduced right after the UN Guiding Principles will be considered.

4.3.1 Legal Impact

Perhaps the most significant impact of the Guiding Principles is the clarification of the roles of the state and the corporation in relation to human rights. In imposing a state duty to protect human rights, along with a corporate responsibility to respect human rights, the UN Guiding Principles demonstrate that the respective roles of states and corporations are different, yet complementary.¹⁹⁵

The entire concept of clarifying the roles is, as has been stated, to ensure also corporations take action to promote further human rights development - especially with regard to those human rights possibly affected by foreign direct investments. However, in submitting the Principles to the Human Rights Council, the SGSR stressed that although a large group of stakeholders contributed to the development of the principles, they are by no means intended to function as a “tool-kit, simply to be taken off the shelf and plugged in”.¹⁹⁶

The Principles, although universally applicable, will not form a one-size-fits-all-solution but rather they aim to recognize that as of 2011 “we live in a world of 192 United Nations Member States, 80,000 transnational enterprises, 10 times as many subsidiaries and countless millions of national firms”.¹⁹⁷ The following quote summarizes the impact on international law:

The Guiding Principles’ normative contribution lies not in the creation of new international law obligations but in elaborating the implications of existing standards and practices for States and businesses; integrating them within a single, logically coherent and comprehensive template; and identifying where the current regime falls short and how it should be improved.¹⁹⁸

In understanding the effects the Principles have on international law – both within investment and human rights – one must remember that they do not constitute a legal framework in a traditional sense. The corporate *responsibility* to respect human rights remain a responsibility only, and cannot be attributed the same meaning as the *duty* imposed upon states. This is due to the fact that international human rights law imposes obligations on states, but not on

¹⁹⁵ United Nations, *Principles for Responsible Contracts*, 25 May 2011, p. 26.

¹⁹⁶ United Nations, *Guiding Principles*, 21 March 2011, p. 5.

¹⁹⁷ Ibid.

¹⁹⁸ Ibid.

corporations directly.¹⁹⁹ Only where international human rights treaties have been incorporated into domestic law may there be a direct impact on corporations.²⁰⁰

The impact of the Principles thus remains dependent on the level of implementation by states and corporations worldwide.²⁰¹ The voluntary character of the Principles has been criticised, especially by NGOs, due to the resulting lack of enforcement.²⁰² Nevertheless, the Principles are considered a major step for the continued integration of business and human rights, and although no legal obligations are imposed upon corporations through the corporate responsibility to respect, they confirm that human rights are not solely a state-concern. In doing so, they encourage states to adopt domestic regulation allowing for corporations to be held responsible for violations of international human rights law.²⁰³

Some progress has been made in this respect. For example, in June 2010, the US amended the Dodd-Frank Consumer Act to require human rights due diligence for corporations utilizing minerals to ensure their products were not “conflict-minerals” contributing to the conflict in the Democratic Republic of Congo.²⁰⁴ Also other states – some more explicitly than others – have expressed their support for the Framework and the Principles implementing it.²⁰⁵ The UK Trade & Investment, for example, implicitly states that the Government is “fully committed to” the implementation of the Principles and “expects UK businesses to operate at all times in a way respectful of human rights whether in Britain or overseas”.²⁰⁶

4.3.2 Principles for Responsible Contracts

Following the introduction of the UN Guiding Principles, the UN SGSR also published a report on Principles for Responsible Contracts.²⁰⁷ The report states that “irrespective of the sector involved, the negotiation process between a host State and a business investor offers a unique opportunity to identify, avoid and

¹⁹⁹ Office of the High Commissioner, *The Corporate Responsibility to Respect Human Rights – an interpretive Guide*, UN doc. HR/PUB/12/02, United Nations, New York and Geneva, 2012, p. 10.

²⁰⁰ Office of the High Commissioner, *The Corporate Responsibility to Respect Human Rights – an interpretive Guide*, UN doc. HR/PUB/12/02, United Nations, New York and Geneva, 2012, p. 10.

²⁰¹ Ibid.

²⁰² United Nations, *Application of the UN “Protect, Respect and Remedy” Framework*, 30 June 2011, p. 5. See for example statement made by Amnesty International.

²⁰³ Schoemaaker, Daan, *Raising the Bar on Human Rights – What the Ruggie Principles Mean for Responsible Investors*, Sustainalytics, August 2011, p. 11.

²⁰⁴ Ibid., p. 12.

²⁰⁵ United Nations, *Application of the UN “Protect, Respect and Remedy” Framework*, 30 June 2011. See for example the European Union Presidency Statement on “Protect, Respect and Remedy” Framework made on November 2009 and the Swedish statements in Third Committee interactive dialogues on 3 November 2010.

²⁰⁶ UK Trade & Development, *Overseas Business Risk - Business and Human Rights*, 29 October 2012, Retrieved 2012-11-29, http://www.ukti.gov.uk/en_ae/export/howwehelp/overseasbusinessrisk/item/308520.html?null.

²⁰⁷ United Nations, *Principles for Responsible Contracts*, 25 May 2011, p. 1. Hereafter referred to in text as the Principles, not to be confused with the Guiding Principles discussed above.

mitigate human rights risks” and the Principles are intended to provide a way through which human rights can be an incorporated part of all such negotiation processes.²⁰⁸ The report asks business investors and host states to incorporate human rights risk in the management of a project and requires for it to be an essential consideration at the negotiation stage in cases where the project is; large-scale or in other ways present significant social, economic or environmental risks or opportunities and; where the project involves significant depletion of natural resources.²⁰⁹

In this sense, the Principles “demonstrates the growing interest for bridging the areas of investment and human rights, in part in order to ensure that the race to attract investors will not result in the host state neglecting its duties to protect and fulfil the human rights of its population.”²¹⁰ However, the report also points to the benefits for both business investors and host states of considering potential adverse human rights impacts at an early stage of the project, and the risks involved for all parties when such considerations are left out.²¹¹

Ten key principles are presented for the full integration of human rights management in contract negotiations, and have a close resemblance with the human rights due diligence as stated in the UN Guiding Principles in the sense that extensive preparation and identification of possible impacts and ways to address such impacts is required.²¹² Also more specific parts of the negotiation process are identified, including the use of stabilisation clauses. Principle 4 states:

Contractual stabilization clauses, if used, should be carefully drafted so that any protections for investors against future changes in law do not interfere with the State’s bona fide efforts to implement laws, regulations or policies in a non-discriminatory manner in order to meet its human rights obligations.²¹³

Furthermore, it is clarified that “the laws, regulations and standards governing the execution of the project should facilitate the prevention, mitigation and remediation of any negative human rights impacts throughout the life cycle of the project”.²¹⁴ It is stated that the host state “should be able to monitor the project’s compliance with relevant standards to protect human rights while providing necessary assurances for business investors against arbitrary interference in the project.”²¹⁵

²⁰⁸ United Nations, *Principles for Responsible Contracts*, 25 May 2011, p. 1.

²⁰⁹ I United Nations, *Principles for Responsible Contracts*, 25 May 2011, p. 5-6 (see especially Figure 1).

²¹⁰ De Schutter, Olivier, et. al., *Foreign Direct Investment and Human Development – the Law and Economics of International Investment Agreements*, Routledge, New York, 2013, p. 163.

²¹¹ United Nations, *Principles for Responsible Contracts*, 25 May 2011, p. 5.

²¹² Ibid. See especially Principles 1 and 2.

²¹³ Ibid., Principle 4.

²¹⁴ Ibid., see especially Principle 3.

²¹⁵ Ibid., see Principle 8.

4.3.3 Impact on Foreign Direct Investment in Developing Countries

Also within the investment-sector the Principles have raised a debate concerning sustainable investment, and the corporate responsibility to respect human rights is becoming increasingly recognized in soft law as well as through voluntary initiatives. Considering the broad recognition of the Principles amongst states, corporations and NGOs there is likelihood the Principles will indeed be implemented in domestic laws.

Further voluntary measures have also been taken and it appears as if the need for further integration of business and human rights is recognized, not the least with regards to human rights in developing countries. At the 2012 United Nations Conference on Trade and Development (UNCTAD) a “new generation of investment policies” was published, recognising the need for an investment policy, internationally and nationally, promoting economic growth whilst taking into account sustainable development.²¹⁶

Despite the recent financial crisis developing countries continue to reach high levels of global foreign direct investment flows, proving the significance of developing countries on the global market as well as a “longer-term shift in economic weight from developed countries to emerging markets”.²¹⁷ The increase in foreign direct investment in developing countries furthermore proves the important role played by investors in promoting human rights and further development, not only in the financial sector but also within other areas.

Also in the OECD Guidelines for Multinational Enterprises²¹⁸ the UN Guiding Principles are recognized, and the 2011 edition of the OECD Guidelines includes a human rights chapter consistent with the corporate responsibility to respect human rights and human rights due diligence. Whilst the OECD Guidelines, much like the UN Guiding Principles, remain a voluntary and unenforceable initiative it is stated “countries adhering to the Guidelines make a binding commitment to implement them...”²¹⁹ Moreover, national or international law may cover matters covered in the OECD Guidelines. To a certain extent it appears as if the OECD Guidelines are a successful initiative despite their voluntary character, and indeed the use of stabilisation clauses remains lower and different in character in OECD countries than in non-OECD countries.²²⁰

In the actual practice of foreign direct investment, there is a trend toward

²¹⁶ UNCTAD, *World Investment Report 2012: Toward a New Generation on Investment Policies*, New York & Geneva, 2012.

²¹⁷ *Ibid.*, p. 15 and p. 25.

²¹⁸ OECD, *OECD Guidelines for Multinational Enterprises*, OECD Publishing, 25 May 2011, date retrieved: 2012-12-11, <http://www.oecd.org/daf/internationalinvestment/guidelinesformultinationalenterprises/48004323.pdf>. Hereafter referred to as the OECD Guidelines.

²¹⁹ *Ibid.*, p. 13.

²²⁰ Schemberg, Andrea, *Stabilization Clauses and Human Rights – a research project conducted for the IFC and the UN Special Representative to the Secretary General on Business and Human Rights*, March 11 2008. See for example p. 17 where the differences between OECD and non-OECD countries are summarized in brief.

increased awareness and respect for human rights and the right to development. For example, having played a significant role in the development of a more global market International Investment Agreements are suddenly becoming “increasingly controversial and politically sensitive”, much due to the potential lowering of standards related to human rights and sustainable development when developing countries negotiate terms of investment.²²¹ A positive trend is noticeable and some “new IIAs include a number of features to ensure that the treaty does not interfere with, but instead contributes to countries’ sustainable development strategies that focus on the environmental and social impact of investment”.²²² For developing countries such changes in attitude may be of great significance, and efforts are being made to change foreign direct investment policies on a global level. The following quote recognizes this change in attitude, but also points out the complexity of the problem for all stakeholders involved:

States are now more often than ever attempting to challenge the investment regime, by insisting on the renegotiation of investment guarantees...By failing to address host states' international human rights obligations, investors are in effect lending credence to the attempts of states and civil society to delegitimise investment contracts and to call for renegotiation.²²³

Despite efforts from investors and governments alike, human rights remain an area of much controversy and difficulty, and whilst action is being taken within environment, labour and anti-corruption, human rights remain the least implemented of the areas of development introduced through the UN Global Compact.²²⁴ In the following Chapter, the implications of this will be considered further. Furthermore, a description of stabilisation clauses along with a discussion on how they relate to the UN Guiding Principles will be provided for. However, before moving on to these matters, it is important to grasp how extensive the problem really is. The following quote is an excellent example to prove this point:

Of the millions of companies in the world, of which some 80,000 operate internationally...only a very small number – some 250 companies according to available information – have publicly stated policy positions on human rights. These 250 companies are indeed amongst the world’s largest and most influential corporate actors, but they are only a very small fraction of corporations engaged in business globally.²²⁵

Although many steps have been taken to truly integrate business and human rights, they remain legal and political areas worlds apart. When moving on to

²²¹ UNCTAD, *World Investment Report: Towards a New Generation of Investment Policies*, New York and Geneva, 2012, p. 22.

²²² UNCTAD, *World Investment Report: Towards a New Generation of Investment Policies*, New York and Geneva, 2012, p. 22.

²²³ United Nations Global Compact, the Human Rights and Business Dilemmas Forum, *Dilemmas and Case Studies: Stabilisation Clauses- Risks to Business*, United Nations, Retrieved 2011-11-30, <http://human-rights.unglobalcompact.org/dilemmas/stabilisation-clauses/>.

²²⁴ United Nations Global Compact, *Annual Review of Business Policies & Actions to Advance Sustainability – 2011 Global Compact Implementation Survey*, June 2012, p. 3.

²²⁵ Institute for Human Rights and Business: *The State of Play” of Human Rights Due Diligence*, London, 2011, p. 1.

consider stabilisation clauses in relation to human rights, it is of significance this is kept in mind.

5 STABILISATION CLAUSES AND HUMAN RIGHTS

So far, a discussion of the legal realms of foreign direct investment and international human rights has been provided for. Also, the recent changes in attitude on business and human rights – and the impacts of the UN Guiding Principles – have been looked at. It remains, however, to tie these together and look into whether foreign direct investment, and more specifically stabilisation clauses, is indeed a threat to human rights. In order to do so, this Chapter provides a number of case studies as well as a presentation of the main concerns involved. The possible impacts on specific human rights are looked at, followed by how stabilisation clauses relate to the UN Guiding Principles.

5.1 Case Studies

To grasp why stabilisation clauses are controversial some examples where the use of such clauses has resulted in a debate concerning human rights and development will be looked at. It must be kept in mind, however, that far from all investment contracts include stabilisation clauses and in cases where such provisions are included application, impact and form vary.²²⁶ In the following text the examples of the BP Oil investment in 2003, the Chad-Cameroon Pipeline Project in 2005 as well as the ACG Oil Field Development Project from 1994 are described, focusing on the possible implications arising from the use of stabilisation clauses. Unfortunately the number of cases available on this topic is limited – much due to the confidential nature of most state-investor agreements.

5.1.1 BP Oil and the BTC Pipeline Project

In 2003 the construction of two pipelines for oil and gas passing through Azerbaijan, Georgia and Turkey began after the signing of the contract for the Baku-Tbilisi-Ceyhan Pipeline Project. The project was established through state agreements between all three states involved as well as state-investor agreements between the consortium, led by BP Oil, and the host states.²²⁷ The project was, and still is, expected to last for at least 40 years, with a possible extension of another 20 years, and has been criticised to undermine the obligations of the states to protect social and environmental rights.²²⁸

Amnesty International expressed concerns regarding the use of stabilisation clauses in the contracts, especially with regards to the one between the consortium and Turkey. Whilst Turkey is bound to international human rights obligations, Turkey agreed for applicable law to be limited to the laws governing the terms of the contract at the time when the agreements was entered into. The following text from the report from Amnesty International pinpoints the issue:

The objective is to create an environment for foreign investment that avoids the risks to companies of changes in national priorities, together with the changes in law that can result. In

²²⁶ United Nations, *Principles for Responsible Contracts*, 25 May 2011, p. 13.

²²⁷ Amnesty International, *Human Rights on the Line – the Baku-Tbilisi-Ceyhan Pipeline Project*, Amnesty International London, UK, May 2003, p. 9.

²²⁸ Ibid.

order to achieve this, the state typically makes an agreement with the investor that contains what are called 'stabilisation' clauses. These demand that there be no changes in the state's policies that would alter the terms for the project initially agreed, without the consent of the other contracting party. Sometimes the intention is to avoid the risks of nationalisation, or the effects of changes in tax rates. In other cases, such as this one, the intention is much wider because Turkey has undertaken, for at least 40 and possibly 60 years, not to apply any fresh legislation or other measures if these will affect the profitability of the project. This includes measures having their origin in international treaties to which Turkey is a party and measures aimed at improvements in environmental and social protection....²²⁹

Much similar to the afore-mentioned state-investment contracts the one between the consortium and Turkey refers to ruling international petroleum pipeline industry standards and practices for comparable projects to govern the project, and thereby exclude internationally recognised standards on human rights to be included in the project.²³⁰ The conclusion drawn by Amnesty International that the stabilisation clauses included in the contract may have a negative impact on human rights thus seems reasonable.

Although it was not until 2003 a debate on the legality of stabilisation clauses began, stabilisation clauses as such were not an entirely new concept. Rather, they had been in use since the 1960s and 1970s as a risk-mitigation tool against rising nationalization and expropriation of foreign investments, and were considered to be an established part of investment contracts within several industries in all parts of the world - especially in emerging markets.²³¹ Apart from the direct criticism towards the use of stabilisation clauses as such, the sudden stir in 2003 surrounding the use of stabilisation clauses also "signalled a heightened social expectation that investors have a responsibility to respect human rights", which later resulted in BP Oil actually amending the contract through what they referred to as a Human Rights Undertaking.²³²

In the following years human rights advocates and civil society groups continued criticising investors using similar methods to ensure their investments, but although some corporations took actions accordingly the industry as such did not come forward with a statement on the use and possible impacts of stabilisation clauses.²³³

5.1.2 The Chad-Cameroon Pipeline Project

The Chad-Cameroon Pipeline Project in 2005 again brought the debate on stabilisation clauses to surface. The critique began when Amnesty International published a report claiming the parties to the investment agreement had "contracted out" of their respective human rights obligations.

²²⁹ Amnesty International, *Human Rights on the Line – the Baku-Tbilisi-Ceyhan Pipeline Project*, Amnesty International London, UK, May 2003, p. 10.

²³⁰ Ibid.

²³¹ Schemberg, Andrea, *Stabilization Clauses and Human Rights – a research project conducted for the IFC and the UN Special Representative to the Secretary General on Business and Human Rights*, March 11 2008, p. 4.

²³² Ibid., p. 2.

²³³ Ibid.

The project was divided into two parts, the first part entailing extraction of oil and drilling of approximately 300 wells in Chad, and the second part the export of the oil through a pipeline from the Doba fields in Chad to the Atlantic coast at Kribi in Cameroon.²³⁴ It was “one of the largest private-sector investments in Africa” and was agreed to by the governments of Chad and Cameroon, but also of the home states of the corporations involved. The consortium for the investment consisted of US corporation ExxonMobil, US Chevron and the Malaysian state owned oil company Petronas.²³⁵ However, several private investors, banks and export credit agencies also supported the financing of the project and the World Bank considered the project “as a means of bringing about economic development and ‘poverty alleviation’ in both Chad and Cameroon – and especially Chad”.²³⁶

The main concern of the report was the long history of severe human rights abuses by the governments of Chad and Cameroon which, combined with several reports on corruption and human rights abuses surrounding the pipeline project, raised questions as to whether the investment agreement would have a negative impact on human rights in these countries for several years to come. Amnesty International argued that the contractual duties imposed by the investment agreement posed a threat to the duties of both governments to fulfil their human rights obligations under international human rights law.²³⁷

There were several legal instruments governing the terms of the investment between Chad, Cameroon and the Consortium, but the report narrows it down to four essential investment agreements. Two agreements regulate the development of oilfields in Chad: the 1988 agreement between the Consortium and Chad with an initial duration of 35 years but possible extension with another 35 years; the 2004 agreement between the same parties also regulating the development of oilfields and with the same duration and possibility of extension. The construction and operation of the pipeline was in turn regulated by two other agreements; the 1997 COTCO-Cameroon agreement lasting for 25 years with the possibility to extend for another 25 years; the 1998 TOTCO-Chad agreement lasting for 30 years and renewable to extend until last concession expires.²³⁸

The duration of the project is, therefore, significant, and several measures were undertaken to ensure a certain degree of legal predictability and stability for the entire duration of the project. A “stabilisation of law” clause was thus included in each of the four agreements, ensuring that domestic amendments of law would not be applicable to the project unless specifically agreed to and that where national law was inconsistent with the agreement the terms of the agreement would prevail.²³⁹ Article 21.3 of the TOTCO-Chad agreement provides an

²³⁴ Amnesty International, *Contracting out of Human Rights – The Chad-Cameroon Pipeline Project*, Amnesty International UK, September 2005, p. 13.

²³⁵ *Ibid.*, p. 7.

²³⁶ *Ibid.*, p. 13.

²³⁷ *Ibid.*, p. 18.

²³⁸ *Ibid.*, p. 20-21.

²³⁹ *Ibid.*, p. 21-22.

example of these terms:

During the term of this Convention, the Republic of Chad guarantees that no governmental act taken after December 19, 1988 will be applied to TOTCO, without prior agreement between the Parties, which has the duly established effect of increasing, directly, indirectly or by virtue of its application to Shareholders, the obligations and charges imposed by this Convention or which has the effect of adversely affecting the rights and economic benefits of TOTCO or of Shareholders as provided for in this Convention, including the effect duly established and passed on to TOTCO of the adverse effect on the charges of Affiliates or of the Contractors as a result of such act.²⁴⁰

In addition the agreements require any disputes arising under the project and the enforcement of the agreements to be possible only through international arbitration, and establish that domestic law is to be interpreted by the arbitrators and not in a way causing economic disadvantages to the consortium.²⁴¹ The agreements exempts the project from international as well as domestic laws, and establish that the project is to be carried out in conformity with “the relevant national petroleum code and ordinary laws that do not conflict with the project agreement” as well as “the operating standards generally acceptable in the international petroleum industry”.²⁴²

This is in direct contrast with the undertakings both governments have under international law. Both Chad and Cameroon have ratified “a number of international and regional treaties that establish a wide range of human rights obligations”, adhered to ILO standards and are bound by customary international law to fulfil their human rights obligations. Furthermore, they have incorporated the UN Charter, the UDHR as well as the African Charter on Human and Peoples’ Rights and under both constitutions “a range of civil, political, economic, social and cultural rights” are recognized.²⁴³ Both governments, therefore, have obligations under international as well as domestic law to protect human rights and must take “all appropriate means” to fulfil these rights – including taking measures to prevent third parties, such as transnational or multinational corporations, from interfering with human rights.²⁴⁴ With regards to the corporations in this specific project Amnesty International expressed that under the UDHR, a corporation “like all non-state actors in society...has a duty to operate in a responsible manner, and this includes respecting human rights”.²⁴⁵

It must be remembered that the project as well as the critique put forward by Amnesty International came prior to the introduction of the corporate

²⁴⁰ Amnesty International, *Contracting out of Human Rights – The Chad-Cameroon Pipeline Project*, Amnesty International UK, September 2005, p. 22. From the TOTCO-Chad 1998 agreement (translated from French). Similar stabilisation clauses can also be found in art. 34.3 of the Chad 2004 agreement, art. 24.2 of the COTCO-Cameroon 1997 agreement as well as art. 34.3 of the Chad 1988 agreement

²⁴¹ Ibid., p. 23.

²⁴² Ibid., p. 24.

²⁴³ Organization of African Unity, *African Charter on Human and Peoples’ Rights*, CAB/LEG/67/3/Rev 5, Nairobi, 1981.

²⁴⁴ Amnesty International, *Contracting out of Human Rights – The Chad-Cameroon Pipeline Project*, Amnesty International UK, September 2005, p. 18.

²⁴⁵ Ibid., p. 19.

responsibility to respect human rights and human rights due diligence in the UN Framework and UN Guidelines. The legal setting with regards to business and human rights was, as has been explained above, rather uncertain and although steps towards the establishment of a corporate responsibility had been taken it was by no means internationally recognized that this was the case. Also under the circumstances of the time, however, the terms of the agreements were in many ways controversial – especially when considering the human rights records of the host states for the investment, which happen to be some of the lowest in the world.²⁴⁶

The already weak system of human rights recognition combined with the use of extensive stabilisation clauses weakens the state position to fulfil their human rights duties, and in effect relies on the corporation to respect human rights on a more or less voluntary basis. Indeed, “...company codes of conduct and promises of high standards, which should be assurances additional to national regulation, appear to be in effect replacing state regulation of investment projects” under these investment contracts.²⁴⁷

5.1.3 The ACG Offshore Oil Field Development Project

In 1994, with a renewed agreement in 2003, the Azeri-Chirag-Guneshly (ACG) Offshore Oil Field Development Project was entered into by a number of multinational corporations including, to mention a few, BP Oil, Statoil and the State Oil Company of Azerbaijan. The 30-year long project agreement was entered into between the corporations, but was recognized by the Government of Azerbaijan, which also guaranteed all undertakings of the contract for the duration of the project.²⁴⁸

Several methods of stabilisation are used in the agreement, and governing law is tied to international petroleum industry standards and practices prevailing in 1994, thereby “freezing” the law for the duration of the project to these standards.²⁴⁹ The freezing clause - along with the clauses for applicable law, economic stabilisation and arbitration – is included in Article XXIII of the Agreement between the parties and allows for the contract to “constitute a law of the Azerbaijan Republic and shall take precedence over any other current or future law, decree or administrative order” inconsistent with the contract.²⁵⁰ If

²⁴⁶ Amnesty International, *Contracting out of Human Rights – The Chad-Cameroon Pipeline Project*, Amnesty International UK, September 2005, p. 12. See UNDP Human Rights Development index 2004 where Chad and Cameroon were ranked in 167th and 141st place respectively out of the total 177 countries.

²⁴⁷ *Ibid.*, p. 12.

²⁴⁸ United Nations Global Compact, *the Human Rights and Business Dilemmas Forum, Dilemmas and Case Studies: Stabilisation Clauses, What is the dilemma*, United Nations, retrieved 2012-12-12, <http://human-rights.unglobalcompact.org/dilemmas/stabilisation-clauses/>. See also *Agreement on the Joint Development and Production Sharing for the Azeri and Chirag Fields and the Deep Water Portion of the Gunashi Field in the Azerbaijan Sector of the Caspian Sea*, 20 September 1994 (verified February 2003), in Baku, Azerbaijan Republic.

²⁴⁹ *Ibid.*

²⁵⁰ *Agreement on the Joint Development and Production Sharing for the Azeri and Chirag Fields and the Deep Water Portion of the Gunashi Field in the Azerbaijan Sector of the Caspian Sea*, 20 September 1994 (verified February 2003), in Baku, Azerbaijan Republic, Article XXIII (23.1).

the Government of Azerbaijan “invokes any present or future law, treaty, intergovernmental agreement, decree or administrative order which contravenes the provisions of this Contract” without prior consent from the parties the investors are entitled to compensation under the economic equilibrium clause under the same Article.²⁵¹ The Government of Azerbaijan thus undertakes not to enter into any treaties or other agreements that may alter the laws and regulations governing the project, including ones related to human rights.²⁵²

5.2 Human Rights Impacts

The examples provided above do not cover the entire spectrum of possible implications on human rights resulting from the use of stabilisation clauses in state-investor agreements, but they do touch upon the core issues in this essay. This section will provide for main concerns shaping much of the critique presented in the above cases, and specific human rights impacted by the use of stabilisation clauses.

5.2.1 Main Concerns

Before looking into the specifics of stabilisation clauses and the human rights discussed above, it should be recalled that human rights are inherent to all human beings whatever nationality, place of residence, national or ethnic origin, sex, colour, language, religion, or other status a person may hold, and that in being inalienable, human rights may not be interfered except under certain circumstances according to due process.²⁵³ Furthermore, human rights are “indivisible, interrelated and interdependent” - whether they are civil, political, economic, social, cultural or collective rights – and the principles of non-discrimination and equality permeate all areas of international human rights law.²⁵⁴

A description of the purpose and interests underpinning the use of stabilisation clauses has been provided above, along with a description of the three types of stabilisation clauses; freezing clauses; economic equilibrium clauses and; hybrid clauses. As we have seen, the entire purpose of stabilisation clauses is to ensure a certain degree of financial and legal predictability and security for an investment. In doing so, there are three ways in which stabilisation clauses can be used; they are a part of the investment agreement “and therefore form a part of the ground rules upon which the investor operates the project”; they are used as a “reference point for informal dealings and formal negotiations between the

²⁵¹ *Agreement on the Joint Development and Production Sharing for the Azeri and Chirag Fields and the Deep Water Portion of the Gunashi Field in the Azerbaijan Sector of the Caspian Sea*, 20 September 1994 (verified February 2003), in Baku, Azerbaijan Republic, Article XXIII (23.2)

²⁵² *Ibid.*, Article XXIII. See, for example, also Article XXVI on environmental protection and safety of the Agreement.

²⁵³ Office of the High Commissioner for Human Rights, *Your Human Rights – What are human rights*, United Nations, Retrieved 2012-11-23, <http://www.ohchr.org/EN/ProfessionalInterest/Pages/InternationalLaw.aspx>.

²⁵⁴ *Ibid.*

parties of to the agreement”; and they are used as a “formal protection of rights if a dispute should arise”.²⁵⁵

A prominent issue is the use of stabilisation clauses in investment agreements for long-term investments in developing countries. The UN SGSR John Ruggie argues that this is the case due to a number of reasons. To begin with, developing countries rely on foreign investment and external funding to finance domestic projects, such as infrastructure. Being dependent upon a successful investment puts the home state in a weaker position in negotiating the terms of the contract, and may relate to the general tendency amongst host states, and more specifically developing countries, to agree to more beneficial terms for the investor with the underlying intent to attract foreign direct investment.²⁵⁶

A developing country in the role of a host state may not have the capability or possibility to reject an investment on the basis that the investor requires for stabilisation clauses to be included in the agreement, and the protection for the investor is provided to the detriment of the rights of the population. Indeed, it appears as if there is a greater demand from investors, combined with willingness of the host state, to include rather extensive stabilisation clauses in agreements, including ones that may have a direct impact on social and environmental improvements for a long period of time.²⁵⁷ Meanwhile:

...foreign investors will wish to protect their position at the moment of their most favorable bargaining power—i.e., when dealing with a weak (developing or transition) government anxious to attract investment before and during the negotiations for an attractive investment.²⁵⁸

Second, the legal frameworks of developing countries “are rarely as developed as they should be”, and although new laws may be required to adhere to international standards on human rights the incorporation of stabilisation clauses may prohibit the host state from passing such laws.²⁵⁹ In this sense, stabilisation clauses pose a direct obstacle to human rights development.

Third, developing countries have a smaller and tighter budget than developed countries, and in having to pay compensation to investors an already strained budget will be unduly affected.²⁶⁰ For developing countries, therefore, having to

²⁵⁵ Schemberg, Andrea, *Stabilization Clauses and Human Rights – a research project conducted for the IFC and the UN Special Representative to the Secretary General on Business and Human Rights*, March 11 2008, p. 35.

²⁵⁶ United Nations Global Compact, the Human Rights and Business Dilemmas Forum, *Dilemmas and Case Studies: Stabilisation Clauses - Risks to Business*, United Nations, Retrieved 2011-11-30, <http://human-rights.unglobalcompact.org/dilemmas/stabilisation-clauses/>.

²⁵⁷ Schemberg, Andrea, *Stabilization Clauses and Human Rights – a research project conducted for the IFC and the UN Special Representative to the Secretary General on Business and Human Rights*, March 11 2008, p. 17.

²⁵⁸ *Ibid.*, p. 4, see footnote number 11.

²⁵⁹ United Nations Global Compact, the Human Rights and Business Dilemmas Forum, *Dilemmas and Case Studies: Stabilisation Clauses - Risks to Business*, United Nations, Retrieved 2011-11-30, <http://human-rights.unglobalcompact.org/dilemmas/stabilisation-clauses/>.

²⁶⁰ *Ibid.*

compensate a corporation for expenses due to changes in law may be a more expensive deal than simply lowering the standards on human rights.

A fourth argument is that most investments where stabilisation clauses are used are long-term projects. In these cases, the perspective over a long period of time “make it imperative that the host state retains regulatory flexibility to protect the population”, especially with regards to changes in international human rights over time. Stabilisation clauses, in this context, may hinder a state to maintain such regulatory flexibility.²⁶¹

Furthermore, due to the additional costs and complications stated above, the use of stabilisation clauses might lead to unwillingness to pass new laws to fulfil international human rights standards and sometimes even “require states to enter reservations to international treaties exempting specific projects from new standards”. From an international perspective this clarifies that stabilisation clauses may pose a threat to human rights, and furthermore allow developing states to pass laws adhering to a lower human rights-standard than internationally recognized.²⁶²

Also for corporations, and other stakeholders, the use of stabilisation clauses may pose significant problems. For example, “...even where companies/lenders do not face legal risks, they can still face a range of reputational risks.”²⁶³ The very nature of state-investor agreements, and the inclusion of stabilisation contracts, adds yet another dimension to the issue at hand. Amnesty International summarizes some of the issues in the following quote:

While these agreements are little known, rarely studied and generally confidential, their creation and content may have important implications for the enjoyment of human rights. Moreover, these agreements may provide incentives for the host state and the company to disregard their human rights obligations or responsibilities.²⁶⁴

This, much like the other main concerns just referred to, should be kept in mind when looking into the examples of human rights violations provided for above.

5.2.2 Different Levels of Impact

From the above, it seems clear that developing countries are much more vulnerable to possible implications associated with the use of stabilisation clauses. It is also in developing countries where the use of stabilisation clauses is most common.²⁶⁵ More importantly, stabilisation clauses covering laws

²⁶¹ United Nations Global Compact, *the Human Rights and Business Dilemmas Forum, Dilemmas and Case Studies: Stabilisation Clauses - Risks to Business*, United Nations, Retrieved 2011-11-30, <http://human-rights.unglobalcompact.org/dilemmas/stabilisation-clauses/>.

²⁶² Ibid.

²⁶³ Ibid.

²⁶⁴ Amnesty International, *Contracting out of Human Rights – The Chad-Cameroon Pipeline Project*, Amnesty International UK, September 2005, p. 11.

²⁶⁵ Schemberg, Andrea, *Stabilization Clauses and Human Rights – a research project conducted for the IFC and the UN Special Representative to the Secretary General on Business and Human Rights*, March 11 2008, p. 17.

concerning human rights are more often included in agreements where the host state is a developing country.²⁶⁶

It is agreed that freezing clauses, and more specifically full freezing clauses are the most controversial. Not only do they provide the corporation with an opportunity to argue they are not obligated to adhere to new laws, but may thereby also discourage the host state from application and enforcement and effectively “work to reduce the effectiveness of new laws”.²⁶⁷ For this very reason, freezing clauses are not used in most OECD-countries and even considered illegal under certain domestic laws.²⁶⁸

However, other types of stabilisation should not as a result be considered harmless since also economic equilibrium clauses and hybrid clauses are argued to have similar impacts. This is the case if they require the host state to pay direct compensation to the investor for the compliance with new laws, and are used only to a limited extent in OECD countries.²⁶⁹ Furthermore, whilst economic equilibrium clauses are included in a very small amount of agreements in OECD countries, the inclusion of such clauses in cases where the host state is a non-OECD country is much more likely to “cover social and environmental laws of general application as well as to provide full compensation for laws that are not discriminatory toward the investor”.²⁷⁰

Why there is such significant disparity between the use of stabilisation clauses in developed versus developing countries may depend on a number of reasons. That most developed countries consider full freezing clauses, or stabilisation clauses limiting the application of human right laws, illegal is certainly a contributing factor to the lack of the more extensive forms of stabilisation clauses where these countries are host states.²⁷¹ The difference may also be explained by the general perception that there is a greater need for stabilisation clauses to be included where the host state is perceived as posing a greater financial and political risk for an investment, and this happens to be closely connected to the level of development of a country.²⁷²

5.2.3 Stabilisation Clauses and the Right to Development

First and foremost, it should be recalled that the right to development is closely related to the primary responsibility of states for human rights, and requires states to act – domestically and internationally – with the right to development

²⁶⁶ Ibid., p. 33.

²⁶⁷ Schemberg, Andrea, *Stabilization Clauses and Human Rights – a research project conducted for the IFC and the UN Special Representative to the Secretary General on Business and Human Rights*, March 11 2008, p. 35-36.

²⁶⁸ Ibid., see executive summary.

²⁶⁹ Ibid., p. 36.

²⁷⁰ Ibid., see executive summary.

²⁷¹ Ibid., p. 5 (see footnote number 13).

²⁷² Ibid., p. 33.

in mind.²⁷³ This includes ensuring that treaties and agreements for foreign direct investment alike are negotiated and applied in a manner that contributes to development.²⁷⁴ With regards to the argument that stabilisation clauses pose an obstacle to human rights, Article 6(3) is of special interest: States should take steps to eliminate obstacles to development resulting from failure to observe civil and political rights, as well as economic, social and cultural rights.²⁷⁵

In this sense, the negotiation of terms of a contract which freezes the implementation of new laws for the improvement of human rights or in other ways limit the legislative sovereignty of a state, appears to contradict the state duty to promote the right to development. The problem lies in that “host states often see stabilisation clauses as a way to encourage inward investment and provide a favourable investment climate” and therefore “accept stabilisation clauses as one way to provide assurances to investors” - even in cases where this may have a negative impact on human rights and development.²⁷⁶

In relation to the right to development, this contrasts with the role of the state in promoting the right to development on a national, regional and international level, but also with the role of the international community to “promote more rapid development of developing countries”.²⁷⁷ The close connection between the right to development and Millennium Development Goal number eight mentioned above further supports such an argument. As we have seen, foreign direct investment continues to grow, and a global partnership for development becomes an increasingly essential component for a functioning global market where the right to development is a truly integrated right in all sectors.²⁷⁸ Also the Covenant on Economic, Social and Cultural Rights suggests that stabilisation clauses may be criticised for hindering the progressive realisation of rights called upon.²⁷⁹

The entire concept of the right to development implies “that the agreement serve the development of the country as a whole, rather than only the specific groups

²⁷³ United Nations General Assembly, *Declaration on the Right to Development*, adopted through UN doc. A/RES/41/128, United Nation General Assembly 97th plenary meeting, 4 December 1986, Art. 3(3).

²⁷⁴ *Ibid.*, see especially Art. 3, Art. 4 and Art. 8.

²⁷⁵ United Nations General Assembly, *Declaration on the Right to Development*, adopted through UN doc. A/RES/41/128, United Nation General Assembly 97th plenary meeting, 4 December 1986, Art. 6(3).

²⁷⁶ Schemberg, Andrea, *Stabilization Clauses and Human Rights – a research project conducted for the IFC and the UN Special Representative to the Secretary General on Business and Human Rights*, March 11 2008, p. 5.

²⁷⁷ United Nations General Assembly, *Declaration on the Right to Development*, adopted through UN doc. A/RES/41/128, United Nations General Assembly 97th plenary meeting, United Nations, 4 December 1986, Art. 4(2).

²⁷⁸ United Nations, *The Millennium Development Goals Report 2012*, New York, 2012, p. 3.

²⁷⁹ United Nations, *The International Covenant on Economic, Social and Cultural Rights*, New York, 10 December 1966.

that stand to benefit from its implementation.”²⁸⁰ From this perspective, the compatibility of stabilisation clauses and the right to development is debatable.

5.2.4 Stabilisation Clauses and The Right to Access to Effective Remedies

In relation to the Right to Access to Effective remedies discussed above, it was mentioned that state-investor agreements are “internationalized” in the sense that the laws applicable to the agreement is international law or municipal law frozen to time of the negotiations of the agreement. The purpose of this is to protect the investor from arbitrary changes in municipal law, but also “...the consequence is that it may be difficult for the groups aggrieved by the particular investment project to file claims against the investor, since the courts may be unwilling or unable to extend the protection of municipal law to the claimants” under the terms of the contract.²⁸¹

In this respect, the use of stabilisation clauses is closely connected with the right to access to effective remedies, and – since most state-investment agreements refer to international arbitration as the sole means for disputes arising from the contract – also to arbitration. If national courts are to engage the responsibilities of the host state following a claim from an aggrieved individual, this might result in the host state being questioned by an international arbitral tribunal for breach of the investment contract.²⁸² This as such complicates the right to access to effective remedies in relation to foreign direct investment, and whilst it may be argued that the fair and equitable treatment promised should not be limited to the interests of the investor but extended also to those negatively affected by the investment project, a human rights argument in favour of the host state may not necessarily exclude the right to compensation for the investor.²⁸³

Indeed, an arbitral tribunal may consider other rules of international law – in addition to the terms of the contract where the parties have designated no other law applicable – and thereby look to international human rights law in solving a dispute even where such an argument is not raised by the host state.²⁸⁴ In some cases, an approach “denying the investor protection were the investor to act in violation of human rights” has been applied, but in general it appears as if arbitral tribunals does not consider such arguments to be of relevance, especially “when the argument was that the obligations imposed on the host State...were such that they were an obstacle to that State discharging its duties towards its population.”²⁸⁵

Regardless of how arbitral tribunals treat the matter, it remains that an individual or group claiming human rights abuses on the grounds of the use of

²⁸⁰ De Schutter, Olivier, et. al., *Foreign Direct Investment and Human Development – the Law and Economics of International Investment Agreements*, Routledge, New York, 2013, p. 171.

²⁸¹ De Schutter, Olivier, et. al., *Foreign Direct Investment and Human Development – the Law and Economics of International Investment Agreements*, Routledge, New York, 2013, p. 175-176.

²⁸² *Ibid.*, p. 176.

²⁸³ *Ibid.*, p. 176.

²⁸⁴ *Ibid.*, p. 177.

²⁸⁵ *Ibid.*, p. 177.

stabilisation clauses are referred to national courts or regional human rights courts, and although these have proven effective in certain cases “reliance on human rights courts does not address satisfactorily the issue of fragmentation of international law: it is only a partial answer to the problem of conflicting obligations imposed on the host state, or to incentives pointing in the opposite direction”.²⁸⁶

5.2.5 Stabilisation Clauses, Legal and Reputational Risks

Having looked at plausible conflicts with international human rights law arising from the use of stabilisation clauses, it might be worth noting that the parties of the contract may face legal risks for such violations of human rights.

As has already been mentioned, the legal risks facing the host state are much larger than for the investor. This is due to the long history of human rights being a state-matter only, and the well-established obligation imposed on states to respect, protect and promote human rights – including in relation to third parties such as foreign investors. In relation to the host state those affected by the investment have the possibility of turning to domestic or regional courts. In relation to the investor, on the other hand, the matter becomes more complicated. Indeed, legal liability may arise in a situation “where preventable human rights violations take place in an area where legal protections have been demonstrably weakened by a stabilisation clause”, or if an investor with reference to a stabilisation clause forces a poor state to pay due compensation with the result of human rights violations.²⁸⁷ However, the following quote demonstrates that it is highly unlikely for a corporation to actually face legal responsibility for corporate-related human rights abuses:

...there are no known judicial or arbitral cases that have considered the issue of direct liability on the part of investors or lenders for human rights violations resulting from the enforcement of stabilisation clauses...²⁸⁸

One must keep in mind that although the legal risks appear to be minimal, an investor not respecting human rights in the host state to standards adhering to international law may face reputational risks or deviate from voluntary measures through such actions. Reputational risks, to mention a few, may include; negative press; brand erosion following activists campaigns; loss of right to operate in a social and political context, resulting in higher costs, community animosity and non-cooperation by the government of the home state; and negative impact on future business opportunities.²⁸⁹ Moreover, voluntary measures such as the OECD Guidelines for Multinational Enterprises often consider violations of human rights due to the inclusion of stabilisation clauses a deviation from good practice.²⁹⁰

²⁸⁶ Ibid., p. 178.

²⁸⁷ United Nations Global Compact, the Human Rights and Business Dilemmas Forum, *Dilemmas and Case Studies: Stabilisation Clauses - Risks to Business*, United Nations, Retrieved 2011-11-30, <http://human-rights.unglobalcompact.org/dilemmas/stabilisation-clauses/>.

²⁸⁸ Ibid.

²⁸⁹ Ibid.

²⁹⁰ Ibid.

5.3 Stabilisation Clauses and the UN Guiding Principles

5.3.1 Stabilisation Clauses and the Corporate Responsibility to Respect Human Rights

For corporations, the endorsement of the UN Guiding Principles has marked a new beginning in relation to human rights. Voluntary initiatives on the promotion of human rights have been an integrated part of the business sector for long, and corporate responsibility has played a role in the work on the integration of business and human rights. However, what differentiates the UN Guiding Principles from other measures in the area is how they indicate a new paradigm in the relationship between business and human rights.

Whilst the UN Guiding Principles remain voluntary and merely impose a responsibility – not a duty – on corporations to respect human rights, they nevertheless impose an extensive requirement on businesses to change their operational standards. The effects of the UN Guiding Principles rely on the incorporation of human rights in all businesses:

Council endorsement of the Guiding Principles, by itself, will not bring business and human rights challenges to an end. But it will mark the end of the beginning: by establishing a common global platform for action, on which cumulative progress can be built, step-by-step, without foreclosing any other promising longer-term developments.”²⁹¹

The UN Guiding Principles and the corporate duty to respect human rights require corporations to “do no harm” and although the corporate responsibility remains independent of the state duty, actions taken by a corporation may not undermine the ability or willingness of the state.²⁹² From this perspective, it appears as if the interest to secure an investment is stronger than the will to ensure it contributes to human rights, and “states sometimes accept sweeping stabilization clauses, along with other terms that appear to tilt the project in favour of the investor”.²⁹³ The concern, as a result, is that “investor protections may wrongly infringe on state duties and investor responsibilities toward human rights”.²⁹⁴

Still, the UN Guiding Principles are intended to create “a global standard for preventing and addressing the risk of adverse impacts on human rights linked to business activity”²⁹⁵ and calls upon all business enterprises to take action

²⁹¹ United Nations, *Guiding Principles*, 21 March 2011, p. 5.

²⁹² United Nations, “*Protect, Respect and Remedy*” Framework, 7 April 2008, p. 17.

²⁹³ Schemberg, Andrea, *Stabilization Clauses and Human Rights – a research project conducted for the IFC and the UN Special Representative to the Secretary General on Business and Human Rights*, March 11 2008, p. 5.

²⁹⁴ *Ibid.*, p. 10.

²⁹⁵ Office of the High Commissioner for Human Rights, *Your Human Rights: Human Rights Issues – Business and Human Rights*, United Nations, Retrieved 2012-11-23, <http://www.ohchr.org/EN/ProfessionalInterest/Pages/InternationalLaw.aspx>.

disregarding where or how they operate.²⁹⁶ Furthermore, special attention is called upon where foreign direct investment may have an impact on groups more at risk for adverse human rights impact, including women, children, indigenous people, minorities and disabled as well as migrant workers.²⁹⁷

In relation to stabilisation clauses this becomes especially interesting: if corporations are to do no harm – especially in cases where the risk of adverse human rights impact is large – it may be questioned how the inclusion of stabilisation clauses forbidding or limiting the ability of the host state to change human right laws can remain a common element of state-investor contracts where the host state is a developing country?²⁹⁸

5.3.2 Stabilisation Clauses, Human Rights Due Diligence and Responsible Contracts

The question just posed is closely connected with the concept of human rights due diligence as an essential component in the fulfilment of the corporate responsibility to respect human rights. Human rights due diligence is intended to ensure investors are aware of human rights risks prior to the initiation of a project, and allow for measures to be taken to avoid such risks. It includes to “identify, prevent, mitigate and account for” adverse human rights impacts and “assessing actual and potential human rights impacts, integrating and acting upon the findings, tracking responses, and communicating how impacts are addressed.”²⁹⁹ Through such a process, adverse human rights impacts caused directly or indirectly by a specific project are to be identified and, hopefully, avoided even before the initiation of a project.

Stabilisation clauses, on the other hand, are intended to ensure a stable legal setting for a long-term investment and in doing so may include limiting or requiring compensation for changed in laws. Whilst one may agree it is legitimate, and even necessary, for an investor to seek protection against arbitrary changes in law for the entire duration of a long-term investment, “stabilisation clauses that freeze laws applicable to the project or create exemptions for the investor with respect to future laws” are highly unlikely to fulfil the requirements of human rights due diligence.³⁰⁰ The inclusion of stabilisation clauses on human right laws do, in fact, stand in direct contrast with the entire concept of applying human rights due diligence on foreign direct investments.

Again, the negative impacts may be significantly higher in a developing country and it only seems reasonable to argue that the need for human rights due diligence identifying possible adverse human rights impacts is greater for such

²⁹⁶ United Nations, *Guiding Principles*, 21 March 2011, p. 20 (See Guiding Principle 23-24).

²⁹⁷ United Nations, *Guiding Principles*, 21 March 2011, p. 13-14 (A. Foundational Principles).

²⁹⁸ Schemberg, Andrea, *Stabilization Clauses and Human Rights – a research project conducted for the IFC and the UN Special Representative to the Secretary General on Business and Human Rights*, March 11 2008, p. 17.

²⁹⁹ United Nations, *Guiding Principles*, 21 March 2011, p. 16 (Guiding Principle 17).

³⁰⁰ United Nations, *Principles for Responsible Contracts*, 25 May 2011, p. 12, see key implications of Principle 4 for the negotiations.

investments. Guiding Principle 18 stresses that the very purpose of human rights due diligence is to “understand the specific impacts on specific people, given a specific context of operations” in order to shape the project after these specific needs already in the initial stages of the process.³⁰¹ Yet, stabilisation clauses covering human right laws are more likely to be included in state-investor agreements where the host state is a developing country.³⁰²

In relation to the UN Principles for Responsible Contracts, and the on-going discussion on stabilisation clauses and human rights due diligence, it is worth mentioning Principle 4 again:

Contractual stabilization clauses, if used, should be carefully drafted so that any protections for investors against future changes in law do not interfere with the State’s bona fide efforts to implement laws, regulations or policies in a non-discriminatory manner in order to meet its human rights obligations.³⁰³

Still, stabilisation clauses doing the exact opposite are a commonly included element in state-investor agreements where the host state is a developing country. The Principles also concludes, “the laws, regulations and standards governing the execution of the project should facilitate the prevention, mitigation and remediation of any negative human rights impacts throughout the life cycle of the project.”³⁰⁴ Also in this respect, the use of stabilisation clauses - where irresponsibly included in state-investor agreements - appears to contradict the intention with the UN Guiding Principles.

³⁰¹ United Nations, *Guiding Principles*, 21 March 2011, p. 16 (Guiding Principle 18).

³⁰² Schemberg, Andrea, *Stabilization Clauses and Human Rights – a research project conducted for the IFC and the UN Special Representative to the Secretary General on Business and Human Rights*, March 11 2008, p. 32. See also footnote number 54 on the same page, referring to certain areas and countries where the use of stabilisation clauses covering social and environmental laws is most prominent.

³⁰³ United Nations, *Principles for Responsible Contracts*, 25 May 2011, Principle 4.

³⁰⁴ *Ibid.*, see especially Principle 3.

6 THE CONTINUING USE OF STABILISATION CLAUSES: AN ANALYSIS

From what has been described above, it has become obvious that the adverse human rights impacts of irresponsibly applied stabilisation clauses stands in direct contrast with the concepts of corporate responsibility to respect human rights, human rights due diligence and responsible contracts. This Chapter provides an analysis of the above, but also a different perspective on the matter is provided for.

6.1 A Different Perspective

This section will discuss a different perspective on foreign direct investment and human rights, focusing especially on the example of Liberia. Following this section a further analysis and continuing discussion on a different perspective on the topic will be provided.

6.1.1 Considering Human Rights in the Drafting of Stabilisation Clauses

When an investment is made in a developing country the financial and legal risks are undoubtedly higher, and the need for inclusion of stabilisation clauses may be inevitable to mitigate the risks of expropriation or other factors relevant for the success of a project.

We must not forget that although a corporate responsibility to respect human rights is established by the UN Guiding Principles, this does not remove the obligation of states in relation to human rights. After all, the primary duty remains with the state and in relation to most international efforts to truly integrate business and human rights – including the UN Guiding Principles - success “depends on good governance at the international level and on transparency in the financial, monetary and trading systems”³⁰⁵ One may wonder, therefore, if the continuing use of stabilisation clauses having a negative impact on human rights is to blame on corporations, or rather the host state accepting these clauses?

Regardless of this, it appears as if there is a general consensus that “depending on the way the stabilization clause was drafted, it may have the potential to unduly constrict the policy space States need to meet their human rights obligations”.³⁰⁶ In this sense the use of stabilisation clauses is incompatible with the corporate responsibility to respect human rights *and* the state duty to protect human rights. For this very reason it must be noted that where the investor as well as the host state consider it necessary for the investment, stabilisation clauses can be used – but only if done so carefully. Investors are thus encouraged to ensure that if stabilisation clauses are used they:

³⁰⁵ United Nations General Assembly, *UN Millennium Declaration*, UN doc. A/RES/55/2, United Nations, New York, 18 September 2000, p. 4.

³⁰⁶ United Nations, *Principles for Responsible Contracts*, 25 May 2011, p. 13.

...should not contemplate economic or other penalties for the State in the event that the State introduces laws, regulations or policies which: (a) are implemented on a non-discriminatory basis; and (b) reflect international standards, benchmarks or recognized good practices in areas such as health, safety, labor, the environment, technical specifications or other areas that concern human rights impacts of the project.”³⁰⁷

6.1.2 Foreign Direct Investment without Stabilisation Clauses: the Example of Liberia

Whilst the use of stabilisation clauses appear to be a threat to human rights, especially for state-investment agreements with developing countries, it must be recalled that the exclusion of stabilisation clauses from such contracts does not automatically ensure the fulfilment of human rights.

Liberia is an excellent example of a developing country working hard to attract foreign direct investment as a means for economic development. A country still suffering from fifteen years of civil war with nearly 95 per cent of the population living on less than US\$2 dollars per day, Liberia is one of the poorest countries in the world despite its natural resources.³⁰⁸

Under the leadership of President Ellen Johnson-Sirleaf a number of measures to attract investors, including; transparency in management; professional negotiation practices for investments and; socially responsible development policies for concession have been adopted and foreign direct investment is a “cornerstone of its strategy to reduce poverty and grow the country’s economy.”³⁰⁹ However, whilst foreign direct investment has become a significant income for Liberia and “promises economic growth and prosperity it also irreversibly alters the lives of those who live within or near project areas.”³¹⁰

In a short period of time, the government of Liberia has signed a number of investment agreements with foreign investors, allowing the extraction of natural resources on land amounting to nearly half of the total landmass of Liberia, an estimate of US\$19 billion dollars in project investment, and around US\$2 billion dollars in tax income and revenues for the Liberian government.³¹¹ Foreign direct investment is expected to benefit the Liberian nation as a whole, and several of the investment contracts indeed require the investor to fund development projects on a local level, to provide for education, health-care and housing and to hire a certain number of locals for top-positions within the project.³¹² However, despite the promises made in the negotiations of the contracts, real-life examples have proven quite the opposite.

³⁰⁷ Ibid., p. 12, see key implications of Principle 4 for the negotiations.

³⁰⁸ Lanier, Frazer, et.al, *Smell-No-Taste – The Social Impact of Foreign Direct Investment in Liberia*, Center for International Conflict Resolution, Columbia University – School of International and Public Affairs, New York, January 2012, p. 10.

³⁰⁹ Ibid., p. 5.

³¹⁰ Ibid., p. 6.

³¹¹ Ibid., p. 10.

³¹² Ibid., p. 11.

An example of this is the Sime Darby Palm Oil Investment. In 2009, an investment agreement was signed for the 62-year project for palm oil in an area of 220,000 hectares between the government of Liberia and the Malaysian corporation Sime Darby.³¹³ The investment is extensive – both in quantity and in length – and Sime Darby is considered to be “the most controversial concessionaire presently operating in Liberia” receiving negative critique “unmatched by any concession in present” from locals as well as from the international community.³¹⁴

The critique is not a result of the inclusion of stabilisation clauses in the agreements governing the investment but rather a result of promises on development and improvements never being fulfilled. Instead, the project has received much critique with regards to land rights and environmental impact.³¹⁵ To simply exclude stabilisation clauses from state-investor agreements does, therefore, not automatically mean a project will be beneficial for further development in the host state.

6.2 Inevitable Tradeoffs

Having looked at the example of Liberia, and the continuing failure to meet human rights obligations despite the exclusion of stabilisation clauses in state-investor agreements, the question arises if a certain amount of detrimental effects resulting from foreign direct investment is inevitable. The normative framework on international human rights law and the state obligations thereby imposed raise a number of questions concerning the future integration of human rights and foreign direct investment, and the suggestions presented in recent years for this integration to occur present a dilemma on their own. For the host state, the dilemmas include “how to manage tradeoffs when the arrival of FDI creates winners as well as losers, and how to reconcile the participation of local communities in determining the conditions according to which investment should be allowed to proceed with other values.”³¹⁶

The tradeoff-dilemma is related to having to balance the interests of the investor and provide a secure setting for an investment to take place, whilst also fulfilling human rights obligations.³¹⁷ A specific project may bring a number of positive and desirable effects, including improvements with regards to human rights, to a certain community for a certain period of time. But the very same project may also result in negative impacts for others, or for a certain amount of time. However, allowing for foreign direct investments only in cases where it is

³¹³ Ibid., p. 18.

³¹⁴ Lanier, Frazer, et.al, *Smell-No-Taste – The Social Impact of Foreign Direct Investment in Liberia*, Center for International Conflict Resolution, Columbia University – School of International and Public Affairs, New York, January 2012, p. 38.

³¹⁵ Ibid., see for example p. 26.

³¹⁶ De Schutter, Olivier, et. al., *Foreign Direct Investment and Human Development – the Law and Economics of International Investment Agreements*, Routledge, New York, 2013, p. 179.

³¹⁷ Ibid., p. 180.

bringing positive effects “would be neither realistic nor desirable”.³¹⁸ Instead, one may argue, it must be ensured that the positive impacts of foreign direct investment outweigh the negative ones. Still, one must be realistic in that “transition costs are an almost unavoidable part of the arrival of FDI: in the short term at least, and prior to the adoption of compensatory measures, there will therefore be losers.”³¹⁹

6.3 The Dilemma

As of today, many believe that “foreign investment would not be possible in many parts of the world without stabilisation clauses”, and that clauses ensuring a certain degree of legal as well as financial stability are necessary to ensure raised costs due to social and environmental legal implementations.³²⁰ This not only suggests there is a need to create regulation ensuring the required stability otherwise, but clarifies that the general view of foreign direct investment and social impacts are considered two completely different areas to be dealt with. When the inclusion of stabilisation clauses is motivated by financial factors, the social impacts are simply neglected.

One would argue that this is the natural course of business. As expressed by Milton Friedman, the business of business should be to increase profits – not to engage in social matters.³²¹ This would put pressure on the host state to ensure stabilisation clauses posing a threat to human rights are not included in state-investor agreements. It is here the disparity between developed and developing countries becomes significant, for one cannot expect a developed country working hard to attract foreign investment as a means for economic development to require stabilisation clauses to be excluded from an agreement, and thereby risk to lose the entire investment. Many developing countries are taking significant steps toward the further integration of business and human rights, and are doing so without having to compromise with attracting foreign investors. But as expressed by the President of Liberia, there is a difficult task of balancing the interests of all stakeholders:

When your government and the representatives sign any paper with a foreign country, the communities can't change it ... You are trying to undermine your own government. You can't do that. If you do so all the foreign investors coming to Liberia will close their businesses and leave, then Liberia will go back to the old days.³²²

³¹⁸ Ibid., p. 180.

³¹⁹ Ibid., p. 180.

³²⁰ Schemberg, Andrea, *Stabilization Clauses and Human Rights – a research project conducted for the IFC and the UN Special Representative to the Secretary General on Business and Human Rights*, March 11 2008, p. 5.

³²¹ Friedman, Milton, *The Social Responsibility of Business is to Increase its Profits*, New York Times Magazine, September 13, 1970, p. 5.

³²² Republic of Liberia President-elect Ellen Johnson-Sirleaf, speaking to rural, indigenous community members affected by the operations of Sime Darby, December 6, 2011. See S. Kpanan Áyoung Siakor and R. Knight, *A Nobel Prize Laureate's Problem at Home*, The New York Times, 20 January 2012, retrieved 2012-12-08, <http://www.nytimes.com/2012/01/21/opinion/in-liberia-a-nobel-laureates-problem.html>. See also De Schutter, Olivier, et. al., *Foreign Direct Investment*

Although the quote concerns governmental relations, the same is applicable to state-investor agreements.

How, then, is the use of stabilisation clauses to be aligned with human rights without forcing developing countries to lose the momentum of possible financial improvements? In answering the research question of this paper, reflections such as this are numerous. Having looked at the above, it appears as if not all forms of stabilisation clauses should be found illegal, but rather that there is an urgent need for all stakeholders involved in projects where stabilisation clauses are used in a detrimental manner to realise that an alternative must be found.

7 CONCLUDING REMARKS

This paper does by no means amount to suggesting a solution or an alternative to the current situation - this would require materials and resources simply out of reach. However, the fact that human rights – even the very basics of those rights internationally recognized – are not respected is simply not acceptable.

Since the introduction – and recognition on a global level – of a corporate responsibility to respect human rights in the UN Guiding Principles last year, this is truer than ever before. The UN Guiding Principles are a step in the right direction, but as we have seen there is a general weakness in that they are not legally binding. After all, the *responsibility* imposed upon the corporate sphere remains a responsibility only. The following quote presents the true dilemma:

Business is the major source of investment and job creation...they constitute powerful forces capable of generating economic growth, reducing poverty, and increasing demand for the rule of law, thereby contributing to the realization of a broad spectrum of human rights. But markets work optimally only if they are embedded within rules, customs and institutions...and escalating charges of corporate-related human rights abuses are the canary in the coal mine, signalling that all is not well.³²³

The continuing use of stabilisation clauses are certainly part of the issue, and from the above it has become clear that such clauses – if used inappropriately – may have detrimental effects on human rights.

It is no surprise, therefore, that stabilisation clauses are surrounded by a certain degree of controversy. Whilst the continuing use of such clauses is justified by a number of reasons, it remains difficult to grasp how such clauses can be accepted when limiting development in areas of human rights. Once again, it is important to recall that business indeed can be a positive force, and may contribute to development in all forms if carried out with human rights in mind. The UN Guiding Principles form an important part of the further integration of business and human rights, but are a weak instrument in relying on voluntary measures. Whilst voluntary initiatives are inspiring and important forces for human rights and development, the realisation of human rights on an international level may not be left in the hands of those who may chose otherwise.

The research conducted for this paper has demonstrated a lack of understanding or willingness to take a different approach to mitigate risks related to foreign direct investments amongst investors and states alike, and whilst the use of stabilisation clauses has nearly vanished from foreign direct investment in developing parts of the world they remain a constant and on-going threat to human rights in developing countries.

It seems reasonable to conclude that there is a reason for why stabilisation clauses are applied in this manner. Indeed, the regulatory bodies governing foreign direct investment may be stronger in a developed country, thus removing the need for stabilisation clauses. However, the disparities in use of

³²³ United Nations, “*Protect, Respect and Remedy*” Framework, 7 April 2008, p. 3.

stabilisation clauses may also be explained by the fact that developed states are simply unwilling to limit their sovereignty in such a manner and possess the power to negotiate the terms of the investment agreement that a developing country may lack.

These reasons for this disparity in use of stabilisation clauses in developed and developing parts of the world may have many other explanations, but pinpoints the need for something to be done. It appears as if the challenge facing the international community is to ensure that measures to attract foreign investors are not allowed to infringe on human rights, and create an international framework regulating their use.

Whilst the UN Guiding Principles, and similar initiatives, are admirable attempts to do so further measures are necessary to create a global market where the positive effects of foreign direct investment are distributed more equally, and where it is allowed to contribute not only to economic development but also to the development and improvement of human rights. To simply put the blame on investors may be an easy way out, but one must not forget that there are several different interests pulling in different directions involved in the dilemma. For an investor must be able to secure an investment, or the investment cannot be made at all.

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