GLOBAL LEAGUE: BUSINESS GROUP

Chair person: Wanderley Fernandes (GV Direito SP)
Ana Viterbo (Università di Torino)
Azam Rifat (IDC Herzliya)
Daniel de Andrade Levy (GV Direito SP)
Eli Bukspan (IDC Herzliya)
Francisco Elíasalde Ibarbia (Instituto de Empresas – Madrid)
Gianmaria Ajani (Università di Torino)
Heloisa Slav (GV Direito SP)
James Speta (Northwestern)
Lie Uema do Carmo (GV Direito SP)
Lior Zemer (IDC Herzliya)
Lorenza Mola (Università di Torino)
Luiz Barreto Xavier (Faculdade de Direito – Univ. Católica de Lisboa)
Marco de Benito (Instituto de Empresas – Madrid)
Maria Lúcia Pádua Lima (GV Direito SP)
Michael Nietsch (EBS Law School)
Paulo Goldshmidt (GV Direito SP)
Zeynep Ayata (KOÇ University)
Zeynep Derya Tarman (KOÇ University)

PROJECT INVESTMENT AND DEVELOPMENT

General introduction:

Following the instructions of the Global League Committee, we opened the opportunity for suggestions of new topics to be developed by our Business Group. We, then, collected ideas, which, in principle, seemed to be too broad and diverse to be unified in just one work.

After several interactions among the members of our group, including in our preparatory meeting in Madrid, we reached the conclusion that, despite the initial diversity, we could find the “unitas multiplex”. In 2013, we were called by the committee to think about protection of direct investments and, as our first work, in 2014, we researched and prepared a report about the enforcement of arbitration decisions in our respective jurisdictions. Therefore, we have decided to revisit the origin of the purpose of our group.
Differently from our last work, when professors from different countries prepared each report. We reached the conclusion that we should promote more integration within the group.

We, then, realized that we could unify all the suggestions under a umbrella which we nominated as “Investment and development”, what could be simply explained as investments, not only with the purpose of profits, but that could be a source of returns to investors and to the local place of investment.

Just as a matter of example, professors Azam Rifat and Eli Bukspan, from Israel have proposed the corporate social responsibility, what is clearly connected with the idea that investments should take into account and promote development of local places where the project is to be implemented.

The same can be said about the analysis of tradeoffs between direct investments and social human aspects, as proposed by Professor Ana Viterbo. In other words, even when dealing with traditional private law concepts, as liabilities, we intend to focus on how the legal tools may favor development in the context of direct investments.

Therefore, in Madrid, we have structured our work as follows:

**General framework: Investment and development**

- Global value chain concept;
- Governance of the global chain: applicable law, seat of arbitration, liability. Interaction with public policy; interaction with international organizations;
- Risk assessment and mitigation, can financing or insurance players determine/impose the governance of the chain?
- Corporate social liability: the tension between private and public determination about what are the social priorities;
- Social human aspects of direct investments (tradeoffs). The denunciation of BITs as a way to preserve regulatory space: the case of South Africa.
- Investment "determinance": private and public point of view:
  - tax incentives;
  - legal rules (choice of applicable law)
  - economic development and law.

Finally, we ended up with a coherent project to encompass all ideas and provide the chance to all of our members to conciliate their personal academic interests with our general purpose. However, we also
have found out that we had in our hands a huge and challenging project that certainly could not be finished until our academic meeting in Cape Town.

Another aspect of our productive debate in Madrid was a serious concern about effectively creating a sense of group, fostering joint research and activities for such purpose, webinars, co-teaching in different schools, especially in the context of future Academic Meetings of the LSGL. Thus, the natural conclusion was that we could propose a broader project of medium term research, so that we could not only develop more consistent research, but also deliver structured papers to be published separately in relevant law reviews or as chapters of a collective book.

In sum, we have decided to present a research proposal to be carried out by all of us, in separate subgroups, as described below:

- **Global value chain concept**:
  - Maria Lúcia Pâdua Lima (GV Direito SP)
  - Paulo Goldshmidt (GV Direito SP)
  - Daniel Levy (GV Direito SP)

- **Governance of the global chain: applicable law, seat of arbitration, liability, Interaction with public policy; interaction with international organizations**:
  - Francisco Elísalde Ibarbia (Instituto de Empresas – Madrid)
  - Lie Uema do Carmo (GV Direito SP)
  - Wanderley Fernandes (GV Direito SP)

- **Risk assessment and mitigation, can financing or insurance players determine/impose the governance of the chain?**
  - Heloisa Slav (GV Direito SP)
  - Wanderley Fernandes (GV Direito SP)

- **Corporate social liability: the tension between private and public determination about what are the social priorities**:
  - Ana Viterbo (Università di Torino)
  - Azam Rifat (IDC Herzliya)
  - Eli Bukspan (IDC Herzliya)
• Social human aspects of direct investments (trade offs). The denunciation of BITs as a way to preserve regulatory space: the case of South Africa:
  o Lorenza Mola (Università di Torino)
  o Ana Viterbo (Università di Torino)

• Investment "determinance": private and public point of view
  - tax incentives;
  - legal rules (choice of applicable law)
  - economic development and law.
  o Daniel Levy (GV Direito SP)
  o Zeynep Ayata (KOÇ University)

Each subgroup was assigned to present a proposal for the respective subject under the following structure:

- Description of work
- State of art of the subject
- Methodology
- Collection of data
- Expected impact of the research
- Deliverable

This index provides an uniform structure of all the topics referred to above.

Despite the legal focus, our analysis will be placed in the context of non-legal concepts, as value chain and networks. Therefore, before presenting each proposal under the structure above. Professor Maria Lúcia Pádua and Paulo Goldschmidt prepared a text about the economic perspective of value chains which shall be an important reference for our legal analysis.
Global Value Chains: an Introduction

Maria Lucia L.M. Padua Lima  
Paulo Goldschmidt

Contemporary capitalism is characterized not only by intensifying the process of internationalization of economic activity but also by the profound change in the way of organizing production, intra-firm investment & trade relations, between countries, and the peculiar conjunction with the financial sphere. In other words, this stage of capitalist development called globalization has altered decisively the productive structures, technical and social relations of production, the organizational format of transnational corporations, the financing arrangements, and the interaction of productive enterprises with the financial market; the pattern of international investment & trade and consequently the contractual forms derived from these productive profound changes.

There is a convergent understanding among analysts that this new model of capitalism or globalization emerged in the early 80s as a outcome due to the lower transport costs, but especially because of the revolution in the technology to organize and to transmit information; the so-called revolution in information and communication technology (ICT). As a consequence of the ICT revolution, companies have realized that it was possible to spread the production process at various locations to get the highest possible reduction of costs by utilizing advantages of both proximity to raw materials and/or cheaper labor. Authors as Baldwin and Venables call this initial movement as the first unbundling when producers were separated from consumers, the second broke up production entirely across long and multinational value chains. In recent times, this second phase of the unbundling has evolved to separate plants (factories) to the administrative functions (offices) including the various components of the service sector resulting in both the outsourcing and offshoring of these services.

The argument to be developed on this topic is that international agreements between the parties are closely related to this set of changes derived from the so-called globalization process. Therefore, it is necessary to adopt a theoretical interpretation of international business relationship quite different from conventional theory on the subject.

1 Baldwin, R and Venables, A - 2010
2 The Orthodox Economic Theory of Foreign Trade was compiled from the original conceptions of David Ricardo in On the Principles of Political Economy and Taxation first published in 1817. The trade pattern is determined by supply. Therefore, the existing differences in productivity among the countries are the pillar in the international trade. Although changes have been introduced in the Ricardo’s principles, such as the admission of the existence of markets with imperfect competition, the existence of asymmetric information and the possibility of economies of scale distortions, the international trade is
The theoretical basis for this approach is found in the literature dealing with the emergence of a global production system. Thus, we intend to address the changes in the role of transnational companies by analyzing the characteristics and the nature of these changes from the concept of global value chains (GVC). The central hypothesis is that these changes have important consequences in the contractual relations between the various parties that make up the numerous GVC.

According to the GVC approach, economic integration transcends the world trade in raw materials and finished products and comprises an internationally dispersed production process with a central coordination that goes beyond the vertical corporate and national boundaries.

It can be considered that the GVC takes two predominant forms: productive chains controlled by supply (producer-driven) and demand (buyer-driven). In the first case, the manufacturing industry has control of the process (governance) organizing the entire production network (forward and backward linkages). Generally, GVC led by the offer is related to typical activities based on intensive capital and technology. Classic example of this form of organization is the automotive industry that has the automaker controlling the entire network of suppliers, distributors and retailers. Other examples of GVC controlled by supply (producer-driven) are the aeronautical, computers, semiconductors and heavy equipment.

On the other hand, in the GVC led by demand (buyer-driven) the organization's format is given by the closest link to the consumer, in other words, the characteristics of the consumer markets are the determinant factor to the production. For this reason, the major retailers, traders and producers with brands are the controllers of this type of GVC. These GVC usually are related to labor-intensive products and include various consumer non-durable goods - textiles and clothing among them. In this case, the production is often decentralized with plants located in various regions of the world, especially in emerging countries. On the other side, the main markets of these goods are often located in advanced countries. For this reason, these GVC are usually under control of the final players in the process.

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3 In the collection of articles edited by Gereffi and Korzeniewicz (1994) a methodology for analyzing the global production system is developed. The main argument of the authors is that despite the internationalization process - understood as the geographical dispersion of economic activity - has started in the seventeenth century, globalization is a contemporary phenomenon that involves the coordination and integration of internationally dispersed economic activities. From this emerges the coordination and integration of global production system. Other important works within this line of argument are: Amin and Theriff, 1994; Conti, 1995; Gereffi, 1994; Gereffi and Korzeniewicz (ed.), 1994; Gereffi, 1999; Stallings, 1995; Massey, 1997; Kaplinsky, 1998.

4 The global supply chain concept considers four dimensions: 1) integration of inputs-product flows between industries; 2) territorial coverage; 3) governance structure; 4) Local institutional framework, national and international

5 Gereffi, 1994 and 1999
The organization of distribution channels controlled by supply (Producer-Driven) and demand (Buyer-Driven) shown in Chart 01 and 02 were originally designed by Gary Gereffi and illustrates the two main types of value chains.

Chart 01 - Global Value Chain led by the Offer: *Producer-Driven*

Source: Gereffi, 1994 and 1999

In the case of GVC driven by supply the high profitability of key players is assured due to the barriers to entry, meaning the high technology, scale and the huge investments needed in this type of GVC. On the other hand, the lower profitability activities are outsourced through contracts based on very precise

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6 Arrows with solid lines indicate direct relationships and dashed arrows point indirect relations
specifications dictated by the chain controller. The key players of this type of GVC are usually large transnational corporations that operate in oligopolistic way.

Regarding GVC driven by demand the profitability of drivers comes from the peculiar combination of elements such as design, marketing, knowledge of consumer preferences and financial services that give those drivers the ability to dominate the mass consumption through wide appeal brands and the establishment of special conditions of supply on a global scale.\(^7\)

The most important conclusion is that in the GVC driven by supply or by demand the key element to earn extraordinary income internationally is the ability of the chain controllers to establish and maintain barriers to entry. Due to the fact that the controller chain dominates the technological process in the first case and in the second the organizational process.\(^8\)

The governance structure of the GVC has been the most prominent dimension because it is considered crucial to establish the controlling agent. Only after this determination is it possible to classify the type of supply chain: producer-driven or buyer-driven. Secondly, given the type of agent that drives the chain it is viable to analyze the forms of barriers to entry and conditions imposed for participation in GVC.

In the specific case of this study, the existing governance type of establishment in a given GVC is an important element in understanding the allocation of guarantees and risks among participants of the GVC.

Last but not least, the identification of key players is crucial both in the discussion of the influence of these in the formulation of rules that make up the institutional apparatuses (local, national and international), as the issue of economic development.\(^9\) In relation to this last point it is also worth mentioning that as the GVC is the organizational basis for participation in international investment & trade, the possibility of improvement in the form of external insertion of the developing countries depends on participating in these chains.\(^10\)

However, if being part of the GVC is a necessary condition for country development, this participation is not sufficient. In order to a developing country to move from the condition of simple assembler of imported inputs (associated with export platforms) and become a producer of goods for export (Original

\(^7\) Gereffi, 1994
\(^8\) Kaplinsky, 1998
\(^9\) The key player has the control of the decisive elements for the privileged participation in international trade such as intellectual property, brands, relationship with consumers and product differentiation. Gereffi and Korzeniewicz (ed.), 1994
\(^10\) Gereffi, 1999
Equipment Manufacturing - OEM) and finally reach the most developed stage of producing private label goods which are internationally recognized (Original brand Manufacturing - OBM), the country must have the ability to learn and establish special links with key actors of the GVC\textsuperscript{11}. (chart 03)

Chart 03: Upgrading on the GVC

The GVC approach contributes to understand the current institutional apparatus (local and global) and also the changes that have been occurring in the rules of international investment & trade. In addition, this approach can offer a new procedure to analyze the contractual practices between the parties participating in the GVC.

It is possible to visualize the concentration power over the global value chains by transnational firms and the simultaneous trend of production process fragmentation and consequent geographical dispersion using chart 03 (below).

\textsuperscript{11} Gereffi uses the example of Japan in the 50s and 60s, the Asian countries of recent industrialization in the 70 and 80 and China in the 90 to demonstrate the possibility of rise in international trade and economic development. Gereffi, 1999
The fragmentation of production in many levels allocated in different countries could assume different forms. Baldwin and Venables (2010) described these forms as “snakes” and “spiders” as showed below (chart 05). The Spider form symbolize the multiple parts that are assembled to compound a final product or a component for a final product. The Snake shape represents a movement in a sequential manner from different stages of the production process in diverse firms and/or countries with value added at each stage.

Chart 05 – Spiders and Snakes
After the development of the World Input-Output Database\textsuperscript{12} it is possible to measure the value added in the global value chains or as Krugman\textsuperscript{13} said it is possible “to slice up the global value chain”. Timmer, Erumban, Los, Steher and de Vries \textsuperscript{14}, based on the World Input-Output Database information, discussed the impact of the fragmentation production process in the trade and cross-border investments and their consequences for the development and well-being of participating countries. They also concluded that further studies should be done to analyze the effects of this new capitalism phase characterized by the global value chains.

It can be said that from the adoption of the GVC approach it is possible to understand better the complexity of contracts demanded by the numerous parties involved in the production processes dispersed all around the world.

For this reason, this group decided to explore the adoption of this approach by analyzing international contracts.

\textsuperscript{12}World Input-Output Database was developed by the official WIOD Project, funded by the European Commission http://www.wiod.org/new_site/home.htm

\textsuperscript{13}Krugman, P (1995)

\textsuperscript{14}Timmer, M.P.; Erumban, A.A; Los B.; Steher, R. and de Vries, G.J. (2014)
INVESTMENT AND DEVELOPMENT

Governance of the global chain: applicable law, seat of arbitration, liability, Interaction with public policy; interaction with international organizations

Global Researchers:
Prof. Francisco Elías de Ibarbia (Instituto de Empresas - Madrid)
Prof. Lie Uema do Carmo (GV Direito – SP – São Paulo)
Prof. Wanderley Fernandes (GV Direito SP – São Paulo)

1. Description of work:

Value chains or networks, stable or dynamic ones, are not legal concepts. However, they may be organized through contracts or organizations, which are legal structures typified, or not, in different jurisdictions.

In such context, the jurist may find some “legal irritations” (in the words of Gunther Teubner), when traditional corporate and contract law does not provide straightforward regulation to deal with such phenomena. We can observe hybrids forms of business organization, as for instance, alliance contracts, strategic alliances, consortium, master agreements or even peculiar forms of associations or legal entities.

Besides organizational structures, we also face some challenges to align the appropriation of gains and risks, through the chains and networks. It is frequent to observe that the value is captured by the top of the chain, when a relevant organization has the power to determine the “governance” of such business model. On the other hand, the liabilities are concentrated in the bottom of the chain.

The issue is more critical in trans border chains, where the applicable law or place of arbitration or judicial disputes may create another barrier for fair allocation of risks.

Can international organizations take a relevant role on such issues, or the market is enough? Contract or corporate law can provide adequate tools? Is it possible to recognize a contractual governance of such dynamic networks?

2. State of art:

In 2012, Emily M. Weitznboeck, a professor from University of Oslo, has published a book with a suggestive title which has a very close proximity to our inquiries: A legal framework for emerging business models. Dynamic Networks as collaborative contracts. She analyses contractual and corporate rules do deal with the same challenges we are concerned with. She focuses, however, in the structures and organizational aspects. She also makes clear that her work is essentially dedicated to private law.

We believe we can take one step ahead.

We also would like to research the role of the international organizations and the effect of the
distribution of gains, liabilities and risks through the chain/network to promote local development of the countries where direct investments are placed.

3. Methodology

As an international cooperation, we will play in a similar functioning of a dynamic network. Professors from different countries with capabilities to carry out a specific subject. Therefore, comparative law tools will be relevant to determine our research procedures.

In additional to legal literature, we will certainly take advantage of the participation of economists in our group to bring a multidiscipline view of our subjects.

We also intend to develop empirical studies to evaluate how the chains and networks are governed in the real word. There are several case studies already published, but we would like to choose some economic activities to be the source of information and tests of our findings. Confidentiality of certain agreements shall be an important barrier, but we believe that, at least, the descriptive data about certain chains may be a valuable source of inputs to our studies.

4. Collection of data

Research in academic websites, websites of universities, and international organizations will be a relevant source of information.

International organizations and chambers of commerce are also a qualified locus of data.

Additionally, we expect to obtain information from direct inquiries and interviews with market agents, and lawyers dealing with international contracts and organizations.

5. Expected impact of the research

As referred to above, we believe we can take some steps ahead in the study of value chains and networks. Therefore, our work may be a contribution to mitigate the “legal irritations” caused by hybrid forms of business organizations. One contribution about the phenomena that has broken the dual category of hierarchy and contracts.

The umbrella subject of “investment and development” will also guide us to keep always in mind that private law shall have a social impact where the development takes place. Therefore, we believe that, even if we do not bring all the answers, we can, at least, call the attention of jurists to the right issues and questions to be addressed.

6. Deliverables

We intend to promote some webinars debates and present to the whole Global League our findings. We expect to have partial results in the form of working papers to be discussed by the group through skype or other media.

Such works would have restricted disclosure and be the basis for further development.

We intend to have a final paper to be published in relevant law reviews or to be part of a joint book of the final results of the whole business group.
INVESTMENT AND DEVELOPMENT:
Risk assessment and mitigation, can financing or insurance players determine/impose the governance of the chain?

Researchers:
Heloisa Slav (GV Direito SP)
Prof. Wanderley Fernandes (GV Direito SP)

1. Description of work:

The concept of value chain encompasses the complete scope of certain markets and the agents involved in the process of manufacturing and marketing products. From the less processed commodities until the production of high technology software and applications.

Each member of this network has a link with the next node of the web, in order to make feasible the businesses carried out through the chain. Step by step the products are transformed, and the legal connection of each agent is modified accordingly.

We have decided to follow this flow of products and links, analyzing the risks and gains and their necessary connections with legal structures. The market to be under our scrutiny will be the agribusiness. Nothing more simple as the phrase “from farm to market”, as moderns cities organize organic fairs where farmers sell fresh vegetables directly to consumers. This, however, is the exception. The agribusiness is quite more complex and entails intricate embroidery of contracts and relationship.

Just as a reference, the transnational or cross-border markets of soybean could be graphically depicted as follows:
The flowchart above shows how the legal relationship among the agents of this web is transformed from the very beginning, including a comprehensive scope of activities and agents involved in the movement and transformation of products within the chain, since the inputs supply phase, production, transportation, storage, commercialization, industrialization, distribution and consumption.

There is a very specific and detailed design of contractual relationships, with sophisticated system of guarantees, financing structures, bond issuances, and monitoring of the behavior of each protagonist of each phase of the value chain.

The purpose of our work is analyzing how legal framework can play an efficient role to promote creation of wealth and fair distribution of risks, gains, and liabilities.

2. State of art:

There are some studies to understand the agricultural value chain, but they are mainly related to the financing tools and mechanisms. Most of them are related to banking preoccupation to provide incentives to production, but with adequate guarantees to their loans. Agriculture is the activity most exposed to the nature. Climate changes, natural disasters are part of this equation. Who is the best risk bearer for such events?

There are some important researches promoted by international organizations, but most of them, related to business aspects of the value chain. Our intention is to dive in such market and analyze how contracts and other legal tools may be an important element of development.
3. Methodology

We intend to develop our work in the following path:

Step 1: collect all available material in the website of international organizations regarding the agribusiness market;

Step 2: interviews of market players, starting with farmers. Traditional families owning real countries inside a country and small farmers producing subsistence agriculture;

Step 3: interviews of traders, like Bunge, ADM, Dreyfuss, etc;

Step 4: interviews of bankers and insurers.

Step 5: analysis of the legal connection (contracts) between each node of the web, and evaluation of how the market distributes risks, liabilities, and gains through the web.

4. Collection of data

As referred to above, the collection of data will be made through field research, interviewing market agents and analyzing real contracts.

We will also take advantage of surveys promoted by international organizations and articles published by relevant universities.

It is important to observe that there is very poor legal literature regarding this matter, and, therefore, we do not intend to improve the state of art, but simply contribute to promote research about the agribusiness issues.

5. Expected impact of the research

Alimentary safety, climate changes, land disputes, etc. These are global issues with strong impact of legal regulation about how countries can control the exploitation of their natural resources.

In Brazil, for instance, the government reacted issuing a resolution limiting acquisition of rural areas by foreign persons and entities.

USA, China, Russia, Brazil, India and other continental countries have an important source of wealth from natural agricultural resources. However, it seems that the academia has been much more concerned about high tech businesses than with the exploitation of nature. Jurists have neglected literature about agricultural law. In our point of view, the agricultural business value chain may be a good starting point to understand how the marked can promote development to countries which are not developed, but provide the nutrients to individuals of wealth nations.

6. Deliverables

In our view, we have a good opportunity to deliver not only the result of our research, that can be an article or a book, but also something even more rich: INFORMATION.

We have some intuition about the matter, but we do not have pre-defined answers. Everything is new, and challenging.
INVESTMENT AND DEVELOPMENT:
Social human aspects of direct investments (tradeoffs). The denunciation of BITs as a way to preserve regulatory space: the case of South Africa.

Researchers:
Prof. Ana Viterbo (Università di Torino)
Prof. Lorenza Mola (Università di Torino)

1. Description of work:

When the current system of international investment law took shape in the second part of the XX century, it was conceived on the political economic premise that only foreign capital could fill the gap between industrialized and developing countries. The aim of the emerging regime was that of fostering the economic development of receiving countries by offering accrued, international protection to capital from exporting countries, through an inter-State deal (i.e., bilateral investment treaties, BITs). This is also the aim of the Convention setting the International Centre for the Settlement of Investment Disputes (ICISD) for international arbitration of investor-State controversies.

Today there is a growing recognition that the conclusion of an investment agreement alone is not capable of influencing foreign investment inflows in a given country, so many affirm that the narrative of BITs being the gateway to development is a myth. Regulatory factors at the national level, such as the protection of property, and economic factors, such as the presence of natural resources and the availability of skills and technology, greatly influence foreign investors' decisions. The impact of international investment agreements (IIAs) on the capacity of a country to attract investments is difficult to assess in isolation.

In parallel, there are increasing concerns over the constraints imposed by IIAs and trade treaties over governments’ room for manoeuvre, especially for what concerns the adoption of social and environmental policies.

These developments prompted some States to opt out from investor-State dispute settlement (ISDS) and denounce the ICSID Convention (Bolivia, Venezuela and Ecuador). Others, like South Africa adopted a new approach. Others, like Brazil have recently acted as new comers into the system, on premises partly similar to the South African approach.

In 2009, South Africa initiated an intensive treaty review program, which led to the decision of terminating its 'first generation' investment treaties (for instance the two with Belgium and Luxembourg, and Spain) and refraining from entering into new BITs, except under certain circumstances. The conclusion of new BITs would be only made on the basis of a new model – currently being finalized - that would reduce the risks inherent in earlier generation BITs.

This decision was accompanied by a vigorous debate over the adoption of a new foreign investment policy framework. The 2013 draft Bill on the Promotion and Protection of Investment was open for public comments until early 2014 and it is now being revised. Should the Cabinet endorse the revised Bill, it will be presented to the South African Parliament in April 2015.
The 2013 draft Bill sought to protect inward investments (post-establishment) by codifying typical BIT provisions into domestic law. Underlining that South Africa has reached a sufficient level of legal stability and development, the Bill offers investors a treatment that largely resembles that offered by BITs, but exclusively provides for recourse to national courts in case of a dispute to arise (South Africa is not a party to the ICSID Convention). In addition, it enshrines the right of the host state to regulate in the pursuit of development goals, as well as to expropriate with the legitimate aim of protecting and promoting public welfare, health and environmental objectives. The Bill intends to achieve a proper balance between the rights and obligations of investors and of the Government, particularly in respect of the Constitutional obligations to safeguard the public interest, while confirming South Africa commitments to an open and transparent environment for foreign investments and to the protection of human rights and of the environment. However, the draft Bill was criticized for not affording enough protection against expropriation, which is subject to a just and equitable compensation aligned with the standards provided in the South African Constitution. Besides, disputes will have to be brought before competent national courts; access to international arbitration will be excluded.

The research will first address the legal effects of denouncing a BIT under international law. In fact it has to be said that the process of denouncing BITs is not as straightforward as it may appears due to the frequent inclusion of so-called “survival clauses”: these provisions extend the enforceability of investors’ rights beyond the lifetime of the treaty, so that its provisions may be invoked before an arbitral tribunal even years after its termination.

The second part of the research will focus on the novelties of the South African “domestic law” approach. In particular, the focus will be on the definition of investment, on the State’s right to regulate and therefore also on the scope of safeguard clauses and on the scope of protection against expropriation. In particular, since the new South African foreign investment and land reform policies are strictly connected (as demonstrated by the ICSID Case Bernardus Henricus Funnekotter and others v. Republic of Zimbabwe as well as by ICSID Case Piero Foresti, Laura de Carli and others v. Republic of South Africa), the research will investigate also this specific profile.

The third part will address other experiences, such as Brazil’s one, in a comparative perspective, in order to draw some conclusions on the main features and implications of the new models of treaty-based development strategies which could affirm themselves at the international level.
INVESTMENT AND DEVELOPMENT

Investment “determinance”: private and public point of view
- tax incentives;
- legal rules (choice of applicable law)
- economic development and law.

Researchers:
Prof. Daniel Levy (GV Direito SP – São Paulo)
Prof. Zenep Ayata (KOC University – Instambul)

7. Description of work:
The legal and conceptual qualification of “investment” is at the centre of this study as it allows the global chain dynamic to gain international protection, one of its most crucial conditions.

Not all investments resulting from a global chain of productions deserve legal protection and not all legal protection results from a global chain investment. We can have purely national investments, or economic investments that do not promote national development, one of the most important conditions of the international Investment system protection.

The very important and original identification of transnational trade practice as a global value chain raises the question whether countries that only receive the first stages of the chain – i.e. supply of primary products – could qualify these “investments” as foreign direct investments (FDI) for the purpose of protection of Bilateral or Multilateral Investment Treaties or Conventions.

Many of the host countries – those receiving FDI and ratifying BITs – are third world or emerging countries that participate in the global chain as primary markets, without really having the chance to preserve any know-how or aggregate any value to its local production. It therefore becomes dubitable whether and how much FDI contributes to the economic development of the country.

Therefore, we could ask: does the transfer of technology or know-how to these primary economies constitute a condition to qualify a FDI? In other words, and in the light of our broader field of study within this group, do all the global chain investment stages deserve international protection within the FDI system? Finally, what are the criteria of an investment to be qualified as a FDI in order to gain protection under BITs or MITs and how the concept of global chains could be extremely useful to assert which stages of a production generates sufficient aggregate value to local economies as a condition for FDI protection.
8. State of art:

The Salini test has provided the most important definition of investment within the framework of the ICSID jurisdiction so far. The test identified three main elements: (i) the existence of contributions in capital or otherwise; (ii) a certain duration; (iii) an element of risk. The decision also added ‘contribution to the economic development of the host state of the investment as an additional condition’ for the qualification of an investment for the purposes of the ICSID Convention (Salini Costruttori S.p.A. and Italstrade S.p.A. v. Morocco (Decision on Jurisdiction, 23 Jul. 2001), para. 52).

The reason why the local development of the host state appeared only as an “additional condition”, is a result of the difficulty of defining the concept of “development” itself, i.e., what kind of wealth transfer is necessary to qualify the strength of a local host economy and its impact on local economic development.

In fact, there is not even a consensus on the criteria of local development. In L.E.S.I. S.p.A. et ASTALDI S.p.A. v. Algeria (Decision, 12 Jul. 2006), another ICSID tribunal found that there is no requirement under the ICSID Convention for the investment to promote economic development (para. 72).

The “economic development” criteria is so controversial that it has been used by arbitral jurisprudence as “a criterion, as a parameter, a characteristic, an element, a requirement, a feature or as a hallmark of an investment” (Nitish Monebhurrun, “The Political Use of the Economic Development Criterion in Defining Investments in International Investment Arbitration”, Journal of International Arbitration, (Kluwer Law International; Kluwer Law International 2012, Volume 29 Issue 5) p. 567).

Thus, even if the economic development of the host state is highlighted by the arbitral jurisprudence and even declared as a goal of the Washington Convention, it still needs to be economically and thus legally defined. This is exactly the focus of our paper and its importance for the global production chain concept as proposed in our Law and Business Group study.

9. Methodology

As our main objective here is to suggest the global value chain as a framework to qualify economic development as criteria of investment protection, it will be essential to draw a parallel between economy and law.

The economic studies on the concept of “Global Value Chains” together with the results of the first subgroup panorama, will give us the economic tools to examine the many investment cases where the “economic development” condition was discussed. This will construct the conceptual part of our study.

At the same time, we need to check each of the arbitral cases, and take advantage of their publicity in order to identify which economic activities are being discussed as FDI and if they would fit in an aggregate value conception within the global value chain. This will be the more
Finally, in a more empirical analysis, it would be very interesting to approach the main market players, as executive and legislative authorities, directors, and actors in multinational companies making FDI, in order to evaluate how their economic decision on shifting part of their production in other countries translate a need to dislocate more basic or complex stages of the production chain. Some interviews would be extremely useful to link the legal and economical perspectives as cited above, and may be facilitated by the multinational nature of our study group.

### 10. Collection of data

The research will be developed in three stages:

- **(i)** Research of the main ICSID awards discussing the “economic development” criteria in order to identify if (a) we may appoint which is the activity that qualifies the investment and if (b) there is any discussion, by the arbitrators, on the aggregate value of this activity as a criteria for the local development and, thus, for the FDI system protection. All the ICSID awards may be available in the ITALAW or the World Bank sites, as they are almost all public;

- **(ii)** Research of the main economic characteristics of the “aggregate value stage” of the global chains in order to try to identify these elements in the above awards.

- **(iii)** Interviews or inquiries with market players in order to identify which parts of the global chain is being transferred to host countries and the importance accorded to the development of local economies through the production of more aggregate value goods to an investment decision.

### 11. Expected impact of the research

This will be the very first time where economic development as criteria to qualify FDI will be studied through the idea of a global value chain. Therefore, depending on the results of these studies, it will be possible to use the different stages of a global value chain and the impact produced in each of them as a real parameter to measure the degree of local development of populations in host economies and, thus, evaluate if these investments deserve the FDI protection system.

The use of an economic concept for a legal qualification may contribute to harmonising divergent conceptions on “economic development” and building a more solid criterion for arbitral tribunals.

In any case, if we can empirically identify how investment decisions are made and which types of activities are dislocated to these emerging or newly emerged economies, we may propose a very concrete element to be considered in future discussions on FDI protection.
12. Deliverables

The result of this study will certainly be unprecedented and essential to future discussion for scholars and arbitrators. It would also be beneficial corporate players with regard to their strategic investment decision.

Therefore, based on the results of this project, it would be very interesting to promote seminars not only for FDI system specialists, from a legal perspective, but also managers and other corporate actors, from a more practical perspective.

Thus, we would suggest to have the study published in a paper format, but also present it to legal, economic and administration professionals through webinar, seminars and even “academic road shows” to present our findings to internal strategic investment departments of multinational companies. The study could also constitute the initial chapter of a book designed and written by the study group as it would entail an economic and legal discussion on investment as a concept.

All these conclusions would certainly impact debate as to whether “economic development” can be identified only through legal perspectives, or if it needs further empirical analysis through a much more economic study.

Recommended Text:

Responsible Corporate Tax:

Corporate Social Responsibility & Tax Base Erosion and Profit Shifting in the Global Digital Economy

Rifat Azam

Abstract

Tax Base Erosion and Profit Shifting (BEPS) refers to tax planning strategies that exploit gaps and mismatches in tax rules to artificially shift profits to low or no-tax locations where there is little or no economic activity, resulting in little or no overall corporate tax being paid. BEPS has expanded rapidly in the era of global digital economy and several high tech multinationals such as Google, Apple, Facebook and many others are using BEPS strategies. The data reveals that these strategies are reducing the effective tax rate substantially and causing substantial loss in tax revenues that risks the democratic welfare state. It is not surprising that people demonstrated against Starbucks for not paying taxes to the UK government and called for closing tax loopholes and that civil society action groups such as Tax Justice Network are lobbying and acting against these tax strategies and the media too is covering the issue widely in recent years. These tax planning strategies that exploit the international tax regime are similar is some aspects to tax planning strategies that exploit the

national tax regimes to avoid taxation but at the same time they are also different. However, in my opinion, all these international and national strategies share the basic essence of tax avoidance that have been used by corporations and individuals since the enactment of taxation.\(^5\)

The Organization for Economic Cooperation and Development (OECD) has addressed the issue of BEPS and has received political support of the G20 to handle the issue.\(^6\) Consequently, the OECD has set an action plan which includes 15 actions to tackle BEPS\(^7\) and is working to publish several deliverables to cope with BEPS.\(^8\) Among the several deliverables published so far, I would like to mention two that are very important in our regard: The deliverable on action 1 which deals with tax challenges of the digital economy. One of the main proposals of this report is the idea of changing the "permanent establishment" nexus by a "significant presence" in a market nexus.\(^9\) And the report on action 6 which deals with Preventing the Granting of Treaty Benefits Inappropriate Circumstances and it recommends that a three-pronged approach be used to address treaty shopping arrangements: – First, it is recommended that treaties include, in their title and preamble, a clear statement that the Contracting States, when entering into a treaty, intend to avoid creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance, including through treaty shopping arrangements. – Second, it is recommended to include in tax treaties a specific anti abuse rule based on the limitation-on-benefits provisions included in treaties concluded by the United States and a few other countries. Such a specific rule will address a large number of treaty shopping situations based on the legal nature ownership in, and general activities of, residents of a Contracting State. – Third, it is recommended to add to tax treaties a more general anti-abuse rule based on the principal purposes of transactions or arrangements. These international legal tools are very important in handling BEPS. Domestic laws too are developing to handle these issues such as the UK Google Tax\(^10\) and President Obama Minimum Global Tax.\(^11\)

My paper does not intend to replace these efforts but to complete them from a different angle. My paper deals with the role of Corporate Social Responsibility in handling BEPS issues in the global digital economy to continue previous work done on the relations between corporate social responsibility and taxation.\(^12\) The

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\(^5\) See: Oxford University Center for Business Taxation, REVIEW OF DOTAS AND THE TAX AVOIDANCE LANDSCAPE (2012);
\(^12\) http://www.wsj.com/articles/u-k-details-google-tax-plans-1418239699
paper begins by summarizing the theories and perspectives on corporate social responsibility. It mainly builds on the business case for CSR which argues that a company can do well by doing good: that is, can perform better financially by attending not only to its core business operations, but also to its responsibilities toward creating a better society, because by that the company reduces costs and risks, builds advantages over competitors, builds value through gains in firm reputation and legitimacy, creates value to the company and other stakeholders.

The main idea of the paper is that the basic social responsibility of businesses is to pay fair taxes while maximizing their profits. Even Milton Friedman’s well know essay “The Social Responsibility of Business is to increase its profits” assumed that business are paying their fair tax and by this tax they fulfill their responsibility. To advance this idea of paying fair tax as the basic social responsibility, the paper argues that the OECD and Governments in designing international and domestic tax law could and should use three different kinds of regulatory tools to handle BEPS and cause corporations to pay their responsible tax: Civil Society, Market and Law.

The paper argues that CSR could and should play a role as a tool for advancing compliance with the spirit of the international tax regime (CSR for Law). The several legal proposals and changes made by the OECD have a lot of merits but at the same time these proposals and law in general have limits and extra legal corporate social responsibility could enhance compliance with the spirit of the law. Scholars have developed the concept of “creative compliance” where much legal regulation is frustrated by clever legal gamesmanship that creatively structures or restructures the legal form of business practices in such a way that it can be claimed they fall outside the ambit of disadvantageous law and beyond the reach of legal control. BEPS strategies are creative compliance strategies that are after all readily justifiable as perfectly legal, not breaking the law but merely using it in creative ways. Therefore, changes to the law alone cannot easily tackle creative compliance and here CSR jumps in to advance compliance with the spirit of the law and fulfill the basic social responsibility of paying taxes. Tax BEPS issues could and should be part of any CSR report of corporations. Civil Society and Market pressures on corporations to advance CSR policies and activities could and should include Tax BEPS issues. Naming and shaming strategies could and should be used to push corporations to pay their responsible tax. The OECD and governments should financially support civil society organizations to limit BEPS and advance real compliance with the spirit of the international tax regime. Putting pressure on business to review its attitude to
law and compliance, shifting the threshold of social responsibility and ethical legitimacy from compliance with the letter of the law to compliance with its spirit and so, potentially, enhancing the effectiveness of the international tax regime. The idea of CSR for law has advanced issues of human rights, environment and labor and it could contribute in advancing effective and fair compliance with the international tax regime. As McBarnet put it clearly:

"Courts of public opinion, markets and investors can set their own standards for what they hold to be legitimate and they may set the bar higher than what is arguably technically legal, viewing even legal compliance through the lens of what is ethically acceptable or socially responsible".\textsuperscript{20}

From the other way around, the paper argues that the international tax regime could and should set legal rules and standards to advance CSR in BEPS issues in the sense of paying responsible tax (CSR through Law). Despite the fact that governments have shown themselves reluctant to make the adoption and implementation of CSR policies a mandatory requirement of company law, governmental legislation has nonetheless played a role in fostering CSR in different fields through indirect regulation and disclosure rules. We argue that the international and domestic tax regimes could and should use such indirect regulation and disclosure rules to foster the payment of fair tax and limit BEPS strategies. Based on this perspective, the paper proposes to enact international and domestic legal rule of full disclosure of the effective global tax rate as an additional tool for handling BEPS and reducing BEPS. According to our proposal, Corporations will be obliged by domestic and international tax law to publish detailed data on their effective tax rates domestically and globally and on their BEPS strategies. The publication will be made on the products of these corporations and on their websites and on the newspapers and on their CSR reports and financial reports. It is important to emphasize that we call for public transparency rather than transparency to tax authorities as have been already proposed.

We argue and believe that such a wide public disclosure will indirectly increase the cost of BEPS strategies in terms of reputation and market share and consequently affects the behavior of corporations in adopting tax policies and BEPS strategies. This full disclosure rule in our opinion will add to the other rules designed to tackle BEPS. We are aware of the literature on disclosure rules and the controversy surrounding the effectiveness of disclosure rules and we will analyze our proposed disclosure rule within this literature.\textsuperscript{21}

In sum, we offer a complex interaction between civil society, market and law which interrelate with and foster each other as complementary measures of regulation which aims to reduce tax BEPS strategies and bring businesses to pay their responsible tax to the society.\textsuperscript{22}

\textsuperscript{22} See: Devereux, Michael (2013) How we can make global companies pay their fair share of tax. The Financial Times, 22nd May 2013;