Foundations of stone or sand?

South Africa is overhauling its international dispute resolution landscape, but after cancelling many of its bilateral investment treaties, will it be enough to reassure foreign investors that it can be trusted?

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THE MIDDLE OF 2017 should see South Africa introduce two new laws, designed to attract international investment and arbitration, and lay the groundwork for a new future as an arbitration centre.

The International Arbitration Bill 2016 and Protection of Investment Act 2015 both offer international dispute resolution mechanisms, but it remains to be seen whether they can repair the country's reputation as an investment destination.

South Africa's decision, beginning in 2012, to withdraw from its bilateral investment treaties (BITs) with many, mostly European nations, alarmed South African businesses and foreign governments.

Without protection for their investments through the BITs' investor-state arbitration provisions, there was a concern that these international parties would be reluctant to invest in a country where there is a risk of reform and expropriation through the Black Economic Empowerment (BEE) programme, designed to correct decades of economic injustice under apartheid.

Attracting international arbitration

The International Arbitration Bill was approved by parliament on 1 March 2017, and is poised to be signed into law by President Jacob Zuma sometime in the middle of the year, it is a long overdue overhaul of arbitration legislation that has been untouched since the Arbitration Act 42 of 1965.

That law remains, overseeing domestic arbitration, but international disputes will be the preserve of the new bill.

The bill adopts the **United Nations Commission on International Trade Law** (UNCITRAL) Model Law, which "will basically bring us up to speed with the best practice in arbitration internationally", argues **Jonathan Sahli**, a dispute resolution partner with **Bowmans**. "It has been 20 years since the South African law reform commission recommended that we promulgate legislation to regulate international arbitration, so there has been a vacuum."

Indeed, it was the need to align the model law with the South African courts, which delayed the bill's original introduction from 2016 to 2017.

The second facet of the bill replaces the Recognition and Enforcement of Foreign Arbitral Awards Act 1977, updating the country's enforcement obligations to recognise foreign awards under the New York Convention, bringing it "in line with more current practices and the direction that our courts have taken", says **Grant Herholdt**, a dispute resolution and international trade law

director with **ENSafrica** in Johannesburg, who believes the law "does all the right things".

Aligning the law with international arbitration best practice is an early move towards establishing an institution to compete with the **Mauritius International Arbitration Centre** (MIAC), believes Herholdt: "We have all the right ingredients," he explains. "Our courts have been very pro-arbitration, the decisions that even our constitutional courts have handed down have been pro-arbitration, applying international standards for arbitration, protecting awards."

He continues: "The infrastructure is very well set up for it, more so than Mauritius. We have a very good legal community in South Africa, good lawyers, well trained, more and more exposure to international arbitrations."

Whether an arbitration centre would "be in the form of a pure state-sponsored arbitration centre, or whether it is going to be a public-private version through our current arbitration facilities under the **Arbitration Foundation of South Africa** (AFSA) we don't know yet", he adds, though early signs indicate the latter.

Despite the existence of the dispute resolution court of *Organisation pour l'Harmonisation en Afrique du Droit des Affaires* (OHADA) in West and Central Africa, which has been plagued by problems, little international arbitration is done on the African mainland. Instead most disputes are handled in London or Paris, or at MIAC, which has established itself as the offshore African jurisdiction of choice. South Africa believes it can capitalise on its status as the home of most of the international lawyers on the continent.

Protecting investments

It was after being challenged by Italian investors through the Belgium-Luxembourg BIT in the 2010 *Foresti* arbitration, that South Africa began reviewing its investment treaties. The case, at the **International Centre for Settlement of Investment Disputes** (ICSID) contested the enforced sale of 26% of a mining company under the BEE policy.

"That case gave the government quite a fright, because they thought potentially their whole BEE programme could be imperilled by these BITs," says **Peter Leon**, global co-chair of **Herbert Smith Freehills**' African practice.

Although the government initially said it would merely revise the treaties to follow the SADC model BITs, it "threw the baby out with the bathwater" and chose to scrap them.

"It does not send a good message to foreign investors to terminate BITs and then give those investors far less investment protection than they had before," says Leon.

However, they are not gone yet, BITs have long wind-down periods. In the case of the UK BIT, although new investments are no longer protected, existing ones will be for 20 years. As a result, the government "still faces the prospect of treaty claims under a treaty which they think is antiquated, outdated and affects a government's right to regulate".

The Protection of Investment Act introduces investor-state mediation and carves out certain areas of industry as being of public importance, exempting the government of duties towards the investors. It takes "an approach of domestic equivalence", treating international investors with the same rights as domestic, explains Leon.

"The one bone they threw out to foreign investors was the right to take the government to mediation," he says, but although the new act makes it compulsory, it is undermined because the regulations make that right subject to the government's consent, "so that claim is *ultra vires*".

Sahli is more positive, saying: "I can never see any drawback between investors and the state trying to resolve things before embarking on legal proceedings," but he acknowledges the concerns.

What is unclear is what happens to the disputes that fall into the carve outs. Herholdt reports that the government has told him that parties "can rely on common law provisions to get those same safeties" but that leaves grey areas over interpretation, particularly since the carve outs are so broad "you could basically pigeonhole just about any dispute" into one. However, he feels positive that the courts will "be as restrictive as possible in interpreting what those carve outs apply to".

However, although more types of disputes are covered than under the BITs, the mediation provisions do not offer investors the same depth of protection. "It is very much a watered down version of investment protection," says Herholdt. Nor may mediation be suited to every kind of

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dispute, particularly complex and high-stakes matters such as expropriations.

As the mediators would be appointed by the Department of Trade and Industry, questions over their independence will come up after every contentious decision and businesses may be concerned that documents they produce during mediation will later be used against them in litigation, despite the rules prohibiting the practice.

Leon argues that "the regulations are not very well-drafted" and suffer from not following the IBA Rules on Investor-State Mediation, particularly with regards to the "competence and independence of the mediators".

The fact that the mediator does not have to be a lawyer will also concern parties in complex disputes: "If you get a mediator who is not necessarily au fait with those kinds of things, it might defeat the object of the exercise," says Sahli. "That would be remedied if any mediators are required to have particular expertise in the fields of investor-trade relations."

Nor is it clear what happens if mediation fails. With mediators having no powers to make an award, and the mediation being dependent on the consent of both parties, failure is a distinct possibility, which will lead companies and the government either to court or perhaps domestic arbitration, if a forum can be agreed.

"There is no provision for arbitration proceedings after that or a reference to some sort of expedited court process, so it leaves that quite open really," says Sahli.

"The court process can take quite a long time. Typically you are looking at a year or two to get a first instance judgment from the date on which you commenced proceedings and you are then still subject to the possibility of an appeal," he continues.

Expropriation is at the heart of the government's worries over BITs and will be the great concern for investors. The Protection of Investment Act's provision for expropriation does not offer the full market value of "prompt, adequate and effective" which would normally be expected in a BIT, instead offering "just and equitable" compensation, says Leon.

"There is no provision at all for international arbitration, it has to be domestic, nor is there any provision for fair and equitable treatment, or for full protection and security, so the provisions you would normally see in a BIT are simply not there."

In the same way that investor-state dispute settlement has been rejected by South Africa, it has become controversial around the world in recent years, attacked by politicians and the media for appearing to favour international corporations over national interests.

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Leon acknowledges this, but points out that "the reason that international arbitration exists is to take [disputes] out of the domestic arena and place it in the international arena and that gives investors a great deal of confidence". South Africa's BIT replacement risks losing that confidence.

Emerging optimism

The proposals are not finalised, however. A consultation period for the act only closed on 28 February, so there is still time for the government to make changes.

It is clear that South Africa's dispute resolution scene is in a period of transition, but despite the flaws and concerns, those practising in the sector remain optimistic that the country will be able to attract a new wave of work that will grow the disputes sector and establish South Africa's position as a venue for arbitration.

Although South Africa has been "relatively sheltered" from international arbitration because of its "outdated legislation" and the lack of the model law, Herholdt expects "a very significant influx of international arbitration over the coming years after the bill is introduced, after the arbitration centre is set up [and] after people find a better level of comfort in international arbitrations here".

"I like to think that the arbitration bill once it has been promulgated will create more opportunities for international arbitration in this country," agrees Sahli.

"We are pretty well-placed to handle international arbitration. We are conveniently located for Europe, we are conveniently located within Africa itself. We have got comparatively great infrastructure, the lawyers here are of a very high calibre, the potential arbitrators as well, we have already got some great jurists, so I like to think there is significant scope for growth," he concludes, while acknowledging that it depends on other factors, including the economic state of the country and the continent.