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Research Report

How to enhance labor provisions in IIAs

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How to enhance labor provisions in IIAs

by

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Free trade agreements (FTAs) and international investment agreements (IIAs) are regarded as instruments to promote world trade, investment flows and market liberalization. The question, however, is whether they promote sustainable development as well. This *Perspective* contemplates incorporating voluntary codes of conduct for multinational enterprises (MNEs) in IIAs to strengthen the protection of labor rights, “the social component [...] embedded in the notion of sustainable development.”¹

The link between employment and trade, which dates back to the 1948 Havana Charter,² focuses on two objectives: greater coherence with international standards aimed at improving workplace conditions and workers’ welfare and the incorporation of such standards in trade negotiations. However, policy space concerns and the fact that international standards are still perceived as protectionism are obstacles to openly including labor provisions in the trade agenda. Therefore, trade-related promotion of the highest available international standards has to be achieved through mechanisms creating market-based incentives on compliance,³ such as corporate social responsibility (CSR) codes or fair-trade labeling. The interaction between employment and investment follows a similar pattern. Hence the question: should reference to labor rights in IIAs be limited to eliminating regulatory distortions created to attract capital (i.e., the “race to the bottom” phenomenon), or should it encourage corporations to embrace the highest available international standards on fair labor? In our view, it should be the latter.

Article 13 of the 2012 US Model Bilateral Investment Treaty (BIT) is devoted to investment and employment. It cross-references the 1998 International Labour Organization (ILO) Declaration on Fundamental Principles and Rights at Work to reaffirm core obligations embodied therein, features a “no-lowering-of-standards” provision according to which parties shall not derogate from labor standards or deliberately fail to enforce their laws to attract or maintain investments and creates an inter-governmental consultation mechanism.

References to labor rights in IIAs are aimed at improving employment conditions and promoting sustainable development. Since employment-related issues usually arise from the acts or omissions of corporations and not the total absence of regulation, provisions should focus on MNEs' activities instead of just governmental action. Indeed, although ILO core standards are widely accepted by governments, corporations may be reluctant to improve employment conditions voluntarily if it only entails costs. Furthermore, the role of foreign direct investment in promoting fair employment depends on the ability of host countries to enforce labor regulation effectively at the highest available international standards without affecting their allure to investors. IIAs could better contribute to this if they included provisions that focus on MNE conduct. The rationale behind this is simple: if investors expect legal security from host countries, they should have a correlative deference for national interests in promoting sustainable development through labor rights enforcement.

There are multilateral instruments that address employment issues from a corporate perspective. Among these are the ILO's Tripartite Declaration of Principles Concerning Multinational Enterprises and Social Policy and the Employment and Industrial Relations chapter of the OECD Guidelines for Multinational Enterprises. They are both focused on issues arising directly out of MNE conduct. For instance, the Tripartite Declaration underlines duties for MNEs operating in developing countries, encourages increasing employment opportunities and urges MNEs to consider host country policies regarding employment.

Although neither instrument is mandatory, MNEs may have a market-based incentive to embrace fair labor as a matter of CSR. Therefore, while IIAs cannot impose binding obligations on MNEs, incorporation⁴ of the content of the Tripartite Declaration and the Guidelines into IIAs or the investment chapters of FTAs can successfully exhort investors to adhere voluntarily to the highest available international labor standards.⁵ Therefore, we favor the approach taken in Canada's FTAs with Peru (2009) and Colombia (2011)⁶ over the approach taken in the 2012 US Model BIT.

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¹ See Vid Prislán and Ruben Zandvliet, "Labor provisions in international investment agreements: Prospects for sustainable development," *Yearbook of International Investment Law and Policy 2012/2013*, forthcoming, also available at <http://ssrn.com/abstract=2171716>.

² Article 7 on Fair Labour Standards.

³ As compliance is rewarded by consumers' preferences. See US – Measures Concerning the Importation, Marketing and Sale of Tuna and Tuna Products, WTO Panel Report, WT/DS381/R, para. 7.289, http://www.wto.org/english/tratop_e/dispu_e/381r_e.pdf.

⁴ Either by cross-reference, appendage or commitment by the contracting states to pass internal regulation. See UNCTAD, *International Investment Agreements: Key Issues*, vol. II (2004), available at http://www.unctad.org/en/docs/iteit200410v2_en.pdf.

⁵ Other examples of international instruments with codes of conduct for MNEs are the UN Global Compact, the UN Draft Code of Conduct on Transnational Corporations, the SA8000 Certification, and the Accord on Fire and Building Safety in Bangladesh.

⁶ See Articles 810 and 816, respectively.

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