

ONTARIO
SUPERIOR COURT OF JUSTICE

BETWEEN:

**THE COUNCIL OF CANADIANS, and DALE CLARK, DEBORAH BOURQUE,
and GEORGE KUEHNBAUM on their own behalf and on behalf of all members of
the CANADIAN UNION OF POSTAL WORKERS, and
BRUCE PORTER and SARAH SHARPE, on their own behalf and on behalf of all
members of the CHARTER COMMITTEE ON POVERTY ISSUES**

Applicants

- and -

**HER MAJESTY IN RIGHT OF CANADA, AS REPRESENTED BY
THE ATTORNEY GENERAL OF CANADA**

Respondents

AFFIDAVIT OF MANFRED BIENEFELD

I, **Manfred Bienefeld**, of the City of **Ottawa**, **HEREBY AFFIRM that:**

1. I received my **Ph.D** from the **London School of Economics in 1969**, and since 1986 have served **as a Professor** in the **School of Public Administration** at **Carleton University**. I have written and **published** extensively on the subjects relating to **the international economy, particularly as these affect economic and social development** in poorer nations. **As such I have knowledge of the matters to which I hereinafter depose. A copy of my Curriculum Vitae is attached as Exhibit "A" to this Affidavit.**

2. I have reviewed the affidavit of **Denyse Vigors MacKenzie** and have been **asked** to comment on certain claims relating **to the risks and** benefits of **Canadian** international trade policy as they relate to foreign investment.
3. To begin with, it is **remarkable**, given the subject matter of **this** litigation, that **no** argument or evidence is presented **by** Ms. MacKenzie to **support** the notion that the investor-state suit provisions of NAFTA **are** needed to achieve Canadian domestic or international policy objectives, including those related to trade. In fact, the failure of the CUSFTA **and current** WTO agreements **to** include analogous provisions demonstrates that robust international trade agreements can **be** established without the inclusion of **such** elements. Apparently, **Canada was of the same** view in putting forward **NAFTA** investment rules that **did not** allow for such unilateral and private **rights** of enforcement.
4. Moreover, as pointed out by Professor Somarajah, **and** since borne out by the virtual collapse **of** efforts to **expand** investment disciplines within **the** WTO, **efforts** to establish such disciplines **as** features of multilateral trade **regimes** have either foundered **or** been soundly rejected.

Affidavit of Professor Somarajah, sworn **April 28, 2003**, paras. **96-102**.

5. Rather Ms. MacKenzie's evidence speaks to more general points, which **are** at best only tangentially related to the question of investor-state litigation, namely that a) **foreign direct** investment **necessarily and** significantly benefits **both** recipient **and capital** exporting nations; **and** b) that international investment treaties are **an** important **means of** fostering FDI. I shall deal with these **explicit** and implicit claims **in** turn.

The Role of FDI in Achieving Canadian Policy Goals

6. In describing the link **between** trade and investment, Ms. MacKenzie states that **"Canadian Policy is based on the recognition that FDI benefits both** recipient and

capital exporting countries”. As evidence to explain or support this core tenet of Canadian international **trade policy** her affidavit attaches a **speech** given by Minister Pettigrew to **the** Conference Board of **Canada** in 2002, **and** a report prepared by the Canadian Chamber of Commerce in partnership with Industry Canada (**the** “CCC report”).

7. Mr. Pettigrew’s **remarks** offer a number of declaratory statements about the putative benefits **of** FDI, but **he does** not present **nor does he** point to empirical evidence to **support** these statements. Rather, his **remarks** simply indicate that Canadian policy with respect to foreign investment fundamentally reflects the neo-liberal economic policy agenda¹ that gained its ascendancy in **the** 1980s, despite the virtual absence of systematic or persuasive empirical or historical supporting evidence, as explained by a paper I have written titled, “Structural Adjustment: Debt Collection Device or Development Policy?” which is attached **as** Exhibit “B” to this affidavit.

8. In fact, according to a recent report published by the World **Bank**, there **is** a real possibility that FDI can have a net negative impact, especially **when** it displaces domestic investment, appropriates domestic R&D capabilities, or “distorts” subsequent national policy **discussion** because it comes to have a disproportionate voice in the **policy** process. Moreover, a recent empirical **study by UNCTAD** confirms that **such** fears **are** not unwarranted since it shows that the only countries that have **been able** to derive significant, **demonstrable benefits** from FDI in recent decades have been relatively more interventionist Asian countries that have not only been selective in their **efforts** to attract FDI, but also **very** active in ensuring that the activities of foreign investors **are** consistent with nationally defined objectives and priorities. While this evidence is not conclusive, **it** is certainly **incompatible** with policies based on **the** assumption that such flows will **always yield large**, and critically important, net benefits. **Copies** of the World

¹ For present purposes I use the term neo-liberal to describe a set of economic policies which promote free markets with a bare minimum of state regulation, a reduction of government spending on social services, the privatization of public assets and resources, deregulated international finance, and free trade.

Bank and UNCTAD reports referred to are attached as Exhibits “C” and “D” respectively, to this affidavit.

9. At present, the weight of the available evidence suggests that policies seeking to attract FDI indiscriminately within an effectively non-reviewable neo-liberal policy framework **are** always **risky and** often detrimental. **And this is why** Canadian government policies have long recognised the need to regulate foreign investment in the **public** interest.

10. The latent conflict between FDI and **domestic policy** goals is **implicitly** highlighted by the long **list of** so-called public policy “impediments to FDI” that **are** identified in the CCC report. **As** Ms. MacKenzie notes, in this report the Canadian **Chamber** of Commerce, **which** describes **itself** as “as an ardent supporter of trade and investment liberalization,” advocates the dismantling of **most** such restrictions on investment, including **many** that are currently maintained by **OECD** countries, including **Canada**. It **is** undoubtedly significant that so many countries with such widely differing political heritages, came, over **time**, to the conclusion that such policies, in one **form** or another, provided the **necessary** framework for both federal and/or **provincial** governments to promote and protect provincial and national economic and social policy goals. **And** although such policies have undoubtedly **been** misused on occasion, there is no **serious** evidence to **support** their effective elimination.

11. It **is** important to understand that the real question **is** not whether FDI is a good thing or a bad thing. Rather, in this case, the question **is** whether it is defensible to **assume** that the effects of FDI will **always** be positive, **let** alone significantly positive, for the recipient society. The answer to that question is clearly “no”, **since** there can be no doubt that **the** net impact of FDI depends on a number of constantly changing circumstances. That **is** why policies dealing with **the** attraction or regulation of FDI should always **remain** subject to review by national policy makers, or courts, a requirement that is incompatible with international

investment treaties that are specifically designed to limit **such** domestic **policy** flexibility, **particularly** when **such** constraints on **public policy may be** enforced privately.

International Investment Treaties and FDI

12. Even **putting aside the** question of whether it is sound **policy** to indiscriminately embrace both **inward and** outward FDI flows, and to remove key decisions regarding their operations **from** national jurisdiction, I do not find in the evidence introduced by **Canada any substantive** support for the claim that binding international investment rules are important for attracting foreign investment to this country, or for protecting the interests of Canadian investors **abroad**. There is certainly no evidence **to** support the notion that such investment, once **received**, serves the **public** interest or **promotes** the **welfare of** Canadians **as it is defined** in this country.

13. Both the history of **FDI** flows into Canada, and the **simple** fact that China, and several other **Asian countries with** relatively interventionist governments, **have** received a large and growing share of the **world's FDI** in recent years, **calls** into question the **claim that** international investment treaties **are** “necessary” to secure high **levels** of FDI flows.

14. The **weakness** of the evidence **supporting the claim that** bi-lateral investment treaties (BITs) are of **material** importance, either for attracting FDI, or for **growth** and development, is clearly summarised by the World **Bank study** previously noted, which **describes** the disconnect **between FDI** and BITs **such as those** negotiated **by Canada, as** follows:

Clearly, a BIT is not a necessary condition to receive FDI. There are many source-host pairs with substantial FDI that do not have a BIT. Japan, the second largest source of FDI has only concluded 4 BITs. The US does not have a BIT with China, its largest developing country destination. Brazil, one of the top receivers of FDI has not ratified a single BIT. In addition, there are also numerous examples of countries that have

concluded many BITs and yet have received only moderate inflows. Sub-Saharan Africa, for instance, has had difficulties in attracting FDI, though it has tried to improve the environment for FDI by entering into various agreements to protect the interests of investors. There are also examples such as Cuba, where it does not have a BIT with either Canada or Mexico, its two biggest foreign investors. On the contrary, almost 60% of the countries it does have a BIT with actually have no foreign investment in Cuba. (Perez-Lopez et.al.)²

15. Furthermore, the same patterns broadly hold true for Canada. Thus the overwhelming majority of Canadian direct investment abroad (CDIA) is destined to the United States and Europe. Although FDI flows between Canada and the United States have increased rapidly in both directions in recent years (at least until the sharp reversals of 2003), there is currently no evidence to suggest that NAFTA investment rules have played a role in promoting such investment, and this assessment is consistent with the fact that flows to and from the EU have also risen during this period even though Canada has no similar investment agreements with the EU. Nor does Canada have such agreements with the most important FDI destination countries in the developing world, including Brazil and China.³

16. Furthermore, as discussed by the World Bank report noted above, the correlation between BITs and FDI has rarely been examined, but on the few occasions when it has been [UNCTAD 1998], no significant correlations were found. Thus the authors of the report Commissioned by World Bank conclude that :

*Analysing twenty years of bilateral FDI flows from the OECD to developing countries finds little evidence that BITs have stimulated additional investment.*⁴

17. It is indicative of the lack of balance in Canadian trade policy that Ms. MacKenzie's evidence offers no acknowledgement that the establishment of binding international investment rules that can be privately enforced is associated

² Exhibit "C" p. 9.

³ Statscan, "The Daily", Tuesday, May 18, 2004, "Foreign direct investment", pp 1-4)

⁴ Exhibit C, p. 22.

with a **risk** of significant adverse impacts. **Thus** her affidavit makes no reference to the authoritative studies such **as** those **by** the World **Bank** and UNCTAD referred to above, nor does it address, **or** discuss, the **considerable risks** and potential impacts associated with international investment agreements, **which** as identified in the report include:

- that, as recent **high** profile legal cases demonstrate, the rights given to foreign investors **may expose public** authorities to potentially large scale liabilities **and** curtail the feasibility **of** potential reform **options**;
- that the strength **of** the **rights** entrenched **by** such agreements **may** entail disincentives for potential domestic investors; or **may provide** foreign investors with levels **of** insurance well beyond those enjoyed by domestic investors or required to foster FDI **with** potentially far-reaching consequences for the **future** policy choices available to host governments; **and/or**
- that **as** the potential **for** legal recourse under international investment agreements becomes more widely known, the importance of such agreements in selecting a location **may** become more important over time, potentially leading to problems of moral **hazard** and adverse selection.⁵

18. **More** broadly, **similar concerns have been raised about the** socio-economic **impact of** the market-oriented neo-liberal. **policies** that provide the **Framework, and the rationale**, for the proliferation of BITs. In fact, the structural adjustment policies that have been aggressively promoted by the World **Bank** and the IMF since 1980 **have** generally **sought** to impose policies that echo, or duplicate, the constraints contained in bilateral and/or international trade **and** investment agreements. Here too the evidence **shows** that the impact **of** these broader neo-liberal policies can

⁵ Exhibit "C", pp. abstract, 3 and 7.

often have detrimental, and sometimes disastrous, effects **as** described **in** my **paper** (Exhibit “B”).

19. The **essential** conclusion of my **work** is **that** it is crucial for sovereign **states** to retain the ability to manage **FDI** related policies pragmatically, **and** in the national interest. This same conclusion has been reached by numerous **leading** authorities, including **Yilman Akyüz** in an UNCTAD Discussion **Paper** on financial liberalization:

*government intervention in finance has often been misguided ... the appropriate response should be to reform the government and rationalize intervention rather than throw in the towel and simply ‘unleash market forces’ ... **Success** .. depends on ensuring reciprocity between support and performance; use of controls, regulations and **subsidies** for the intended purposes; and readiness to revise them **as** necessary.⁶*

20. Similarly, Dani Rodrik, of Columbia University, concludes his 1999 book on the new global economy **and** developing countries, **as** follows:

*The evidence from the experience of the last two decades is quite clear: the **countries** that have grown most rapidly since the mid-1970s are those that have invested a high share of GDP and maintained macroeconomic stability. The relationship between growth rates and indicators of [economic’ **openness** – levels of tariff and non-tariff barriers or controls on capital flows – is weak at best.⁷*

*The countries that fell apart did so because their social and political institutions were inadequate to bring about the bargains required for macro-economic adjustment – they were **societies** with weak institutions of conflict management ... [because] ... adjusting to changing circumstances, and to external shock in particular, requires the presence of institutions that **can** mediate distributional **conflicts** in **society**. In the absence of such institutions, the **policy** adjustments needed to re-establish macro-economic balance are delayed ... Societies with deeper cleavages (along ethnic, income, or regional lines) are particularly susceptible to policy paralysis of **this** sort, making institutions of conflict management all the **more important**.⁸*

⁶ Yilman Akyüz ; *Financial Liberalisation: The Key Issues* [UNCTAD DP 56, March 1993, UNCTAD: Geneva].

⁷ Rodrik, Dani (1999) *The New Global Economy and Developing Countries: Making Openness Work*, Washington D.C.: ODC – Policy Essay No. 24, at p. 2.

⁸ Idem, p. 17.

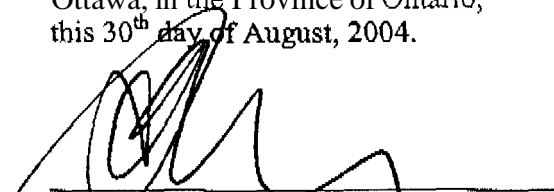
Conclusion

21. While the federal government is certainly entitled to adopt **an** agenda of international trade **and** investment liberalization, **good** public policy development **requires** that government policies **be** defensible and based on **the** best available **evidence**, This is **especially** true in cases where policies significantly **infringe** or constrain **the** policy and legislative options **of** the country's sovereign institutions, **as** in this instance. Indeed, **given** the **dearth of empirical** evidence to **support**, and the substantial evidence **to refute**, the broad propositions **on** the basis of which Canada **has made** binding international commitments under several BIT agreements, and NAFTA's Chapter 11, it is **fair** to suggest that these policies **were fundamentally based** on ideology, **rather** than on **persuasive** evidence.

22. For these reasons, in my opinion Canada's commitments to such international investment agreements, particularly in light of the fact that **they** may be privately enforced, can neither be justified on **the** grounds that **their** effects are beneficial, nor on the grounds that they **are** an important means of fostering **FDI**. In fact, these commitments diminish **the** policy and regulatory prerogatives of governments while exposing Canada and the taxpaying citizenry to open-ended liabilities and **risks**, **all** in return for **highly** uncertain, hypothetical benefits.

23. I **make** this affidavit in **support** of **an** application and **for** no other or improper purpose.

AFFIRMED before me at the City of)
Ottawa, in the Province of Ontario,)
this 30th day of August, 2004.)



A commissioner for taking affidavits, etc)



MANFRED BIENEFELD

DEPARTMENT: School of Public Policy and Administration

July 2004

a) **NAME:** BTENEFELD, Manfred, full professor, tenured, member Graduate Faculty

b) **DEGREES:**

B.A., (Hons.), University of Toronto, 1964

Ph.D., University of London, London School of Economics, 1969

This is Exhibit "A" referred to in the affidavit of ~~M. Manfred Tenefeld~~ sworn before me on this 20th day of August, 2004. A COMMISSIONER, ETC.

c) **EMPLOYMENT HISTORY**

Academic Appointments:

1986- Professor, School of Public Administration, Carleton University

1972-86 Research Fellow, Institute of Development Studies; University of Sussex, UK

1969-72 Research Fellow, Economic Research Bureau; University of Dar es Salaam

Other:

1966-68 Teaching Assistant in Economics; London School of Economics, University of London, UK

d) **HONOURS:**

1978-86 Governor: Institute of Development Studies (Sussex: UK)

e) **SCHOLARLY OR PROFESSIONAL ACTIVITIES:**

i) Editorial Responsibilities:

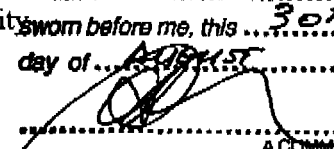
1987-2002 Member, Studies in Political Economy Editorial Board

ii) Other Professional Activities:

December 2003 Joint organizer (with Professor Antonio Iglesias and Orlando Gutierrez, University of Havana) of an International Conference on "Public Administration for the 21st Century: Research and Human Resource Development Challenges", University of Havana and Carleton University, Havana.

April 2003 Joint organizer (with Professor Orlando Gutierrez, University of Havana) of Research Workshop on "The Social Impact of the Reforms", University of Havana, Havana.

Structural Adjustment: Debt Collection Device or Development Policy?

This is Exhibit..... "B" referred to in the
Manfred Bienefeld affidavit of MANFRED BIENEFELD
Carleton University, sworn before me, this 30th
day of AUGUST..... 2004

.....
A COMMISSIONER, ETC.

Introduction¹

Economies must constantly **adjust** to **changing** circumstances **and**, as the world economy **has** become more volatile **and** more integrated, economies have had to become continually more flexible **and** responsive. Unfortunately, **many** developing countries **were** unable to **meet** this **growing** challenge **during** the **seventies** **and** many borrowed heavily **abroad** or **squeezed** their **export** sectors, to avert **an** economic or political collapse. This **further** worsened **imbalances** in **trade**, production **and** finance and these eventually became unsupportable when commercial bank lending **abruptly** ended in **the** early eighties. When **several large** debtors were forced into virtual bankruptcy, the world suddenly discovered the debt crisis.

The International Financial Institutions (IFIs) were now **called upon** to **restore** order **and** to **save** the global **financial** system **from collapse**. They did so by mobilising emergency credits to **allow** countries to meet their most **pressing** obligations, and **by** making receipt of **those** credits conditional on **the** implementation of policies designed to enhance economic flexibility. The aim **was** to assist them in eliminating chronic balance of payments problems, **often** dominated by a **heavy** debt service charges. The primary focus of **these** structural adjustment policies **was** therefore on increasing debt **service** capacities **through export expansion** and **import** compression. Debt service obligations **had** to be given **an** overriding **priority** because **substantial** debt relief was not forthcoming **and** because the re-establishment **of** credit worthiness **and** of access to international capital **markets was** assumed **to** be **an** essential prerequisite for **a** return to development **and** growth.

The neoliberal policies that **were** to **help** countries achieve **this** transformation were **designed** to **allocate** resources **strictly** in accordance with global market **signals**. Prices, exchange rates **and** factor incomes were to **be** allowed to move to equilibrium levels so that **markets** would clear **and** allocative efficiency **would be** maximised. **Resources would be allocated** strictly in accordance **with** the global **distribution** of income **and** property **rights**, including those of the owners of the Third World's debt. **Countries** with high debt service burdens, low productivity, surplus labour **and weak** technological capabilities could only hope they **would** reach equilibrium before the

¹ A first draft of this Paper **was** written for a series of lectures on 'Structural Adjustment: Past, Present **and** Future' that were **given** at Sophia University, Tokyo on November 24 and 25, 1993. At that **time** those notes appeared **as** a Discussion Paper in the Sophia University: ADMP Series No5 (Tokyo: Sophia University: Administration and Management Program). Subsequent events have only reinforced the central message of the paper, **as the Postscript** explains.

This is Exhibit..... "C"referred to in the
affidavit of MARY HALLWARD-DRIEMEIER
sworn before me, this 30TH
day of MAY.....2004
.....
A COMMISSIONER, ETC.

Do Bilateral Investment Treaties Attract FDI? Only a bit ...and they could bite

Mary Hallward-Driemeier*
World Bank, DECRG

June 2003

Abstract: Toted as an important commitment device that attracts foreign investors, the number of bilateral investment treaties (BITs) ratified by developing countries has **grown** dramatically. This paper tests empirically whether BITs have actually had an important role in increasing the FDI **flows** to signatory countries. **While** half of OECD FDI into developing countries by 2000 was covered by a BIT, **this** increase is accounted for by additional country pairs entering into agreements rather than signatory **hosts gaining** significant additional FDI. **The** results also indicate that **such** treaties act more as **complements** than **as substitutes** for **good institutional quality and local** property rights, the rational often cited by developing countries for ratifying BITs. The relevance of these **findings** is heightened not only by the proliferation of such treaties, but by recent high profile legal cases that demonstrate that the rights given to foreign investors not only exceed those enjoyed by domestic investors, **but** expose policy makers to potentially **large** scale liabilities **and** curtail the feasibility of different reform options. Formalizing relationships and protecting against **dynamic** inconsistency problems are still important, but the results should caution policy makers to **look** closely at the terms of **agreements**.

* I wish to thank Richard Newfarmer, Pierre Sauve, Beata Smarzynska, the participants at the Columbia Law School Conference on Regulating FDI and participants in the World Bank's Economist Forum for their comments. I am grateful to Sweta Bagai for research assistance. The views expressed here are those of the author and do not necessarily reflect those of the World Bank, its Executive Directors or its member countries.

