



Position Paper

Promotion of Foreign Direct Investments in the Czech Republic

- systemic problems, and proposals for their resolution -



© GARDE (Global Alliance for Responsibility, Democracy and Equity) – Environmental Law Service – November 2007



The publication has been made possible through funding from the European Commission – DG Environment.
The sole responsibility of this material lies with the author. The Commission is not responsible for any use that may be made of the information contained therein.



Foreign direct investments by multinational corporations in the Czech Republic have become an especially significant phenomenon during the last few years. Lawyers at the GARDE program of the Environmental Law Service (hereinafter GARDE-EPS) have been working for years on domestic foreign investment cases, such as e.g.: the Mexican Nemak aluminum works in Havraň near Most, the Japanese-French Toyota Peugeot Citroën Automobile auto manufacturing plant near Kolín, the Korean-Dutch LG.Philips Displays TV screen factory in Hranice, or most recently, the Korean Hyundai auto manufacturing plant in Nošovice.

The findings of GARDE-EPS during their work on the above mentioned cases lead to the conclusion that governments are unable to face the negative environmental, economical and societal impacts connected with the activities of foreign investors. Public administration has been not fulfilling one of its functions, and in certain cases, has been even actively participating in the execution of actions with severe adverse impacts on society. Enforcement of the law and protection of important public interests thus have often been failing in the face of strong corporate interests. Phenomena connected with promoting and implementing extensive direct investments have been disturbing the fundamentals of the democratic, legally consistent state itself.

According to GARDE-EPS, the following systemic problems are connected with the process of promoting and implementing foreign investments in the Czech Republic:

1. The design of and role of the government's CzechInvest investment promotion agency are a threat to several fundamental democratic principles.

CzechInvest is a typical product of the process of the deliberate actions taken to increase the extent and significance of foreign investments in the international field. It is designed in accordance with the model of investment promotion agencies that was introduced and supported by international monetary institutions (especially by the World Bank). The main characteristics of this unified model are interrelation between the public and private sectors and a concept named simply "One-Stop Shop." Under the One-Stop Shop concept, investment promotion agencies should either provide foreign investors with all the permits that they need, or provide services that secure non-problematic issuing of these permits by the public administration. The essence of the One-Stop-Shop concept - the provision of special advantages to investors during the execution of public administration -, thus threatens one of the fundamental principles emphasised in all human-rights protection documents: the principle of equality before the law.

2. CzechInvest has been creating an atmosphere that outright endorses conflicts of interests and corrupt behaviour.

The establishment of CzechInvest (in 1992) as the institutional basis for foreign investments promotion was a result (and an accomplishment) of the activities of what has been termed the "comprador service sector." This clearly identifiable group of people comprises certain executive officers (in particular officers from institutions connected to foreign capital) and local companies that provide legal and administrative services to foreign investors, such as the local branches of global consulting and legal advisory service firms, and their local competitors. The position of the comprador service sector was later on strengthened by the establishing of the Association for Foreign Investments (AFI) – an association that has, since its founding, been helping private entities such as auditing, legal, counselling, advisory, architectural, and translation companies join together. Both of these institutions, dominated by the comprador service sector, were then interconnected through a number of joint activities. The public and private sphere have thus been integrated through a variety of personal links, institutional channels, and material benefits.

3. The process of awarding investment incentives is set up badly; this leads to insufficient protection of public interests.

Representatives of CzechInvest took part in the preparation of legislation regarding investment incentives. While this may seem natural, they left dangerously large footprints on the legislation. It sets down very sparse legal restrictions against the awarding of investment incentives. They are especially sparse as regards restrictions related to possible threats that the investment would present towards various public interests. Moreover, they are sometimes even sparse as regards restrictions related to projects that would break the law. Thus, investment incentives have been often provided to projects whose implementation logically implies an infringement of at best the public interest, and at worst, the law.

In addition, it is CzechInvest who assesses companies' compliance with the legal requirements for receiving state incentives packages. Meanwhile, by its nature and as part of its specified duties, CzechInvest is obligated to support foreign direct investments, and provide such investors with free services. This is an obvious, institutionalized conflict of interest. CzechInvest cannot both be a service provider for FDI investors,

and be truly open to the possibility of doing them a disservice by objectively assessing (and possibly denying) the compliance of their state incentive requests with the law.

4. Unlawful obligations arising from agreements between investors and municipal authorities/the state have been negatively influencing the proper exercising of public administration.

Agreements between investors and municipal authorities/the state often contain obligations focused on removing various "administrative obstacles" and on ensuring that the investment can come to fruit in minimal time. The interest of the municipality or the state in successful completion of the investment project leads to a variety of promises within such agreements, such as promises to: collaborate as needed to obtain for the investor all necessary permits and approvals, or to refrain from all steps that could in any way threaten the project. In many cases, the agreements contain clauses that make implementation of the project conditional on the obtaining of all necessary permits, that determine such permits' contents, or that set a binding schedule for the permits to be issued. Contractual obligations of this sort imply by their very nature a willingness by said municipal/state authorities to interfere in the independent exercising of public administration. However, this goes contrary to the fundamental principles of such bodies' functioning, which do not allow intervention of this sort. For that reason clauses of this kind, when viewed through the law, can only be considered unlawful and void.

5. Systemic prejudice: cases where an official makes a decision about a request that was submitted by his employer.

The construction of industrial zones is often performed by municipal authorities directly and is funded from the state or municipal budget and CzechInvest grant programs. Municipalities usually (on behalf of themselves or of the investor) submit requests for the issuing of the necessary permits to their own officials. This creates a situation where the official has to decide whether or not to issue a permit for his own employer, or at least for an investor whose project is supported by his employer (by way of a contractual obligation). Such an official thus obviously cannot decide the issue objectively and without prejudice -- cannot decide it in accordance with the law. This conceptual problem - the conflict of interests generated by the situation where municipality employees decide on issues that directly affect their own economical, political or other interests, is termed "systemic prejudice."

6. Limited enforcement of the law: court suits brought by the affected public against the issuing of construction permits are being decided at the time when said construction is already complete.

Investors are deliberately contributing to the unlawfulness of the construction permits granting process – typically by signing unlawful agreements with the state or municipal authorities. Although the unlawful permits can be later reversed by the courts, investors still run no risks here. Even when suits have been submitted by the affected public, judges have rarely ruled for preliminary measures, injunctions or similar measures. Thus, court rulings are often being delivered at a moment when construction is already complete (often months or years after the cases in question were submitted).

The effective protection of the rights of the affected public or other public interests is thus diminished. This is underlined by the fact that it has been almost impossible to achieve the removal of unlawfully built structures, even in cases where their permits have been annulled by the courts. With regard to the diction of the Czech Building Code and its application in practice, it can hardly be assumed that proceedings for the removal of structures will even commence in such cases.

GARDE-EPS proposes the following measures as a solution for the systemic problems connected with the promotion of foreign investments (and many domestic ones as well) in the Czech Republic:

Proposals regarding CzechInvest and the investment incentives system:

- establish a joint committee (with the participation of all concerned ministries) that assesses and decides upon all requests for investment incentives, under the Czech laws/procedures for the institution typically translated as "administrative proceedings."
- introduce legislation that will allow the public to actively participate in these investment-incentives proceedings.

- make an assessment of proposed incentives' effectiveness be a part of these investment-incentives proceedings.
- require application of the Environmental Impact Assessment (EIA) process before the final decision on the incentive.
- require that CzechInvest relinquish its membership in AFI.
- require that CzechInvest and AFI cease cooperating to organize informal meetings between head executive officers and business representatives, increase the transparency of the informal meetings mentioned above.
- update the Czech conflict of interests act (Act no. 159/2006) in such a way that:
 - *it will directly prohibit and sanction the situation where a public official uses their position or power, or information acquired while in office, to obtain a pecuniary or other benefit for themselves or another person,*
 - *suspension from one's office will be added as a possible sanction,*
 - *selected public officials will receive the obligation of maintaining a publicly accessible itinerary containing their entire planned and expected agenda; this obligation must be secured by an adequate sanctions system.*
- introduce direct legal regulation of lobbying
- apply a non-competition clause to the employment contracts of CzechInvest employees. Such clause should limit the employment of CzechInvest staff at corporations that they were in contact with during their engagement in CzechInvest.

Proposals strengthening the independence of public administration and law enforcement:

- apply lower criteria for awarding preliminary measures (injunctions) and similar measures in cases where an affected public is suing to challenge permits related to implementation of an investment project
- expand the range of valid legal reasons for removing existing structures in situations where a building permit was reversed by court decision and the developer has actively participated in the unlawfulness of the permit process
- adopt a legal institution that will eliminate the risk of systemic prejudice. Such an institution was included in the original draft of the Czech Administrative Code, but later it was removed from the final version:
 - *in cases where a request by a municipal authority would be decided by its own officials, then another office subordinated to the same superior administrative body as that authority will undertake the proceedings instead*
- adopt legislation governing civil employees' duties towards the state administration (a Civil Service Act) with the aim of reducing the influence of local (or national) politicians on the performance of public administration

A detailed analysis of the problems connected with the promotion of foreign investments, including a number of concrete examples, can be found in a publication written by Pavel Franc and Jiri Nezhyba entitled "*Foreign direct investments and CzechInvest as the factors destabilizing democratic legally consistent state,*" published by GARDE-EPS in September 2007 (in Czech, 56 pp., PDF, 2.4 MB). The publication is downloadable for free from www.responsibility.cz.

GARDE (Global Alliance for Responsibility, Democracy and Equity) is a program of the Environmental Law Service (ELS), the largest non-profit public interest law organization in the EU.

GARDE is intended to serve as a response to the rapid societal changes connected to globalization processes, and therefore one of its focuses is identifying the key issues surrounding these changes. But its primary aim is to help people who are harmed by the negative impacts of globalization, by providing them with free legal aid. With the above in mind, GARDE decided after its founding that corporate accountability was the first important issue to address. Therefore, our mission is to hold corporations responsible.

Our core activity is strategic litigation. We stand up to large multinationals in cases of environmental and human-rights infractions. Further, using the practical experience we have earned, we try to promote systemic changes, both at the EU level and in the Czech Republic. GARDE is unique in its activities in the CEE region. There is no other organisation systematically working on corporate accountability and corporate social responsibility from this critical point of view, and connecting both topics together.

GARDE's main activities are:

- Legal aid to communities and individuals negatively affected by multinationals' foreign direct investment in the Czech Republic.
- Legal aid to employees discriminated against by multinationals.
- Using consumer rights to hold corporations accountable.
- Promoting transparent relationships between the private and public sector in the Czech Republic.
- Raising awareness about corporate accountability and corporate social responsibility and problems connected with them in the EU

Contact:

GARDE - Environmental Law Service
Dvořákova 13
602 00 Brno
Czech Republic

tel: +420 545 575 229
fax: +420 542 213 373
e-mail: brno@eps.cz
www.responsibility.cz, www.eps.cz