Banning investments in cluster munitions producers

National legislation

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Cover photograph
MZD2 submunition fired from a 122mm rocket
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Introduction

On 3 and 4 December 2008, a group of 94 states signed the Convention on Cluster Munitions (CCM), which categorically prohibits the use, production, transfer and stockpiling of cluster munitions. Driven by a commitment to end the humanitarian harm caused by cluster munitions, more than 113 states have joined the CCM by now and 84 are full States Parties bound by all its obligations. But why would one ban a weapon for the humanitarian harm it causes, yet continue to allow for investments in companies that produce them abroad?

Article 1(1)(c) of the Convention on Cluster Munitions states: “Each State Party undertakes never under any circumstances to assist, encourage or induce anyone to engage in any activity prohibited to a State Party under this Convention.”

The Cluster Munition Coalition and a growing group of states interpret the prohibition on assistance in the Convention on Cluster Munitions to include a prohibition on investments in cluster munitions. Investment would amount to assistance with production of cluster munitions, which is prohibited under the convention. Several CCM signatories have already made interpretive statements that identify investment in cluster munitions as prohibited under the CCM and/or have implemented laws that prohibit investments in cluster munitions.

This background paper serves as a “positive example guide”. Legal systems differ per state and existing national legal systems will dictate how a state will design and implement laws in general. By looking at strong components in existing laws that prohibit investment in cluster munitions, however, we strive to inspire states to pass their own disinvestment laws and build on the strong examples that already exist.

At the time of writing, nine states have adopted legislation that prohibits (various forms of) investments in cluster munitions: Belgium, Ireland, Italy, Liechtenstein, Luxembourg, the Netherlands, New Zealand, Samoa and Switzerland.

It is vital that more states confirm that article 1(1)(c) encompasses a ban on investment in cluster munitions. States should make this explicit by banning investments in cluster munitions producers in national legislation. Experience with the legislation in Belgium, Ireland, Italy, Liechtenstein, Luxembourg, the Netherlands, New Zealand, Samoa and Switzerland can serve as an example for all states, both States Party to the CCM and States not Party, to prohibit investment in cluster munitions producers by national law. A prohibition on investments in cluster munitions producers can be included as part of the ratification of the CCM or of national implementation legislation required under Article 9 of the convention, or can be covered in separate laws.

This paper outlines examples of existing disinvestment legislation. The existing investment prohibitions in Belgium, Ireland, Italy, Liechtenstein, Luxembourg, the Netherlands, New Zealand, Samoa and Switzerland are diverse in scope. These investment bans contain both positive elements as well as elements that leave room for clarification and/or could have been more encompassing. Although these existing bans are not fully encompassing they do all
contain strong elements which could be of example for other states when drafting disinvestment legislation. To assist other states to create comprehensive legislation to ban all forms of investments in cluster munitions producers, we highlight the strong components of existing legislation on disinvestment in this background paper.

In order to be comprehensive, and stem all investment flows to producers of cluster munitions and to provide clarity to financial institutions, national legislation should address the following questions:

1. **What should a ban on investment include?**
   The definition of cluster munitions producers should be as comprehensive as possible.

2. **What is meant by ‘investment’ or ‘financing’?**
   The legislation should prohibit any kind of financial or investment link or service offered to producers of cluster munitions.

3. **To whom does the investment ban apply?**
   In order to create a complete ban on investment, legislation should make clear that any investment by any party is prohibited.

4. **How is the legislation enforced?**
   Legislation on disinvestment is powerless without monitoring the implementation thereof, whether by public institutions, ethical councils or other actors explicitly assigned to audit the implementation of the law.

By taking good examples from existing legislation we hope to facilitate sharing of experience amongst states and encourage states to work towards strong national legislation to ban investments in cluster munitions producers.

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1 Art. 7 (1) of the Italian implementation law criminalizes financial assistance to acts that are prohibited by the No. 95 legislation. A draft bill was submitted to the Senate on 26 May 2010 to create separate legislation with a specific prohibition on the “financing of the production, use, repair, promotion, sale, distribution, import, export, storage, possession, or transport of antipersonnel mines and cluster bombs and submunitions thereof.”

2 Additionally, 27 states have not yet passed legislation against investment in cluster munitions producers but did express the view that investments in cluster munitions are prohibited by the CCM. Australia, Bosnia and Herzegovina, Canada, Cameroon, Colombia, the Democratic Republic of Congo (DRC), the Republic of Congo, Croatia, the Czech Republic, France, Ghana, Guatemala, the Holy See, Hungary, Lao PDR, Lebanon, Madagascar, Malawi, Malta, Mexico, Niger, Norway, Rwanda, Senegal, Slovenia, the United Kingdom and Zambia.
1. What should a ban on investment include?

1.1. The legislation should ban investment in producers, not just production

Legislation should prohibit the financing of cluster munitions producers, i.e. the company as a whole, rather than the financing of cluster munitions production. Since companies’ financial structures allow reallocation of funds and other assets internally, all investment in a company that produces cluster munitions or their key components needs to be banned. Otherwise capital can always potentially contribute, directly or indirectly, to the production of cluster munitions. For example, profit from one production line can be invested in other production lines; and money for general corporate purposes can be used for any of the company’s activities. Money invested in general corporate capital can therefore free money to invest in the production of cluster munitions, even if an investor requests a guarantee that its specific money or investment will not be used for cluster munitions.

Example from existing legislation

“[…] a company […] which is involved in the manufacture, use, repair, marketing, sale, distribution, import, export, stockpiling or transportation of [anti-personnel mines and or] sub-munitions […] and with a view to distribution thereof.”

(Belgium, 2007)

1.2. The definition of cluster munitions producers should be as comprehensive as possible

As explained under 1.1., legislation should prohibit investment in cluster munitions producing companies as a whole, not solely the production of cluster munitions.

A ban should consider a company or group of companies to be a cluster munitions producer when any part, however small, of its total turnover is derived from producing (key components for) cluster munitions or explosive submunitions, according to the definitions of the Convention on Cluster Munitions (CCM)³, regardless of the nature of the company’s other activities. This is important, because most companies that produce cluster munitions also produce other defence and/or civil products. All cluster munitions producers should be excluded from investment, however small a part of its turnover is derived from cluster munitions. Even if a company only gets 1% of its turnover from cluster munitions, this 1% can represent a considerable amount of money and can mean the production of large numbers of cluster munitions.
We therefore define a cluster munitions producer as follows:

- Any company or group of companies that, in its own name or through a subsidiary, develops or produces cluster munitions and/or explosive submunitions according to the definitions in the CCM.

- Any company or group of companies that, in its own name or through a subsidiary, develops or produces key components of cluster munitions or explosive submunitions. Key components are components which form an integral and indispensable part of the cluster munitions or explosive submunition.

In drawing up disinvestment legislation, the definition of a cluster munitions producers should be as comprehensive as possible and should encompass the production of submunitions as well as key components.

Example from existing legislation

“Whoever […] develops, produces, acquires in any way, […] cluster munitions or parts thereof […]”

(Italy, 2011)

1.3. The legislation should extend to cluster munitions producers abroad

All States Parties to the CCM must prohibit companies under their jurisdiction or control from producing or developing cluster munitions. Therefore, a ban on investments for CCM states means that it should stem investments going to producers of cluster munitions elsewhere, since domestic companies are no longer allowed to produce or develop cluster munitions anyway. Legislation to ban investments in cluster munitions producers should thus explicitly mention that the scope of the law extends to producers abroad.

Example from existing legislation

“[…] any national or foreign enterprise which produces, sells or distributes cluster munitions.”

(The Netherlands, 2013)
**Subsidiaries**

It is important that national disinvestment legislation prohibits investment in any company or group of companies that, in its own name or through a subsidiary, develops or produces cluster munitions and/or explosive submunitions, or key components thereof, according to the definitions in the Convention on Cluster Munitions. Otherwise, the company group could simply refer activities to a subsidiary, while retaining the liberty to internally allocate funds to the subsidiary.

Both the Belgian and the Dutch legislation acknowledge that it is needed to include subsidiaries. However, in this regard the two laws apply only to enterprises “holding more than half of the share capital” of a company involved in cluster munitions.7

We consider it undesirable to allow for investments in a company that holds any share at all in a cluster munitions producer. Economic reality dictates that even holding a 5% share in listed companies nowadays could be enough to become the leading share holder. When one holds shares, one is partial owner of the company and all its assets. When one invests in a company that holds a minority stake in a company producing cluster munitions, the investor buys part of the minority share in that producer.

Furthermore, there is no way to prevent the company with the minority stake from reallocating its capital to the cluster munitions producer. This is undesirable and runs counter to the purpose to shun investment in cluster munitions producers as a whole.
2. What is meant by ‘investment’ or ‘financing’?

2.1. The legislation should ban any financial or investment link or service to producers of cluster munitions

Legislation should prohibit investment in all its forms, including any financial or investment link with or financial service to cluster munitions producers. It is quite difficult to list all forms of (future) possible financial assistance. It may include equity securities (including shares), debt securities (including bonds), loans, bank guarantees, products of third parties, investments made on behalf of clients, discretionary mandates, index-funds, derivatives, etc. Although it might be advisable to use such lists as examples of financial assistance or investments banned by the law, it is recommended not to present lists of financial activities as comprehensive lists, as any list risks leaving out certain activities.

Example from existing legislation
“A person commits an offence who provided or invests funds with the intention that the funds be used […] in the development or production of cluster munitions.”
“It means assets of every kind, whether tangible or intangible, moveable or immovable, however acquired; and includes legal documents or instruments (for example bank credits, travellers’ cheques, bank cheques, money orders, shares, securities, bonds, drafts, and letter of credit) in any form (for example, in electronic or digital form) evidencing title to, or an interest in, assets of any kind.”
(New Zealand, 2009)

2.2. The legislation should ban all investment: no differentiation between direct and indirect investment

Legislation should encompass all financial assistance to producers of cluster munitions. Therefore, a ban should not differentiate between so-called direct and indirect investments. Furthermore, because it is often not clear who means what with ‘direct’ and ‘indirect’ it troubles implementation of the law. However, if differentiation would be incorporated in legislation, it should be defined clearly what is meant with direct and indirect financing or investments, as the terms are used differently by different actors.

To completely ban financial support to cluster munitions producers, the legislation should include all investments (both direct and indirect investment), regardless of the definition therefore, otherwise it runs the risk of leaving out certain types of investments. The simplest way to do so is to avoid the difference between direct and indirect investment altogether.
Example from existing legislation

“Nothing in any enactment that authorises the investment of public money shall be taken to authorise any investment, direct or indirect, in a munitions company.”

(Ireland, 2008)

2.3. The legislation should contain clear stipulations about ongoing contracts

Legislation banning investment in cluster munitions producers is aimed at preventing future funding of companies that produce or develop these weapons. However, it is important that legislation clearly stipulates how and in which timeframe investors should dispose of ongoing contracts or current existing investments.

Example from existing legislation

“In the event that a company which has already been granted financing (…) this financing should, insofar as contractually possible, be fully terminated.”

(Belgium, 2007)

There is no clear, ‘universal’ definition of ‘direct’ and ‘indirect’ financing. With regard to ‘direct’ investments, some might consider direct financing to be the provision of loans and specific banking services, leaving out asset management. Some might consider direct investment to constitute investments for the own account of a financial institution, leaving out certain types of asset management and investments made on behalf of clients. Yet, regardless of the definition issue of direct and indirect investments, a disinvestment ban should apply to all types of investments in order to prevent money going to companies that produce cluster munitions.

For a paper on different interpretations of “direct and indirect” investments, see “The scope of bank’s sustainable investment policies- the issue of direct and indirect investments” by FairFin, available on http://www.stopexplosiveinvestments.org/uploads/pdf/Direct%20and%20indirect%20investments.pdf.
3. To whom does the legislation apply?

3.1. **The legislation should make it clear that it prohibits any investment by any party.**

In order to create a complete ban on investment in cluster munitions producers, the legislation should make clear that *any investment by any party* is prohibited. In order to not only promote compliance with the ban, but also to provide clarity and understanding for investors which companies should be excluded from investments, it is highly recommendable for the legislator to create an exclusion list (see point 4.2.).

**Example from existing legislation**

“Whoever [...] develops, produces, acquires in any way, stores, retains, or transfers, directly or indirectly, cluster munitions or parts thereof, or financially assists, […].”

(Italy, 2011)
4. How should the legislation be enforced?

4.1. The legislation should provide supervision and monitoring tools

Legislation on disinvestment from cluster munitions producers is powerless without the monitoring of investments, whether by public institutions, by ethical councils or by other actors explicitly assigned to audit the implementation of the law.

Example from existing legislation

The explanatory notes of the Dutch law (2013) explicitly refer to the structural compliance costs “[…] in providing a supervisory body with evidence that efforts are made to avoid investments in enterprises that produce, sell or distribute cluster munitions.”12 The Dutch legislation (2013) e.g. is part of the Financial Supervision Act, the supervision therefore is defined in a broader institutional context and falls under the authority of the Netherlands Authority for the Financial Markets (AFM).

(The Netherlands, 2013)

4.2. The legislation should provide for a public list of companies falling under the ban

Monitoring is only possible with a clear agreement about the definition of cluster munitions producers, which is why it is recommendable to publish an exclusion list of companies falling under the ban. This will furthermore provide clarity to investors about which companies are off limits for investment due to involvement with cluster munitions.

Example from existing legislation

“To this end the King shall […] prepare a public list
i) of companies that have shown to carry out an activity as under the previous paragraph,
ii) of companies holding more than half the shares of a company under i) and
iii) of collective investments institutions holding financial instruments of companies as designated under i) and ii)”13

(Belgium, 2007)
4.3. The legislation should contain penalties

Legislation on disinvestment from cluster munitions producers should contain penalties to promote compliance. Clear examples of penalties can be found in for example the legislation of Italy (2011), Liechtenstein (2013), Luxembourg (2009) and Switzerland (2013).

Example from existing legislation

“Art. 35b Offences against the prohibition of financing
1 Any person who wilfully fails to comply with the prohibition on financing […] without being able to invoke an exception […] is liable to a custodial sentence not exceeding five years or to a monetary penalty.”
(Switzerland, 2013)

“Those who knowingly breach articles 2 or 3 can be penalised with 5 to 10 years detention and a fine ranging from €25,000 to €1 million.” 14
(Luxembourg, 2009)

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14 It is important to note that although the provision in the Belgian law is strong, until today no exclusion list was published, which weakens the implementation practice of the Belgian law.
Conclusion

Article 1(1)(c) of the CCM states: “Each State Party undertakes never under any circumstances to assist, encourage or induce anyone to engage in any activity prohibited to a State Party under this Convention.” A growing group of over two dozen CCM countries have already made interpretive statements that identify investment in cluster munitions as prohibited under the CCM. Additionally, nine states have currently implemented laws that explicitly prohibit (forms of) investments in cluster munitions.

Cluster munitions continue to be produced in some states that have not yet outlawed these weapons. Although States Parties to the CCM must stop producing cluster munitions, some banks and other financial institutions in or from these states may continue to fund their production by investing in corporations that manufacture them elsewhere. Investing in a cluster munitions producer supports the development and production of these weapons that cause unacceptable harm.

Any governmental effort to oppose the unacceptable humanitarian harm that cluster munitions cause should include efforts to dry up the supply capital that funds cluster munitions producers. Therefore, states should explicitly acknowledge that the treaty prohibits investments cluster munitions under the prohibition on assistance under article 1(1)c and should install legislation that prohibits investments in companies that develop and/or produce cluster munitions or key components thereof.

Because disinvestment is a shared responsibility, we see the need for governments to issue clear guidelines or laws. We hope that this background paper has provided information on positive elements of existing disinvestment legislation and that it will aid states in drawing up a comprehensive prohibition on investments in cluster munitions producers.
References


