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Recommended Features of a Foreign Investment Code for Cuba's Free Market Transition

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Recommended Features of a Foreign Investment Code for Cuba's Free Market Transition

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Recommended Features of a Foreign Investment Code for Cuba's Free Market Transition

Matias F. Travieso-Diaz, Esq. & Alejandro Ferrate, Esq.[†]

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I. Introduction

Foreign investment, and foreign direct investment in particular,¹ has in recent times been the driving force behind the growth and restructuring of formerly sheltered economies, and has also served as a vehicle for the internationalization of many of those economies.² Even though its economy remains under tight government controls, Cuba has recently joined the global trend towards encouraging foreign investment. Cuban officials, as well as students of Cuban affairs on the island and abroad, point to foreign investment as an important source of hard currency and as one of the principal mechanisms on which the current government relies to reverse the contraction of the country's economy.³

New laws, regulations and practices implemented in the last few years have succeeded in attracting a sizeable amount of foreign

¹ Direct investment is defined as the establishment of a permanent relationship between a party (the investor) and the object (some business operation), with the party seeking to exert real influence over the object's operation. Foreign direct investment is the acquisition of a lasting interest in an economy other than that of the investor. The definition of foreign direct investment includes, in addition to actual investment transactions, extended trade credits from a parent company to a foreign subsidiary; acquisition of shares of a foreign enterprise; loans from a parent to its foreign subsidiary; a parent company's guarantee of a subsidiary's loan; and self-financing over and above the normal consolidation requirements. The aim of foreign direct investment according to the IMF definition is to "acquire a lasting interest in an enterprise operating in an economy other than that of the investor, the investor's purpose being to have an effective voice in the management of the enterprise." Lars Oxelheim, *Foreign Direct Investments and the Liberalization of Capital Movements*, in THE GLOBAL RACE FOR FOREIGN DIRECT INVESTMENT 11 n.1 (Lars Oxelheim ed., 1993) [hereinafter THE GLOBAL RACE FOR FOREIGN DIRECT INVESTMENT].

² *Id.* at 1.

³ Jorge Perez-Lopez, *A Critical Look at Cuba's Foreign Investment Program* 1-4, paper presented at the 1995 Meeting of the Latin American Studies Association, Washington, D.C. (Sept. 1995) [hereinafter *Critical Look*]; see also Carmelo Mesa-Lago, *Cuba's Economic Strategies for Confronting the Crisis*, in CUBA AFTER THE COLD WAR 200-03 (Carmelo Mesa-Lago ed., 1993) [hereinafter *Confronting the Crisis*]. A Cuban government official recently described succinctly what Cuba seeks to get from foreign investments in the island as "market, technology and working capital." *Minister Says Light Industry to Undergo Reshaping Process*, PRENSA LATINA, June 5, 1995, translated in BBC SUMMARY OF WORLD BROADCASTS, June 13, 1995, available in LEXIS, News Library, Bbcswb File.

investment into Cuba.⁴ Foreign investment in Cuba has bolstered certain economic sectors, particularly tourism, and has served to expand the island's economic relations with other countries.⁵ The impact of foreign investment in Cuba is, however, limited by the country's political and economic program, which restrains foreign investment in a number of significant respects.⁶

As Cuba makes its transition to a free-market economy, foreign investment will play an increasingly important role in the island's economic reconstruction.⁷ Cuba's laws affecting foreign investment need to be updated as the transition unfolds to effectively regulate, and at the same time foster, foreign investment in the country.

⁴ Cuban officials have claimed that the aggregate value of foreign investment in the country as of mid-1995 amounted to over \$2 billion. *Cuba Reports Foreign Investment Exceeding \$2 Bn*, REUTERS, July 10, 1995, available in LEXIS, News Library, TTXNEWS File; *Trade Minister Reports Growth in GDP, Commercial Trade*, translated in BBC SUMMARY OF WORLD BROADCASTS, July 4, 1995, available in LEXIS, News Library, BCSWB File. These figures are probably quite overstated, since the total investment by a foreign venturer is usually not known, is spread out over a period of many years, and is contingent on many factors. The true figure of the amount invested thus far by foreign investors is probably closer to \$500 million. Thomas T. Vogel, Jr., *Investors Find Cuba Tantalizing Yet Murky in Financial Matters*, WALL ST. J., Aug. 7, 1995, at A1; *Critical Look*, supra note 3, at 4-13. For catalogues of foreign joint ventures in Cuba see *An Index of Foreign Investment in Cuba*, LA SOCIEDAD ECONOMICA, BULLETIN 43 (Sept. 1994); AMERICAN INSTITUTE FOR FREE LABOR DEVELOPMENT, AFL-CIO, OILING THE CUBAN GOVERNMENT MACHINE (Feb. 1995).

⁵ Prior to the current economic crisis, Cuba only encouraged what its officials called "social tourism," in which sympathetic travelers from around the world were invited to come to Cuba and were offered tours of model communes, sugar plantations, and other workplaces where the achievements of Castro's socialism were put on display. T. BABUN GROUP, INC., CUBA—SUMMARY OF OPPORTUNITY (Oct. 1994) (no page numbers in document) [hereinafter CUBA—SUMMARY OF OPPORTUNITY].

With the shift in emphasis to more traditional tourism in the late 1980s, the industry became the focus of attention of many foreign investors. Tourism is projected to bring about \$1 billion (gross) in foreign exchange to Cuba in 1995. Frances Kerry, *Cuba Forecasts Tripling of Tourism by Year 2000*, REUTERS BUSINESS REPORT, Apr. 27, 1995, available in LEXIS, News Library, REBUS File. Other export industries are also being increasingly pursued and are resulting in significant ventures by investors from many countries, notably Canada, Mexico, Spain, France, and other European nations. *Id.*; see generally Larry Luxner, *Investing in Cuba*, U.S./LATIN TRADE 38 (May 1994).

The United States is the only major country that is not involved in the expansion of foreign investment in Cuba. The lack of U.S. presence in Cuba is due to the existence of a tight embargo by the U.S. on trade with Cuba. This embargo was imposed in 1962 and remains in effect to this date. See generally 22 USC § 2151 et seq. (1963).

⁶ See *infra* part II.E.

⁷ See Ernest H. Preeg, *A Five Year Projection for a Restructured Cuba*, in CUBA IN TRANSITION—PAPERS AND PROCEEDINGS OF THE THIRD ANNUAL MEETING OF THE ASSOCIATION FOR THE STUDY OF THE CUBAN ECONOMY 153, 162 (Aug. 1993) [hereinafter ASCE-3]; ERNEST H. PREEG & JONATHAN D. LEVINE, CUBA AND THE NEW CARIBBEAN ECONOMIC ORDER 55-56 (Roberta Howard et. al. eds., 1993) [hereinafter PREEG & LEVINE]. Cuba is the largest country in the Caribbean and has the potential to become the largest U.S. trading partner in the region, once the sanctions have been lifted. THE ATLANTIC COUNCIL OF THE UNITED STATES, A ROAD MAP FOR RESTRUCTURING FUTURE U.S. RELATIONS WITH CUBA 19 (1995). The Atlantic Council study concludes that the level of trade will depend in large part on the extent to which Cuba is allowed access to U.S. markets as well as the availability of financing. *Id.*

This article seeks to identify what should be the objectives of Cuba's foreign investment legislation during its transition to a free-market economy and to describe the main features that such legislation should contain in order to maximize direct foreign investment in the island. Since foreign investment laws must be integrated with other economic development legislation, the paper also seeks to identify some of the key areas of interaction between foreign investment laws and other transition period legislation.

There is no "ideal" foreign investment code which could be copied for use in Cuba. Even if such legislation existed, it would probably be to a large extent inapplicable to Cuba due to the unique circumstances that will exist during the country's market transition.⁸ Certain features in foreign investment laws and related legislation, however, are recognized as creating an attractive climate for foreign investment. These favorable features have been analyzed by scholars and incorporated into general guidelines for investment legislation, such as the World Bank Guidelines on the Treatment of Foreign Direct Investment (hereinafter World Bank Guidelines).⁹ The successes and failures of countries making the transition from a command to a free-market economy also provide insights into the probable results of particular elements of foreign investment laws. These experiences should be considered for their potential applicability to Cuba.

The discussion in this article reflects the above considerations. Part II describes the foreign investment legislation that is in place in Cuba today and summarizes its main shortcomings. Part III defines what the objectives of foreign investment legislation for Cuba should be in order to support the country's orderly transition to a free-market economy. Part IV draws upon the preceding Part III to define the recommended features and requirements of foreign investment legislation for Cuba during its free-market transition. Part V discusses the relationship between Cuban foreign investment legislation and other transition period laws. Lastly, Part VI provides some pertinent conclusions and recommendations.

⁸ A number of conditions unique to Cuba make the foreign investment environment in the country potentially different from that of other countries with transitional economies. These unique conditions include (1) the existence of a very large Cuban exile community in the U.S., many of whose members are financially able to, and probably interested in, investing in their home country; (2) the close proximity of Cuba to a vast natural trading partner, the U.S.; (3) the pendency of expropriation claims by U.S. and Cuban nationals amounting to billions of dollars against much of the property that would be suitable for foreign investment; (4) the current critical economic condition of the country, which is likely to persist into the transition period; (5) the probability of political instability during the transition. See generally *Critical Look*, *supra* note 3, at 16-32.

⁹ IBRAHIM F. I. SHIHATA, *LEGAL TREATMENT OF FOREIGN INVESTMENT: THE WORLD BANK GUIDELINES 155-64 (1993)* [hereinafter *LEGAL TREATMENT OF FOREIGN INVESTMENT*].

II. Foreign Investment Legislation in Cuba Today

A. *The 1982 Foreign Investment Law: Opening the Door to Foreign Investment*

Cuba had no foreign investment laws in place at the time of the 1959 Revolution, nor for more than twenty years thereafter. The Cuban government issued the country's first foreign investment code in 1982, Decree-Law No. 50 of February 15, 1982 (Law 50).¹⁰ This legislation allowed foreign investors to enter into joint ventures with state-owned enterprises in the development of specific projects and authorized the repatriation of profits or dividends in convertible currency.¹¹ The law, however, imposed many restrictions on investors. For example, in certain cases, it limited a foreign investor's share in a joint venture to 49%, although investors could negotiate operational control of the project.¹²

Foreign investment in Cuba had been negligible since the early days of the Revolution, and the 1982 foreign investment law, in itself, failed to attract much foreign investment to the island.¹³ Indeed, the first foreign investment project in Cuba since the Revolution was completed in 1990, eight years after Law 50 went into effect.¹⁴

B. *The Post-1989 Liberalization of Foreign Investment in Cuba*

The year 1989 marked a watershed for the communist world: the iron curtain collapsed and the countries of the Soviet bloc started to make their transitions to democracy and free-market systems. That year also witnessed the beginning of the disintegration of the Soviet Union itself.¹⁵ The collapse of communism in Europe brought about

¹⁰ For a sympathetic description of the features of Law 50 and the business opportunities it created for foreign investors, see ADAR COMMUNICATIONS, *INVESTING IN CUBA TODAY* 21-29 (1993). But, for a discussion of the shortcomings of Law 50 see Jorge F. Perez-Lopez, *Odd Couples: Joint Ventures Between Foreign Capitalists and Cuban Socialists*, NORTH-SOUTH AGENDA PAPERS No. 16 (Nov. 1995) [hereinafter *Joint Ventures*].

¹¹ BUSINESS INTERNATIONAL CORPORATION, *DEVELOPING BUSINESS STRATEGIES FOR CUBA* 23-24 (1992) [hereinafter *BUSINESS STRATEGIES FOR CUBA*].

¹² *Id.* at 23.

¹³ Antonio Jorge & Robert D. Cruz, *Foreign Investment Opportunities in Cuba: Evaluating the Risks*, in *INVESTING IN CUBA: PROBLEMS AND PROSPECTS* 17, 26 (Jaime Suchlicki & Antonio Jorge eds., 1994) [hereinafter *Jorge & Cruz*]; *Critical Look*, *supra* note 3, at 1.

¹⁴ The first joint venture between the socialist regime and a capitalist firm since the Revolution was negotiated with the Spanish hotel chain of Sol-Meliá and resulted in the opening of a hotel in Varadero Beach in 1990. That hotel is 50% owned by the Spanish chain. *BUSINESS STRATEGIES FOR CUBA*, *supra* note 11, at 24.

¹⁵ Relations between Cuba and the Soviet Union began to deteriorate after the introduction of perestroika and *glasnost* in the latter country. In 1986, Cuba launched an economic counter-reform program (the Rectification Process) that set it against the worldwide socialist current of market reform. Though Cuba was critical of the reforms in other socialist countries, it continued to trade with and accept aid from the Soviet Union and

a steep decline in the Cuban economy, which was dependent on favorable trade relations with the nations of the Soviet bloc.¹⁶ In addition, all economic aid from the former Soviet Union was suspended in 1992 and trade was dramatically curtailed.¹⁷ As a result of these developments, Cuba's economic output declined by 50% between 1989 and 1993.¹⁸ During that period, the country's exports declined by 70%, imports dropped by 80%, and the gross domestic product decreased by somewhere between 30% and 40%.¹⁹

In response to the economic crisis, Cuba turned to foreign direct investment.²⁰ To attract such investment to the island, the government significantly liberalized its foreign investment practices.²¹ Amendments to the Cuban Constitution in 1992 eliminated some important restrictions on foreign investment. As amended, the Constitution permits property ownership by mixed enterprises and the transfer of state property to joint ventures with foreign capital.²²

These constitutional amendments enabled the institution of a more liberal foreign investment regime within the framework of Law 50.²³ As set up after 1992, the foreign investment regime had the following salient features:

other Soviet bloc nations. See generally Carmelo Mesa-Lago, *The Last Communist Warrior*, in CUBA AFTER THE COLD WAR, *supra* note 3, at 4-11.

¹⁶ Ariel Terrero, *Trade Statistics, New Measures Reported*, BOHEMIA 30-35 (Oct. 1994), translated in F.B.I.S. (LAT-94-234), Dec. 6, 1994 at 10; Carmelo Mesa-Lago, *The Economic Effects on Cuba of the Downfall of Socialism in the USSR and Eastern Europe*, in CUBA AFTER THE COLD WAR, [hereinafter MESA-LAGO ON THE DOWNFALL OF SOCIALISM], at 133-88.

¹⁷ MESA-LAGO ON THE DOWNFALL OF SOCIALISM, *supra* note 16, at 151; Berta E. Hernandez Truyol, *Out in Left Field: Cuba's Post-Cold War Strikeout*, 18 FORDHAM INT'L L. J. 15, 53 (1994).

¹⁸ See Jorge & Cruz, *supra* note 13, at 17.

¹⁹ See *Id.* at 24; GILLIAN GUNN, CUBA IN TRANSITION—OPTIONS FOR U.S. POLICY 28 (Gillian Gunn ed., 1993) [hereinafter CUBA IN TRANSITION]; COMISION ECONOMICA PARA AMERICA LATINA, CUBA: EVOLUCION ECONOMICA DURANTE 1994 17 (May 1995).

²⁰ CARMELO MESA-LAGO, ARE ECONOMIC REFORMS PROPELLING CUBA TO THE MARKET? 17 (1994) [hereinafter MESA-LAGO ON ECONOMIC REFORMS].

²¹ *Id.* at 34. In order to make itself more attractive to possible trading partners, the Cuban government began in 1989 to form business-oriented Sociedades Anonimas ("SAs"). SAs are state-owned enterprises, organized like corporations and acting in many respects like private companies (e.g., they hold foreign exchange in offshore accounts, serve as trading partners to foreign investors, and can hire and fire at will). See CUBA IN TRANSITION, *supra* note 19, at 34.

²² See CONSTITUCION DE LA REPUBLICA DE CUBA (1992) [Constitution] art. 23 (Cuba), published in Gaceta Oficial (Aug. 1, 1992) at 36 [hereinafter CONSTITUCION DE 1992]. Article 23 provides that:

The State recognizes the right of mixed enterprises, corporations and economic associations established in accordance with the law to own property. The use, enjoyment and disposition of the assets which are the property of the above mentioned enterprises shall be governed by the provisions of the laws and treaties, as well as by the enterprises' own articles of incorporation and bylaws.

²³ See Jorge & Cruz, *supra* note 13, at 26; GARETH JENKINS & LILA HAINES, CUBA: PROSPECTS FOR REFORM, TRADE AND INVESTMENT 65 (1994) [hereinafter CUBA PROSPECTS].

- 1) Foreign ownership of up to 49% of an enterprise's shares. (In special cases, such as tourism, mining, and Latin-America based investments, foreigners were allowed to own 51% or more of an enterprise's shares.);
- 2) Total exemption of taxes on gross income, personal income, and the transfer of real estate and businesses. The only taxes levied were 30% on profits and 25% on the payroll, to cover social security benefits for Cuban employees. Even those taxes could be waived or deferred at the discretion of the government;
- 3) Elimination of customs duties for necessary imports of equipment and inputs;
- 4) Unrestricted repatriation in hard currency of dividends, profits, and the salaries of foreign employees;
- 5) Freedom in hiring foreign executives and technical personnel;
- 6) State handling of the labor force, including disciplining of workers, a ban on strikes, and relatively low wages (to be paid in hard currency by the investor) for Cuban labor;
- 7) State insurance covering lost profits due to accident, non-payment of merchandise, and non-fulfillment of terms of contracts due to political conditions; and
- 8) Availability of government support in areas such as legal, economic, accounting, and information services.²⁴

In addition to the general arrangements described above, the Cuban government sought to negotiate special deals in which foreign investment played an important role.²⁵ Cuba has also signed bilateral investment treaties (BITs)²⁶ with several countries; these agreements contain, inter alia, promises not to expropriate investor property and to allow repatriation of investor profits.²⁷ These guarantees are intended to provide further assurances to foreign venturers that their investments are secure.²⁸

²⁴ MESA-LAGO ON ECONOMIC REFORMS, *supra* note 20, at 17; CUBA PROSPECTS, *supra* note 23, at 65-68.

²⁵ The Cuban Government has sought to negotiate debt-for-equity schemes to reduce some of its foreign debt obligations by offering some state enterprises to investors from creditor nations. For example, Cuba has converted part of its outstanding \$310 million debt to Mexico to equity by Mexican entrepreneurs in joint ventures: in September 1994, a contract was signed between Cubapetroleo, S.A. (Cubpet), and the Mexican enterprise of Mexpetrol under which Cubpet would keep 51% ownership of the joint venture, while Mexpetrol would have 49% ownership in exchange for a commitment to finish and upgrade the heavily underutilized oil refinery at Cienfuegos. In a similar agreement, Cemex, a Mexican cement manufacturer, reportedly invested \$40 million to purchase a one-half interest of the Mariel cement plant. Both of these ventures include significant debt-for-equity swap components. *Joint Ventures*, *supra* note 10, at 17; *Critical Look*, *supra* note 3, at 8-10.

²⁶ ALAN C. SWAN & JOHN F. MURPHY, CASES AND MATERIALS ON THE REGULATION OF INTERNATIONAL BUSINESS AND ECONOMIC RELATIONS 717 (1991).

²⁷ Michael Z. Wise, *The New Cuban Invasion*, INSTITUTIONAL INVESTOR, Feb. 1995, at 71. Cuba has signed BITs with Britain, China, Colombia, Germany, Italy, Russia, and Spain. *Id.*

²⁸ *Id.*; CUBA PROSPECTS, *supra* note 23, at 69-70.

C. Recent Foreign Investment Experience in Cuba

The entire Cuban economy, with the exception of health care and education, was declared open to foreign investment in 1994.²⁹ The main sectors where significant foreign investment has taken place include tourism, light industry, medical equipment and medicine production, mining, oil exploration, construction, and agro-industry.³⁰

Up to the present time, foreign investments in Cuba have taken one of three forms:

- 1) Joint ventures, in which a Cuban partner and a foreign partner invest jointly in a project. (This option includes management contracts, in which the foreign venturer provides the management skills to run the enterprise and the Cuban partner provides all or most capital assets—an arrangement particularly common in the tourism industry.);
- 2) Production agreements, in which Cuba supplies the labor and facilities and the foreign partner supplies equipment and materials, or provides advance credit. The foreign partner often becomes an exporter or distributor;
- 3) Joint accounts, in which the foreign partner manufactures and distributes abroad products designed in Cuba. Thus, the foreign partner assumes the risks but reaps the profits.³¹

The most commonly used format has been the formation of joint ventures between the foreign party and a Cuban enterprise which is either an existing state instrumentality or a “private” SA formed by the Cuban government.³² Over 200 such ventures have been established in the last five years.³³ While the foreign investor was generally not allowed to assume a majority interest in a joint venture, there have been a number of instances in which majority ownership by the foreign

²⁹ Roberto F. Campos, *Council of State's Lage on Expanding Foreign Investment*, PRENSA LATINA, Oct. 30, 1994, available in F.B.I.S. (LAT-94-210), Oct. 31, 1994 at 12-13. Despite these broad assertions, the areas of the economy available for foreign investment remain limited. Thus, Vice Minister for Foreign Investment Octavio Castillo stated recently: “The open features [of the new foreign investment law] do not commit in any case the capital or assets of sugar mills, railroads, machinery or even less the land. In other words, the country is still ours, under the old or the new legislation.” RADIO PROGRESO, Aug. 22, 1995, broadcast, on file with authors.

³⁰ See generally CUBA—SUMMARY OF OPPORTUNITY, *supra* note 5; CUBA PROSPECTS, *supra* note 23.

³¹ CUBA IN TRANSITION, *supra* note 19, at 33; *Critical Look*, *supra* note 3, at 7-11.

³² See generally Jorge Perez-Lopez, *The North-South Agenda Papers* (1995) [hereinafter *North-South Agenda Papers*].

³³ As of mid-1995, Cuba reported it had established 212 economic associations, including joint ventures, with foreign partners. *Cuba Reports Foreign Investment Exceeding \$2 Bn*, *supra* note 4. Spain leads the way in terms of the number of joint ventures undertaken by its nationals in Cuba, but Mexico and Canada surpass Spain in the reported total amount of investment. Jose A. Ferrs & Pascal Fletcher, *Spain Exploits Old Ties in New Havana—The Former Colonial Power is Helping to Lead the Way in Investment in Cuba*, FIN. TIMES, July 20, 1995, at 4.

venturer was approved.³⁴

Despite the post-1989 liberalization of Cuban foreign investment law, foreign investors still have had to cope with an abundance of risks and red tape. One of the shortcomings of Law 50 was that the joint ventures it authorized between foreign investors and state entities required case by case negotiation and individual approval by the Executive Committee of the Council of Ministers.³⁵ In addition, Cuban laws failed to provide explicit guarantees against expropriation—an important omission given the uncompensated expropriation of more than \$2 billion worth of foreign-owned assets in 1959 and 1960.³⁶ Foreign investors also had to contend with the possibility that the Cuban government might unilaterally terminate a venture—as apparently has happened in more than one case—or that an enterprise could become subject to a restitution claim deriving from the expropriation of foreign assets after the Revolution.³⁷

D. Cuba's New Foreign Investment Law

On September 5, 1995, Cuba's National Assembly of People's Power (the country's highest legislative body) enacted a new foreign investment law, Law No. 77 of 1995 ("Law 77"), to replace Law 50.³⁸

³⁴ Gareth Jenkins & Lila Haines, *Cuba: Prospects for Reform, Trade and Investment* (The Economist Intelligence Unit) (1994), at 67 [hereinafter *Prospects for Reform*].

³⁵ MESA-LAGO ON ECONOMIC REFORMS, *supra* note 20, at 17; Wise, *supra* note 27, at 71. The protracted foreign investment approval process was further delayed in mid-1995 when allegations surfaced that bribes and kickbacks were being paid to government officials by prospective investors in exchange for approvals. See, e.g., Christopher Marquis, *Cuba Takes a Hard Look at its Reforms*, THE MIAMI HERALD, Aug. 3, 1995, at 1A; Susana Lee, *Un Alerta Para Ser Mas Disciplinados, Austeros y Eficientes*, GRANMA, July 13, 1995, at 3; Michael McGuire & George de Lama, *Cuba Accountants New Guardians Against Corruption*, CHICAGO TRIB., July 17, 1995, at 1.

³⁶ Cuba expropriated most U.S. and other foreign-owned property on the island starting in 1959, with the bulk of the expropriations taking place in the second half of 1960. In a parallel process, most assets owned by Cuban nationals, except for small parcels of land, homes, and personal items were expropriated at various times between 1959 and 1968. See Matias F. Travieso-Diaz, *Some Legal and Practical Issues in the Resolution of Cuban Nationals' Expropriation Claims Against Cuba*, 16 U. PA. J. INT'L BUS. L. 217, 220 (1995) [hereinafter *Travieso-Diaz on Claims*].

³⁷ *Critical Look*, *supra* note 3, at 20, 24.

³⁸ LEY NUMERO 77 DE LA INVERSION EXTRANJERA, *published in Gaceta Oficial*, Sep. 6, 1995. The law went through at least seven drafts over the course of a year; the authors were able to review Drafts 3 (dated Mar. 13, 1995), 6 (dated June 8, 1995) and 7 (dated Aug. 25, 1995). A review of the incomplete "legislative history" of this law provides interesting insights into the political establishment's power to water down some of the more significant changes that were initially proposed to the country's foreign investment regime. For example, in Draft 3 the decision whether to approve a proposed investment was vested (except in enumerated areas) in the Ministry of Foreign Investment and Economic Cooperation (MINVEC). Law 77, Draft 3, art. 20 (on file with the authors). As finally enacted, foreign investment approvals are left, as they were under Law 50, in the hands of the Executive Committee of the Council of Ministers or some unspecified "Government Commission" it may designate. Law 77, art. 21. As these changes were being made, Cuban officials such as MINVEC Minister Ernesto Melendez continued to extol the innovative features of the new

Predictably, Law 77 does not represent a fresh start but retains many of the provisions as well as the generally restrictive investment climate of Law 50. However, some of the changes in Law 77 represent potentially significant improvements from the previous law, and if implemented could help liberalize the island's basic economic structure.³⁹

1. Major Similarities to Law 50

Law 77 retains the basic structure of Law 50. The familiar forms of business organization in Law 50 (joint ventures, production agreements, and joint accounts) are retained in the new law. But Law 77 also creates a new form of investment vehicle: the "enterprise with wholly foreign capital."⁴⁰

Approval of investments is still done on a case-by-case basis. The Ministry of Foreign Investment and Economic Cooperation is charged with supervising foreign investment activities, receiving foreign investment applications, and submitting them for approval to the Executive Committee of the Council of Ministers or to a yet to be established Commission appointed by that Committee.⁴¹ A decision on whether to approve an application must be reached within sixty days from the date of the application, and is not appealable.⁴²

The new law sets out to establish a centralized processing system by granting MINVEC primary authority to receive and evaluate the

law, stating inter alia that it would "establish more flexible mechanisms and specific regulatory elements to improve its clarity." *Minister Interviewed on Foreign Investment in Sugar, Real Estate, Banking*, translated in BBC SUMMARY OF WORLD BROADCASTS, June 20, 1995, available in LEXIS, News Library, Bbcswb File [hereinafter *Foreign Investment in Sugar*].

³⁹ Cuba's new law bears some similarities to the current Vietnamese foreign investment law. Thus, Vietnam's law, like Cuba's, also allows 100% foreign ownership of enterprises established in that country, guarantees rights of investors to repatriate invested capital and profits, and provides explicit guarantees against expropriation of foreign investments. Note, *Protection of Foreign Direct Investment in a New World Order: Vietnam—A Case Study*, 107 HARV. L. REV. 1995, 2003-05 (1994).

⁴⁰ Law 77, *supra* note 38, art. 12, 15. One aspect of Law 77 that caused considerable debate during its consideration by the National Assembly was its definition of foreign investor as "a natural or juridical person residing abroad and having foreign capital," a definition that potentially includes Cuba expatriates. *Id.*, art. 2(1). In his intervention in the debate of the new law, President Castro had to defend the inclusion of Cuban expatriates among potential investors. *Cuba Expected to Open Economy*, ASSOCIATED PRESS, Sept. 5, 1995.

⁴¹ Law 77, *supra* note 38, art. 21(1). The Executive Committee of the Council of Ministers retains the sole power to approve the most important types of new foreign investments, including those in which the total capital contribution is in excess of \$10 million; those in the form of enterprises with wholly foreign capital; those involving public works or services; those in which the foreign enterprise has foreign government participation; those involving the exploitation of natural resources; those involving the transfer of state assets or state-owned real estate; and investments involving military-owned enterprises. *Id.*, art. 21(2).

⁴² *Id.*, art. 23(6). The law does not specify how that 60-day approval deadline is to be enforced, particularly against the Executive Committee of the Council of Ministers; nor does it state the consequences of that deadline being missed. The law also does not address the pre-application process of negotiations between the investor and the authorities.

investment applications.⁴³ Nevertheless, authorization from the Council of Ministers, as well as from other interested state entities, will still be required.⁴⁴ The result is likely to be a continuation of the cumbersome and unpredictable approval process now in place.⁴⁵

The provisions on profit repatriation remain basically the same. Since the new foreign investment law contains provisions (discussed below) that commit the state to provide compensation in the event of expropriation and allow foreign investors to sell their shares in joint ventures, Law 77 lists moneys received pursuant to those provisions among the authorized forms of profit repatriation.⁴⁶ The new law also authorizes the repatriation in hard currency of any amounts received upon the winding up of the enterprise.⁴⁷

The new law generally retains Law 50's system of labor regulation for foreign investments. Enterprises with wholly foreign capital must still hire workers indirectly, that is, they must contract for labor with a designated state labor supply agency.⁴⁸ (As in the old law, foreign investors are free to employ foreigners in upper management and technical positions.⁴⁹) The state (via the labor supply agency) is still responsible for disciplining workers and for resolving disputes between foreign investors and their employees.⁵⁰ The foreign venturers must still pay wages in hard currency to the labor supply agency, which in turn pays the employees in pesos, thus pocketing the difference.⁵¹ Foreign employees, however, will continue to be able to repatriate their salaries in hard currencies.⁵²

The new code, however, creates a potential exception to the

⁴³ See *id.*, art. 20-25.

⁴⁴ The MINVEC is required to forward a summary of the foreign investment application to "such other agencies and instrumentalities as may be pertinent" to secure the views of these entities in the areas of their competence. *Id.*, art. 23(4).

⁴⁵ Foreign investment application approvals are contained in "investment authorizations," which are official documents that set forth the conditions to which the investment is subject, and the objectives and authorized duration of the investment. *Id.*, art. 24. The investor may seek clarification from MINVEC as to the conditions for the investment's approval. *Id.*, art. 25. The process of negotiating the terms of the venture and securing the investment authorization has been so dilatory in the past that it has caused a number of prospective investors to give up on their plans. Annet Cardenas Vega, *Foreign Investments: Business in Good Legislation*, PRENSA LATINA, Aug. 14, 1995, translated in BBC SUMMARY OF WORLD BROADCASTS, Aug. 22, 1995, available in LEXIS, News Library, Bbcswb File.

⁴⁶ Law 77, *supra* note 38, art. 3, 6 & 8.

⁴⁷ *Id.*, art. 4 & 8.

⁴⁸ *Id.*, art. 33(3). MINVEC is to designate an "employing enterprise" which will be responsible for hiring workers and contracting them out to the foreign investor. *Id.*

⁴⁹ *Id.*, art. 31(2).

⁵⁰ *Id.*, art. 34(1). However, in the event employee claims are settled by the labor supply agency, the agency has the right of indemnification against the foreign venturer. *Id.*, art. 34(2).

⁵¹ *Minister Explains Foreign Investment Law*, LA VANGUARDIA, Oct. 8, 1995, available in F.B.I.S. (LAT-95-198), Oct. 13, 1995, at 6-7.

⁵² MESA-LAGO ON ECONOMIC REFORMS, *supra* note 20, at 17.

official labor regime by stating ambiguously that a foreign investor in a joint venture with a Cuban partner may be authorized in exceptional cases to utilize a different labor arrangement from that specified in the law.⁵³

Finally, Law 77 maintains the existing tax structure for foreign investors. Foreign investors must pay taxes on net profits at 30% and payroll taxes at 25% to cover social security benefits.⁵⁴ The tax rate on profits for investments that exploit renewable or non-renewable natural resources can be increased by the Cuban Government up to 50%, depending on the natural resource being exploited.⁵⁵

The Ministry of Finance, in consultation with the MINVEC, can declare a foreign investment temporarily exempt from all or some of the applicable taxes.⁵⁶ Likewise, the new law states that special reductions in any applicable tariffs may be granted to foreign investors by Cuba's Customs Service on a case-by-case basis.⁵⁷ Thus, the tax regime for foreign investors under Law 77 remains as subject to the discretion of the government as it was under Law 50.

2. Significant New Provisions in Law 77

Perhaps the most significant new provision in Law 77 is an express guarantee against uncompensated expropriation of the property of foreign investors.⁵⁸ The state also promises to "protect" the investor

⁵³ Art. 33(1) of Law 77 states in pertinent part: "In exceptional cases, the authorization that approves a joint venture may stipulate that all or some of the persons rendering services to the joint venture may be hired directly by the venture, always in accordance with the terms of the laws in effect with respect to contracting labor." While there is no indication in the law or in the pronouncements of Cuban government officials as to when such an exceptional case might occur, it has been suggested that the existing labor regime may be modified in the free trade zones (further discussed below) which Cuba plans to open in the near future. *Cuba's Business Law Puts Off Foreigners*, WALL ST. J., Oct. 10, 1995, at A16.

There is also a residual provision regarding labor in art. 35 of Law 77, which reads: "The authorization that approves a foreign venture may set forth labor regulations that are different from those set forth in the preceding Articles." *Id.* It is unclear whether this additional provision further enlarges the exception set forth in art. 33.

⁵⁴ *Id.*, art. 39(a), (c). However, the Executive Committee of the Council of Ministers can, in cases where for reasons of national interest it deems it convenient to do so, waive wholly or in part the payment of net profit taxes to the extent those are reinvested in the country. *Id.* Joint ventures and economic association arrangements are exempt from payment of individual income taxes, whereas enterprises with wholly foreign capital are liable for those taxes. *Id.*, art. 39(d).

⁵⁵ *Id.*, art. 39(b).

⁵⁶ *Id.*, art. 43.

⁵⁷ *Id.*, art. 41.

⁵⁸ Article 3 of Law 77 reads:

Foreign investments in the national territory enjoy full protection and safety, and cannot be expropriated except for those actions taken for reasons of public utility or social interest, as declared by the Government in accordance with the Constitution and the laws in effect, and the Agreements for the Promotion and Reciprocal Protection of Investments, and subject to prior indemnification in freely convertible currency in an amount equal to the commercial value of the investment, as mutually agreed or as assessed by an international organization with recognized expertise in

against third party claims, to the extent such claims are in accordance with Cuba's laws and the rulings of Cuba's courts.⁵⁹ Compensation for expropriation is to be given in a convertible currency, although the amount and type of currency are left to be determined by agreement of the parties or, in the case of disagreement, by an experienced "international organization" chosen by the foreign investor in conjunction with MINVEC.⁶⁰

Another important new provision allows investments by "enterprises with wholly foreign capital"—that is, investments without Cuban equity participation.⁶¹ Such enterprises can be established in two different ways: 1) by the foreign individual or entity registering in its own name with the Chamber of Commerce of Cuba; or 2) by setting up a wholly-owned Cuban corporation as a subsidiary of the foreign entity.⁶²

Allowing foreign investors to operate as sole proprietorships or through wholly-owned subsidiaries not only expands the types of business organizations available to foreign investors but also moves Cuba's foreign investment legislation closer to internationally-recognized standards for foreign investment legislation. Experience in other countries shows that allowing 100% foreign ownership of enterprises is necessary to attract substantial amounts of foreign investment, particularly to countries with economies in transition.⁶³ If enterprises wholly owned by foreign investors are allowed to acquire the assets of state-owned enterprises, their doing so could signify the start of the privatization of state enterprises in Cuba.

The possibility that the Cuban government will allow the acquisition of state-owned assets by foreign investors raises issues regarding the status of title to properties expropriated after the 1959 Revolution. Cuban nationals and foreigners have outstanding property expropriation claims totaling billions of dollars.⁶⁴ The claims by U.S. nationals certified by the Foreign Claims Settlement Commission alone total \$1.8 billion in 1960 dollars, not counting interest.⁶⁵ If assets subject to

business valuation, authorized by the Minister of Finance and Prices and engaged for that purpose through agreement between the parties or by agreement between the investor and the MINVEC in the case of an enterprise with wholly foreign capital.

Id.

⁵⁹ *Id.*, art. 5.

⁶⁰ *Id.*, art. 3.

⁶¹ *Id.*, art. 12(c), 15.

⁶² *Id.*, art. 15(2). It should be noted, however, that President Castro has warned that very few businesses will be authorized to operate as 100% foreign-owned ventures. Douglas Farah, *Socialist Cuba Alters Course to Spur Foreign Investment*, WASH. POST, Sept. 6, 1995 at A25.

⁶³ See *infra* part IV.B.3.

⁶⁴ For a discussion of the Cuban expropriations and claims arising thereunder see Travieso-Diaz on Claims, *supra* note 36.

⁶⁵ *Id.*

expropriation claims were acquired by foreign investors, resolving the expropriation claims and delaying the lifting of the U.S. trade embargo against Cuba may be difficult because the resolution of the property claims of U.S. nationals is one of the conditions necessary to lift the embargo.⁶⁶

Another provision enables foreign investors to acquire interests in real estate, but only in limited situations and subject to the specific approval of Cuba's Council of Ministers.⁶⁷ Investments in real estate can only be made in structures intended as personal dwellings or vacation homes of non-resident foreign individuals, residences of foreign investor officials, or corporate offices.⁶⁸ The acquisition of structures does not include the acquisition of the underlying land. More importantly, the term "acquisition" is not defined, and the conditions under which the real estate is acquired are to be set in the authorization issued to the foreign investor and are therefore subject to ad-hoc determination by the Cuban authorities.⁶⁹ For all intents and purposes, the real estate rights acquired by investors are just long or medium term leases of the improvements.

⁶⁶ Matias F. Travieso-Diaz, *Requirements for Lifting the U.S. Trade Embargo Against Cuba* 23 (unpublished manuscript, on file with *The University of Miami Yearbook of International Law*) [hereinafter Travieso-Diaz on the Embargo]. To further complicate matters, on March 5, 1996, the United States enacted the Cuban Liberty and Democratic Solidarity Act of 1996, Pub. L. No. 104-114, 109 Stat. 785, popularly known as the "Helms-Burton Bill" or the "Libertad Act". Title III of the Libertad Act grants a right to U.S. nationals whose property was confiscated by the Cuban government to bring actions for money damages in U.S. federal district courts against foreign nationals or foreign governments that "traffic" in their confiscated properties. Trafficking is defined broadly as "knowingly and intentionally" selling, transferring, distributing, dispensing, brokering, managing, or otherwise disposing of confiscated property, or purchasing, leasing, receiving, possessing, obtaining control of, managing, using or otherwise acquiring or holding an interest in confiscated property; engaging in a commercial activity using or otherwise benefiting from confiscated property; or causing, directing, participating in or profiting from trafficking by another person or otherwise engaging in trafficking through another person, without the authorization of any United States national who holds a claim to the property. Libertad Act, 109 Stat. 785, at tit. III.

Initial reports following enactment of the Libertad Act suggest that a number of foreign investors operating in Cuba may withdraw from the island, and others who were considering investing in Cuba are likely to change their plans. Pascal Fletcher, *U.S. Embargo May Stall Foreign Cash*, FINANCIAL TIMES SURVEY OF LATIN AMERICA FINANCE AND INVESTMENT, Mar. 25, 1996, at vi; Pascal Fletcher, *Cuba Retreats Behind Hardline Policies*, FIN. TIMES, Mar. 28, 1996, at 6; Peter Morton, *Canadian Firms Face Cuba Fallout: Sweeping Power of U.S. Law Puts Corporations with Links to Havana on the Defensive*, FIN. POST, Mar. 13, 1996, at 1; Elena Cherney, *Mountain of Cuban Sugar is Anathema to Americans: Sweetening with the Enemy*, THE GAZETTE (Montreal), Mar. 16, 1996, at D1.

⁶⁷ Law 77, *supra* note 38, arts. 16, 21(2)(f).

⁶⁸ *Id.*, art. 16(2).

⁶⁹ *Id.*, art. 18. In a June 1995 interview, Cuba's foreign investment minister clarified that the real estate investments that are being allowed in Cuba involve only giving "usufructuary property rights to companies comprising Cuban and foreign partners without transferring property rights as established by our constitution . . . under no circumstance is the ownership of the property compromised." *Foreign Investment in Sugar*, *supra* note 38, at 7.

Finally, the new Cuban foreign investment law authorizes the establishment of a system of "duty-free and industrial park zones," which are a form of Export Processing Zones (EPZs).⁷⁰ Special incentives may be granted to enterprises located in these zones. These incentives are not defined in the law, but they are said to relate to "customs, currency exchange rates, taxes, labor, immigration, public order, investment and foreign trade."⁷¹ The types of activities which may be carried out in the duty-free zones include importation, exportation, storage, product modification, re-export and financial operations.⁷²

It is unlikely that the duty-free zones will attract large amounts of foreign investment. The worldwide performances of EPZs in attracting investment is said to have been lackluster.⁷³ In addition, the success of EPZs (particularly in the Caribbean) depends to a large extent on trade concessions from importing countries, which stimulate foreign investors to establish manufacturing facilities for export products (*maquiladoras*) in the EPZs.⁷⁴ An example of the effect of these concessions is the success of the Dominican Republic's EPZs in attracting apparel *maquiladoras* which take advantage of reduced quotas and import duties for their products under the United States Caribbean Basin Initiative (CBI) program. Operation of these EPZs is, at least in part, responsible for the tripling of the Dominican Republic's apparel exports between 1987 and 1991.⁷⁵ Cuba presently is not eligible for CBI benefits, and it will continue to be ineligible as long as current U.S. policy towards Cuba remains in effect.⁷⁶ In addition,

⁷⁰ Law 77, *supra* note 38, art. 50.

⁷¹ *Id.*, art. 51.

⁷² *Id.* Cuban officials have characterized the development of EPZs as something "for the future." *Head of Chamber of Commerce Assesses Foreign Investment*, PRENSA LATINA, June 7, 1995 translated in BBC SUMMARY OF WORLD BROADCASTS, June 20, 1995, available in LEXIS, Nexis Library, Bbcswb File. On the other hand, a bill for the creation of free zones and industrial parks is reported to be under review. *Creation of Free Zones, Industrial Parks Believed Possible*, RADIO REBELDE, Nov. 21, 1995, available in F.B.I.S. (LAT-95-227), Nov. 27, 1995, at 6.

⁷³ OECD, INVESTMENT INCENTIVES AND DISINCENTIVES: EFFECTS ON INTERNATIONAL DIRECT INVESTMENT 53 (1989) [hereinafter OECD on FDI].

⁷⁴ Alejandro Ferrate, *Foreign Direct Investment in Costa Rica after the "Death" of C.B.I.*, J. INT'L LEGAL STUD. (forthcoming Summer 1996).

⁷⁵ U.S. INTERNATIONAL TRADE COMMISSION, POTENTIAL EFFECTS OF A NORTH AMERICAN FREE TRADE AGREEMENT ON APPAREL INVESTMENT IN CBERA COUNTRIES 16-18 (1992) [hereinafter POTENTIAL EFFECTS OF NAFTA ON CBI].

⁷⁶ Travieso-Diaz on the Embargo, *supra* note 66, at 43. Under current legislation, the President cannot "designate a country as a CBI beneficiary 1) if it is a communist country; 2) if it has nationalized, expropriated, or seized U.S. property, or unduly infringed other property rights of U.S. citizens; 3) if it has not respected arbitration awards to U.S. parties; 4) if it affords preferential treatment to the products of another developed country which adversely affects U.S. commerce; 5) if its government violates U.S. copyrights; 6) unless it has agreed to extradite U.S. citizens; and 7) unless it is taking steps to afford internationally recognized worker rights." *Id.*

even if Cuba were eligible for CBI benefits, the conclusion of NAFTA and the phasing out of the Multi-Fiber Agreement quotas under the Uruguay Round of the GATT have severely impaired the value of CBI benefits as investment incentives in beneficiary countries.⁷⁷

E. Current Constraints on Foreign Investment in Cuba

The present state of Cuba's foreign investment law is not unlike that of similar laws in Central and Eastern European countries, such as Hungary, the former Czechoslovakia, and Poland, prior to their transition to free-market economies.⁷⁸ Like those countries, Cuba is still imposing constraints on foreign investment in order to control the investment process. In addition, there are external factors that prevent the widespread entry of foreign investment into Cuba.

1. Constraints Placed on Foreign Investment by Cuba

Despite the relative liberalization of Cuba's foreign investment law, there remain a number of restraints imposed by Cuba on foreign investment. The following significant restrictions are still in effect:⁷⁹

- a) Foreign joint ventures still have to be individually authorized by the Cuban government, in a process that in the past has been protracted and has involved successive reviews by several agencies, with Fidel Castro as the ultimate decision-maker in the approval of the venture. It does not appear that the new foreign investment law will do much to alleviate this problem;
- b) Until recently, ventures were only permitted in selected areas of the economy; other areas, like the sugar industry, were considered off-limits. Investment in sugar is now starting, but is still limited to the pre-financing of sugar crops and loans towards the acquisition of fuel, fertilizers, herbicides, spare parts, and other inputs rather than the transfer of ownership or control of productive assets which remain in the hands of the state;⁸⁰
- c) Investments directed at developing the internal Cuban market are generally not allowed because the objective of encouraging foreign investment is to secure foreign exchange via exports;

⁷⁷ See generally Renee T. Legierski, Note, *Out in the Cold: The Combined Effects of NAFTA and the MFA on the Caribbean Basin Textile Industry*, 2 MINN. J. GLOBAL TRADE 305 (1993).

⁷⁸ For example, up to 1988 foreign investors could only operate in Hungary as minority partners in joint ventures with domestic enterprises. ZBIGNIEW DOBOSIEWICZ, *FOREIGN INVESTMENT IN EASTERN EUROPE* 45 (1992).

⁷⁹ See generally *Critical Look*, *supra* note 3.

⁸⁰ See *Foreign Investment in Sugar*, *supra* note 38, at 3; see also *Sugar Slump Blights Improving Cuban Economy*, REUTERS, July 21, 1995; *Dutch ING Financing 20 Pct. of Cuban Sugar*, REUTERS, Apr. 4, 1995; *Mercedes-Benz Renews Commercial Operations in Country*, EFE, July 25, 1995. Pre-financing of Cuba's production of various commodities is now taking place with the backing of several European banks. Pascal Fletcher, *Western Banks Test the Waters in Cuba: Hopes are High that a Pioneering Presence Will Bring Later Gains*, FIN. TIMES, Aug. 15, 1995, at 4.

- d) Foreign investors are still not permitted to acquire title to the properties in which they invest;
- e) A joint venture can still be terminated by the Cuban government essentially at will, with all property in Cuba involved in the venture remaining in the hands of the state;
- f) Contacts between the foreign investor and the internal economy of the country, and the population at large, are rather limited;
- g) Foreign venturers cannot hire labor directly, but must choose from a government-selected pool of candidates. The joint venturer must pay the Cuban agency that supplies the labor relatively high salaries in convertible currency, while the agency pays workers low salaries in pesos;
- h) The Cuban Government remains in control over the investment process and can dictate arbitrarily the terms under which each investment is authorized and when it is to come to an end.

Thus, although the new foreign investment law may create a somewhat improved framework for foreign investment in the island, Cuba's successful transition to a free-market economy will require a far greater liberalization to the country's foreign investment regime than the new law provides. This has been demonstrated by the disappointing results thus far of the new legislation: no major new investments have been announced since Law 77 was enacted, and the amount of foreign investment going into Cuba remains limited.⁸¹

2. *External Constraints on Foreign Investment in Cuba*

In addition to the internal constraints on foreign investment presented by Cuba's current regulatory environment, foreign investment is hampered by two main types of external constraints. First, Cuba is largely isolated from the international monetary and financial system because of its massive external debt burden, which denies it access to international credit.⁸² Second, Cuba is cut off from the U.S. market because the United States maintains a stringent trade embargo against Cuba and actively seeks to discourage trade and investment on the island by other nations. While a detailed discussion of these constraints is outside the scope of this paper, brief mention will be made of them to complete the picture of the foreign investment outlook in Cuba.

a. *Cuba's External Debt*

Cuba's external debt situation is bleak. Even before the collapse of the Soviet Union, Cuba owed over \$9 billion (not counting accrued

⁸¹ *Cuba Business Law Puts Off Foreigners*, *supra* note 53; Peter Katel, *Doing Business by the Little Red Book*, WASH. TIMES, Dec. 10, 1995 at A9.

⁸² *Cuba Releases Details of its External Debt*, J. COM., Nov. 20, 1995, at A8.

interest) to international private and public lenders in the West, and had defaulted on its loan obligations.⁸³ As a result, Cuba is not eligible for credit from Paris Club members or private lenders.⁸⁴ Also, Cuba owes Russia, as successor to the Soviet Union, about \$30 billion in loans that it has never repaid.⁸⁵

Cuba is also not a member of the IMF⁸⁶ and does not receive export credits from foreign governments except for Spain and France, which are actively encouraging their nationals to do business in Cuba.⁸⁷ The country's inability to secure credit from the world's financial institutions restricts its ability to finance projects and limits both the number of investors and the types of investment projects that can be undertaken.

b. The U.S. Trade Embargo

The U.S. trade embargo is also a factor that restricts foreign investment in Cuba. The embargo prohibits U.S. individuals and companies, and their foreign subsidiaries, from doing business in Cuba.⁸⁸ Moreover, the U.S. pursues a policy of actively seeking to discourage third country entrepreneurs from investing in Cuba.⁸⁹

One of the arguments used by the U.S., sometimes effectively, to discourage third country investors from going into Cuba is that many of the joint ventures solicited by Cuba involve properties that were confiscated from U.S. citizens.⁹⁰ The U.S. warns that investment in such properties could lead to litigation against the investors now or in the event of a change of government in Cuba.⁹¹ Also, it is sometimes said that those investing in Cuba might be subject to adverse action by a successor government coming to power on the island.⁹²

⁸³ *Id.*; Mesa-Lago on the Downfall of Socialism, *supra* note 15, at 151; *see also* PREG & LEVINE, *supra* note 7, at 57.

⁸⁴ In 1986, Cuba unsuccessfully sought to renegotiate debt payments with its Paris Club creditors, and afterwards declared a moratorium on debt-services payments. Because of Cuba's drop in creditworthiness, it was forced to rely mostly on trade with socialist countries and to curtail sharply hard currency imports. ASCE-3, *supra* note 7, at 27. *See also* Thomas T. Vogel, Jr., *Cuba Seeks to Revamp Its Default Debt*, WALL ST. J., June 26, 1995, at C1.

⁸⁵ MESA-LAGO ON ECONOMIC REFORMS, *supra* note 20, at 5.

⁸⁶ CUBA IN TRANSITION, *supra* note 7, at 32.

⁸⁷ CUBA PROSPECTS, *supra* note 23, at 57.

⁸⁸ *Id.* at 39-42.

⁸⁹ *North-South Agenda Papers*, *supra* note 32, at 25.

⁹⁰ *Id.*

⁹¹ *Id.*

⁹² *See generally* Jorge & Cruz, *supra* note 13, at 38-42. Because of the perceived regulatory, political and economic risks of investing in Cuba, the island is regarded as a poor prospect by potential investors. *See, e.g., Doing Business by the Little Red Book*, *supra*, note 81. In its March 1995 semi-annual survey of country investment and credit risks, the magazine *Euromoney* ranked Cuba 183rd out of 187 countries surveyed in terms of investment and credit worthiness. The survey was based on the countries' existing debt burden, access to international financing, economic performance, and political risk. Cuba scored very low in all those categories. Charles Piggot, *U.S. Has Passed Its Peak*, EUROMONEY, Mar. 1995, at 149.

As noted earlier, recently enacted U.S. legislation—the Libertad Act—⁹³ greatly increases the potential for litigation in the U.S. against investors from other nations doing business in Cuba, and subjects such investors to potential sanctions in the areas of immigration, trade, and financing.⁹⁴ While the long-range effects of this legislation remain to be seen, it is likely that it will further cloud the picture for the third party nationals contemplating investing in Cuba.⁹⁵

III. Objectives of a Foreign Investment Code for a Country in Transition

Foreign investment legislation can seek two goals which are largely contradictory: on the one hand, enabling and fostering the entry of foreign investment; on the other, regulating and controlling such investment to minimize its adverse impacts on the host country. Which of these two goals is pursued at a given time depends on the philosophy of the government in power, as well as on prevailing political and economic conditions.

Until the last decade, a “provider mentality” pervaded most developing countries, particularly those with an abundance of natural resources. This mentality was based on the belief that having “an ample stock of natural resources was what made a country rich and its products competitive.”⁹⁶ This mentality caused many countries to effectively close their doors to perceived exploiters—investors from industrialized countries and multi-national corporations.⁹⁷ Thus, countries enacted laws that emphasized the regulatory and exclusionary aspects of foreign investment legislation and thereby tended to

⁹³ Cuban Liberty and Democratic Solidarity (Libertad) Act of 1996, Pub. L. No. 104-468, 109 Stat. 785 (1996).

⁹⁴ *Id.*

⁹⁵ Title III of the Libertad Act grants a right to U.S. nationals whose property was confiscated by the Cuban government to bring actions for money damages in U.S. federal district courts against foreign nationals or foreign governments that “traffic” in the confiscated properties, where “trafficking” is defined very broadly. Libertad Act, 109 Stat. 785, at tit. III.

Initial reports following enactment of the Libertad Act suggest that a number of foreign investors operating in Cuba may withdraw from the island, and others who were considering investing in Cuba are likely to change their plans. Pascal Fletcher, *U.S. Embargo May Stall Foreign Cash*, FINANCIAL TIMES SURVEY OF LATIN AMERICAN FINANCE AND INVESTMENT, Mar. 25, 1996, at vi; Pascal Fletcher, *Cuba Retreats Behind Hardline Policies*, FIN. TIMES, Mar. 28, 1996, at 6; Peter Morton, *Canadian Firms Face Cuba Fallout: Sweeping Power of U.S. Law Puts Corporations with Links to Havana on the Defensive*, FIN. POST, Mar. 13, 1996, at 1; Elena Cherney, *Mountain of Cuban Sugar is Anathema to Americans: Sweetening with the Enemy*, THE GAZETTE (Montreal), Mar. 16, 1996, at D1.

⁹⁶ See KENICHI OHMAE, *THE BORDERLESS WORLD: POWER AND STRATEGY IN THE INTERLINKED ECONOMY* 173 (1990) [hereinafter *BORDERLESS WORLD*].

⁹⁷ *Id.*

discourage, rather than stimulate investment.⁹⁸

Other countries, particularly those in the Pacific rim, started some time ago to shrug off the provider mentality and opened their markets to foreign investment. The results have been dramatic; countries like Malaysia have become active and successful participants in the global marketplace.⁹⁹ Their experiences are living proof of the wisdom of opening the door wide to foreign investment. Likewise, the successful experience of Central and Eastern European countries underscores the critical role of enabling foreign investment legislation in the rebuilding of the economies of countries in transition.¹⁰⁰

A. *Fundamental Pillars of Foreign Investment Legislation*

The main objective of an enabling foreign investment code is to create a legal and regulatory regime attractive to foreign investors.¹⁰¹ In order to achieve this goal, the foreign investment framework needs to meet at least three criteria: 1) it must provide for non-discriminatory, or "national," treatment of foreign investors; 2) it must grant adequate protection to foreign investor property; and 3) it must establish streamlined foreign investment regulations and procedures.¹⁰² These criteria represent the fundamental pillars of successful foreign investment legislation.

⁹⁸ One such country is Mexico. In 1918, the Mexican Constitution granted the federal government direct ownership of land and waters of the Mexican territory with a right to transfer title to private persons. Currently, the Foreign Investment Law of 1973, and the Constitution regulate foreign investment. Under the law, foreign investment equity in Mexican corporations could not exceed 49%. Moreover, specific activities were reserved solely for the federal government or Mexican investors. Any exception to the 49 percent ownership limitations were made only for special projects having the characteristics consistent with the government's economic policies. In May 1989, Mexico enacted new regulations that repealed all existing administrative regulations, decrees, and the Foreign Investment Commission's general resolutions. However, the 1973 Foreign Investment Law was not repealed. As a result of these measures, the foreign investment regime in Mexico became less restrictive than before, but still left the door open to reverting one day to a "provider mentality" investment climate. See Dionisio J. Kaye, *Mexico Liberalizing Foreign Investment*, 4 TEMP. INT'L. & COMP. L.J. 79 (1990).

⁹⁹ BORDERLESS WORLD, *supra* note 96, at 173-81.

¹⁰⁰ It may be argued that Cuba had no foreign investment code in place before the Revolution and enjoyed a significant influx of foreign investment, so a foreign investment code may not be necessary. A Cuba making its free-market transition, however, will face a totally different domestic and international set of circumstances than those which prevailed before 1959: the country will be impoverished and face strong competition for the attention of foreign investors from developing countries in Latin America, Asia, and elsewhere. Like virtually all countries making a transition from socialism to a free-market, Cuba will need an enabling foreign investment law to foster the entry of investment under those conditions.

¹⁰¹ LEGAL TREATMENT OF FOREIGN INVESTMENT, *supra* note 9, at 155.

¹⁰² These three criteria are a distillation of the recommendations in the World Bank's Guidelines on the Treatment of Foreign Direct Investment. See LEGAL TREATMENT OF FOREIGN INVESTMENT, *supra* note 9, at 155-64.

1. *National Treatment of Foreign Investors*

National treatment is a crucial element of a hospitable foreign investment regime.¹⁰³ National treatment means that foreign investors should not be put at a competitive disadvantage versus domestic investors regarding access to permits or authorizations necessary to conduct operations in the host country.¹⁰⁴ At the same time, the laws should not give foreign investors a competitive advantage over national investors, absent compelling circumstances. In other words, the laws should apply fairly and equally to all investors.

2. *Protection of Foreign Investors' Property*

Adequate protection of investor property is also a fundamental pillar of a favorable foreign investment climate. Such protection has several elements. The most obvious and important one is a guarantee against the uncompensated taking of investor property by the state.¹⁰⁵

Another type of protection that must be given to foreign investors is the avoidance of excessive taxation and other government actions that diminish the value of the investment.¹⁰⁶ Foreign investors should also be free from discriminatory treatment and should receive the same protection of their persons and property (including intellectual property rights) as that accorded to nationals.¹⁰⁷

¹⁰³ The right of national treatment obligates countries to treat foreigners as they would their own nationals under their own laws. CHERYL W. GRAY, WORLD BANK DISCUSSION PAPERS VOL. 209, EVOLVING LEGAL FRAMEWORKS FOR PRIVATE SECTOR DEVELOPMENT IN CENTRAL AND EASTERN EUROPE 8 (July 1993) [hereinafter EVOLVING LEGAL FRAMEWORKS]. This principle assumes, of course, that the country's own citizens are able to participate fully in economic activities, including investment. As will be discussed below, such is not the case in Cuba today.

¹⁰⁴ LEGAL TREATMENT OF FOREIGN INVESTMENT, *supra* note 9, at 158, 204.

¹⁰⁵ The taking may not be outright but take the form of "creeping expropriation," which refers to measures that have the effect of impairing the economic viability of the enterprise; for example, interfering with investor access to needed facilities and supplies; denying the investor access to funds or profits; coercing the investor to sell the enterprise at unfairly low rates; and, in the most extreme cases, forcing the investor to leave the country and deprive it of effective control of the enterprise. SWAN & MURPHY, *supra* note 26, at 785-87.

¹⁰⁶ As noted earlier, shortly after the Castro government came to power, it seized most business enterprises and other private property on the island. Some of the takings came in the form of outright expropriations, while others proceeded indirectly via taxation and onerous administrative requirements placed on industries such as oil and mining. The regime also imposed such severe restrictions on the export of foreign currency that they effectively prevented any payment from being made to creditors outside the country. See Delissa A. Ridgeway, *Viewing the Future Through the Rear View Mirror: An Historical Perspective on U.S. Expropriation Claims Against Cuba*, in SHAW, PITTMAN, POTTS & TROWBRIDGE'S WORKSHOP ON PROPERTY CLAIMS IN CUBA'S TRANSITION 1, 2 (Jan. 26, 1995), available in Shaw, Pittman, Potts & Trowbridge's Library, Washington, D.C.

¹⁰⁷ LEGAL TREATMENT OF FOREIGN INVESTMENT, *supra* note 9, at 204.

3. *Streamlined Foreign Investment Regulations and Procedures*

The third fundamental pillar of a favorable foreign investment regime is a regulatory process free from bureaucratic impediments to investment. The concept of "one-stop shopping" has been postulated as the ideal method for streamlining foreign investment regulations.¹⁰⁸ Under this concept, there is a central office where foreign investors can register and satisfy all other requirements to set up their enterprises.¹⁰⁹ The obvious benefits of such a central office are time and transaction costs savings for foreign investors. Other advantages of the central office concept are the reduction of administrative costs, the elimination of duplicative government structures, and the minimization of conflicting requirements and interpretations of existing laws.¹¹⁰ An indirect, but perhaps important advantage of the establishment of a central agency to deal with foreign investors is that it gives the investors the certainty of having a single contact with whom to deal, and from which to obtain advice and help in resolving problems as they arise.

B. *Specific Objectives of Foreign Investment Laws in Countries in Transition*

In addition to the fundamental pillars on which successful foreign investment regimes rest, conditions in countries making a transition from socialism to a free-market society warrant that additional objectives be fostered by the foreign investment codes and related legislation. This section discusses four such objectives. The continued relevance of these specific objectives depends, of course, on the conditions that exist in a country as the transition unfolds.

1. *Promotion of Rapid Investment in the Country's Infrastructure*

After years of communist rule, important elements of the infrastructure of former socialist countries are typically in a state of disrepair.¹¹¹ In Cuba, early foreign investment will be required to rebuild, enhance and modernize critical areas of the infrastructure, such as energy production, telecommunications, and transportation.¹¹² These sectors of the economy are not only crucial to the welfare of the population, but their upgrading is required to attract foreign investment. Given the importance of rapidly modernizing

¹⁰⁸ LOUIS T. WELLS, JR. & ALVIN G. WINT, FACILITATING FOREIGN INVESTMENT: GOVERNMENT INSTITUTIONS TO SCREEN, MONITOR, AND SERVICE INVESTMENT FROM ABROAD 1-3 (1991) [hereinafter FACILITATING FOREIGN INVESTMENT].

¹⁰⁹ *Id.* at 1.

¹¹⁰ *Id.*

¹¹¹ *Project Finance: In the CIS Slow Lane*, THE BANKER, Jan. 1995.

¹¹² PREG & LEVINE, *supra* note 7, at 39.

Cuba's infrastructure, foreign investment legislation should not unduly burden investments in this area but, to the contrary, encourage the participation of foreign investors in these strategic sectors.

2. *Promoting the Transfer of Modern Technology*

Recent experience in Central and Eastern European countries in transition suggests that foreign investment has helped reduce the gap between the state of technological development in those countries and conditions in the rest of the industrialized world.¹¹³ Foreign investors have consistently installed the latest (or near-latest) technologies in their facilities in Central and Eastern Europe.¹¹⁴ Foreign investment legislation, therefore, should foster investments that will introduce state-of-the-art technologies during the transition period and should provide adequate protection of foreign investor technology to encourage its importation into the country. Such protection should be afforded by the foreign investment code and other laws, particularly the intellectual property laws.

3. *Fostering Employment-Creating Enterprises*

An important objective of foreign investment legislation in countries in transition is to encourage the creation of new sources of employment for the population during the transition to a market economy. There are two reasons for this importance.

First, one of the effects of the transition process is a rise in unemployment as inefficient state enterprises shut down and the government bureaucracy is culled.¹¹⁵ The experience in many Central and Eastern European countries—and some Latin American countries—implementing radical economic reform packages is that the rise in unemployment leads to social instability and popular backlash against the economic reform process.¹¹⁶ To minimize these phenomena, foreign investment in employment-creating enterprises should be

¹¹³ DOBOSIEWICZ, *supra* note 78, at 29.

¹¹⁴ *Id.*

¹¹⁵ This process is already at work in Cuba. Along with universal health care, education, and housing, guaranteed employment is regarded as one of the achievements of the Cuban Revolution. But in an effort to make Cuba's economy more efficient, the Cuban Government is rescinding the guarantee of lifetime employment. In a May 1995 interview, Pedro Ross Leal, secretary general of the Cuban Workers' Union, described the process as one of "rationalization of employment" that is producing a contingent of "available workers" who have agreed to be "voluntarily relocated." As many as 800,000 people are expected to be eventually "rationalized" by the new policy, when fully implemented. *In Radical Move, Cuba Ends Guaranteed Jobs*, CHICAGOLAND, May 14, 1995, at C11.

¹¹⁶ Reforms towards a market economy also result in lowering the standard of living for the average working person. Marek Wierzbowski, *Foreign Investment in Eastern Europe*, 4 TRANSNAT'L LAW 623, 629 (1991). For example, while Poland was going through the initial stages of the economic transition process, there was a thirty percent decrease in the standard of living of the population. *Id.* at 637.

encouraged as a way to promote social stability and ensure the orderly implementation of economic reforms.

Second, employment in foreign-owned enterprises exposes the domestic labor force to modern work practices that improve productivity.¹¹⁷ Typically, most workers of countries in transition lack the skills and discipline necessary to improve productivity and compete in the global marketplace.¹¹⁸ In addition, those countries suffer from an acute shortage of qualified management personnel during the transition to a market economy.¹¹⁹ Foreign investors in Central and Eastern Europe have introduced market-tested management skills that have trickled down to indigenous enterprises.¹²⁰

4. *Improving the Balance of Payments*

Countries in transition in Central and Eastern Europe have relied on foreign investment to increase exports and thus improve their balance of payments.¹²¹ Indeed, an important objective of the foreign investment regime of a country in transition should be to encourage investment in export-oriented enterprises.

IV. Recommended Elements of a Cuban Foreign Investment Code

The concepts discussed in the previous section can be applied to determine the type of foreign investment code that would be most beneficial to Cuba during its free-market transition. Two important observations need to be made at the outset. First, the experience in Central and Eastern European countries shows that it is very difficult if not impossible to develop a suitable foreign investment code in a single try.¹²² Several attempts are often necessary, either because the starting point of the effort is an inadequate code which must be molded in incremental steps into a workable piece of legislation or because the contents of the legislation are driven by political and economic conditions that are in a state of flux.¹²³

Second, if a choice is to be made between speed and perfection, speed should prevail. There will be a great need in Cuba for foreign investment legislation that meets the requirements of both the country and the investors. Under those circumstances, it will be preferable to have adequate but perhaps less than perfect legislation enacted early than to hold up passage while seeking to refine the formulation.

A third observation follows from these two. The first foreign

¹¹⁷ See DOBOSIEWICZ, *supra* note 78, at 28.

¹¹⁸ *Id.*

¹¹⁹ *Id.*

¹²⁰ *Id.*

¹²¹ *Id.* at 32.

¹²² *Id.* at 38-39.

¹²³ *Id.*

investment code that is enacted during Cuba's transition should be kept as simple as possible in an effort to shorten the drafting period, minimize debates among the decision-makers, and avoid causing strain in the transition period government structures, which may not be capable of administering overly complex statutes.

For these reasons, the substantive provisions discussed below may not all be capable of early implementation. The highest priority provisions, and consequently those that must be included from the start in the Cuban foreign investment code, are those granting national treatment to foreign investors and allowing 100% foreign ownership of Cuban enterprises; those guaranteeing full compensation in the event of expropriation; those removing restrictions on profit repatriation; and those streamlining the regulation of foreign-owned enterprises.

A. Provisions to Implement the Fundamental Pillars of Foreign Investment Legislation

Foreign investors considering going into Cuba during its transition must be reassured that no burdensome limitations, conditions, or impediments will be placed on their ability to operate in the country;¹²⁴ that their investment will be protected against adverse actions by the state; and that they will be able to repatriate profits and move capital in and out of the country without restrictions. In short, the investment climate must be fair and favorable to the investor. This section discusses the main foreign investment code provisions that will create such an investment climate in Cuba.

1. Guaranteeing National Treatment

Equal treatment of foreign investors in Cuba could be guaranteed through express declarations in the Foreign Investment Code (and perhaps the Constitution) that foreign investors enjoy the equal protection of Cuba's laws and are subject to the same treatment afforded domestic individuals and enterprises. To the extent that any distinctions need to be made between foreign and domestic business entities, such distinctions should be clearly defined and should be identified in the Foreign Investment Code or cross-referenced there to other applicable legislation.

¹²⁴ For example, the transition period 1991 Polish Law on Foreign Investment has eliminated most restrictions on foreign investment. In all but a very few cases, foreign investment does not require any special permits, and there is no upper or lower limit on the amount to be invested. There is also no limit on the repatriation of profits abroad. Marek Kaszubski, *Overview of the Law Governing Foreign Investment in Poland*, in LEGAL ASPECTS OF TRADE AND INVESTMENT IN THE SOVIET UNION AND EASTERN EUROPE 1990 328-31 (PLI Commercial Law and Practice Course Handbook Series No. 549, 1990). The drafters of the new law believe that the Polish economy requires at least \$10 billion of foreign investment. Wierzbowski, *supra* note 116, at 643.

For domestic political reasons, it is also important to avoid creating the impression that foreign investors are being given advantages over the country's nationals.¹²⁵ This is crucial in Cuba, where growing resentment exists over special treatment accorded to foreigners by the current Cuban Government.¹²⁶ Continued special treatment for foreign investors may be poorly received by the Cuban people and may serve as political ammunition for those opposed to economic reforms.¹²⁷

2. *Eliminating Restrictions on Property Ownership by Foreign Investors*

Restrictions on foreign equity participation in domestic enterprises are designed to ensure direct or indirect state control over the enterprises, particularly in socialist countries.¹²⁸ In free-market countries, these restrictions (typically in the form of mandatory percentages of local equity participation in foreign-owned enterprises) are most often imposed in "strategic" national industries such as utilities or telecommunications companies.¹²⁹

¹²⁵ It may, however, be deemed in the country's interest to provide special incentives to investment in areas of importance to the country's development, such as infrastructure projects. Such incentives should be available to all investors even if, initially, only foreign investors have the capital and technical resources to take advantage of the incentives.

¹²⁶ Since the legalization of the use of the dollar and dollar-based enterprises in 1993, Cuba has seen a growing division of its society into classes based not in the traditional Marxist principles, but on one's access to the dollars brought in by foreign investors and visitors. Such class distinctions have led to a growing feeling of animosity towards foreigners as well as against Cuban employees of the joint venture industries. Mark Cooper, *Letters From Havana—For Sale: Used Marxism. Castro's Grandchildren Discover the Glory of the Dollar*, HARPER'S MAG., Mar. 1995, at 56, 64.

¹²⁷ Venezuela serves as a good example of the problems that arise when politicians capitalize on the popular backlash against liberal economic reforms. Rafael Caldera came to power with the votes of Venezuelans hurt by a drastic, yet necessary, economic reform program implemented by his predecessor. President Caldera instituted a series of measures, such as foreign exchange and prices controls, aimed at easing the pain resulting in part from the economic reform program. These measures, however, exacerbated, rather than alleviated, the country's economic crisis, scaring away foreign investment. See U.S. FEDERAL TRADE COMMISSION, *Venezuela Briefing Note*, Feb. 1995, on file at Shaw, Pitman, Potts & Trowbridge, Washington, D.C.

¹²⁸ M. SORNARAJAH, THE INTERNATIONAL LAW ON FOREIGN INVESTMENT 104-07 (1994) [hereinafter INTERNATIONAL LAW ON FOREIGN INVESTMENT].

¹²⁹ See Mark B. Baker & Mark D. Holmes, *An Analysis of Latin American Foreign Investment Law: Proposals for Striking a Balance Between Foreign Investment and Political Stability*, 23 U. MIAMI INTER-AM. L. REV. 1, 14-17 (1991). The authors advance the argument that restrictions on foreign equity participation in important national industries reduces expropriation risk. They argue that, for example, Mexico's sale of its telecommunications company to foreign investors could be subsequently undone by a nationalistic government which opposes privatization. The authors suggest that the host country retain ownership of important national industries to prevent changes in policy from damaging the country's reputation with prospective foreign investors. *Id.* at 32-34. On the other hand, equity restrictions have been criticized for creating "an elite group of local businesses who form associations with foreign capital and enable governments that are favourable to their business interests to remain in power." INTERNATIONAL LAW OF FOREIGN INVESTMENT, *supra* note 128, at 111-12.

These types of restrictions have been prevalent in Cuba. As noted earlier, under Law 50 majority participation by local enterprises was a requirement, or at least a practice followed in most instances.¹³⁰ Under Law 77, it would be possible for a foreign investor to be sole owner of its enterprise. However, it will be interesting to see whether such investments will actually be permitted, particularly in sensitive areas of the economy.

All equity participation restrictions should be abolished in Cuba's foreign investment legislation because they generally deter foreign investment.¹³¹ Under the principle of national treatment, foreign investors should be able to use the same forms of business organization available to nationals, without additional equity participation restrictions.¹³²

The experience of countries in transition in Central and Eastern Europe, which now allow 100% foreign ownership of domestic enterprises, supports the wisdom of removing restrictions on equity participation.¹³³ Several countries in Latin America, including Mexico and Venezuela, have also eliminated or relaxed restrictions on foreign equity participation, although significant restrictions remain in place in some countries.¹³⁴

¹³⁰ Initially, under Law 50, the Cuban government restricted investment to certain areas of the economy such as oil extraction and tourism. As the economy worsened, the government opened additional sectors. See *Minister Interviewed on Foreign Investment in Sugar*, *supra* note 38; CUBA IN TRANSITION, *supra* note 19, at 33.

¹³¹ OECD ON FDI, *supra* note 73, at 58.

¹³² *Id.*

¹³³ EVOLVING LEGAL FRAMEWORKS, *supra* note 103, at 8. For example, Hungary, the Eastern European country that has attracted the largest amount of foreign investment, has succeeded by establishing liberal investment legislation that permits 100% foreign ownership of investment. *Id.* at 79. To date Hungary has attracted \$8.5 billion in foreign direct investment, as much as the rest of Central and Eastern Europe combined. WHITE HOUSE CONFERENCE ON TRADE AND INVESTMENT IN CENTRAL AND EASTERN EUROPE, HUNGARY, (Jan. 12-13, 1995) (no page citation available) (on file with authors). Most Central and Eastern European countries, however, prohibit foreigners from owning real property. Foreign investors can circumvent these prohibitions by purchasing real estate through a 100% foreign owned domestic enterprise. The Czech Republic, for example, permits 100% foreign-owned Czech enterprises to own real estate. *Id.*; EVOLVING LEGAL FRAMEWORKS, *supra* note 103, at 55.

The extent of allowable real estate ownership by foreigners will undoubtedly be a thorny issue in Cuba's market transition. Before the Revolution, foreign ownership of significant portions of agriculture and commercial land was a source of popular discontent. The revolutionary leaders used the popular discontent as justification for the expropriation of foreign assets in Cuba. Nelson R. Amaro, *Mass and Class in the Origins of the Cuban Revolution*, in CUBAN COMMUNISM 1959-1995 39, 47 (Irving L. Horowitz, ed. 1995). Because of this experience, a transition government in Cuba may feel compelled to impose restrictions on the ownership of real estate by foreigners. If such restrictions are imposed, provisions like those currently in place in the Czech Republic might be an effective way to allow foreign investment in real property while minimizing popular concerns.

¹³⁴ Baker & Holmes, *supra* note 129, at 14-17.

3. Protection Against Uncompensated Expropriation of Property

a. Domestic Law Protections

Considering Cuba's history of private property takings, providing strong guarantees against uncompensated expropriation must be an essential element of its foreign investment legislation.¹³⁵ Guarantees against uncompensated expropriation should be incorporated into the country's Constitution and restated in the Foreign Investment Code.¹³⁶

As important perhaps as giving express guarantees against uncompensated expropriation is setting forth a proper standard for compensation in the event of expropriation. The internationally-recognized standard is the formulation coined in 1938 by U.S. Secretary of State Cordell Hull: "prompt, adequate and effective compensation."¹³⁷ The World Bank Guidelines incorporate this

¹³⁵ Cuba's new Law 77 does include express guarantees against expropriation. See *supra* note 51 and accompanying text. However, the effectiveness of the mechanisms defined in the law for giving effect to these guarantees would have to be tested in practice.

¹³⁶ See Matias F. Travieso-Diaz & Steven R. Escobar, *Cuba's Transition to a Free-Market Democracy: A Survey of Required Changes to Laws and Legal Institutions*, 5 DUKE J. COMP. & INT'L L. 379, 410 (1995) [hereinafter Travieso-Diaz & Escobar on Cuba's Transition]. It is important to understand, however, that guarantees against expropriation written into the laws of a country do not necessarily bind a successor government if it chooses to abrogate the laws providing the guarantees. INTERNATIONAL LAW OF FOREIGN INVESTMENT, *supra* note 101, at 96. The laws, however, may be enforceable against the country in international fora when resolving investment disputes. *Id.* at 96-98. They also serve an important signaling function in that they indicate to foreigners that past practices against foreign investors are no longer pursued. *Id.* at 95.

¹³⁷ A shorthand sometimes used for the Hull formula is that of "just compensation," meaning "in the absence of exceptional circumstances . . . an amount equivalent to the value of the property taken . . . paid at the time of the taking . . . and in a form economically usable by the foreign national." Patrick M. Norton, *A Law of the Future or a Law of the Past? Modern Tribunals and the International Law of Expropriation*, 85 A.J.I.L. 474, 476 (1991) (quoting RESTATEMENT (THIRD) OF THE FOREIGN RELATIONS LAW OF THE UNITED STATES § 712 (1987)).

Developing countries have attacked the Hull formula, which was perceived as an encroachment on their sovereignty by developed countries. This challenge was manifested in *Permanent Sovereignty Over Natural Resources*, U.N. G.A. Res. 1803, at XVII, which called for "appropriate" compensation under both national and international law. Developing countries continued their attack through *Charter of Economic Rights and Duties of States*, U.N. G.A. Res. No. 3281, at XXIX (the Charter). The Charter states that compensation controversies are to be settled under the law of the expropriating state, implying the ability of a state to pay less than full compensation for expropriated property. See, SWAN & MURPHY, *supra* note 26, at 775-76.

Resolution No. 1803's "appropriate" compensation standard, however, is arguably analogous to the Hull formula. Haliburton Fales, *A Comparison of Compensation for Nationalization of Alien Property with Standards of Compensation Under United States Law*, 5 NW. J. INT'L L. & BUS. 871, 880-82 (Winter 1983-84). The Hull formula, therefore, remains for all practical purposes the internationally-recognized standard. In addition, the need to encourage foreign investment in developing countries has eroded the support that once existed for limited compensation formulations such as that implied in the Charter. Norton, *supra*, at 475.

standard.¹³⁸ Under current practice, the "prompt" element of the Hull formula means payment without delay.¹³⁹ The "adequate" element means that the payment should reflect the "fair market value" or "value as a going concern" of the expropriated property.¹⁴⁰ The "effective" element is satisfied when the payment is made in the currency brought in by the investor, in a convertible currency (as designated by the International Monetary Fund), or in any other currency acceptable to the investor.¹⁴¹

b. Use of Bilateral Investment Treaties (BITs)

Bilateral investment treaties protect investors from a signatory country providing a framework in the host country for national treatment of such investors and setting up dispute settlement procedures, methods for compensation for expropriation, and guarantees of the convertibility and repatriation of profits.¹⁴² Given the increasing use of BITs—particularly by the United States—Cuban foreign investment legislation should authorize and call for the conclusion of such agreements.¹⁴³

c. Multilateral Dispute Resolution Agreements

The International Convention on the Settlement of Investment Disputes Between States and Nationals of Other States (ICSID Convention) is a multilateral agreement intended to reduce foreign investor concerns by helping resolve investment disputes of private parties with foreign states; as such, it is particularly useful in countries in transition.¹⁴⁴ Accession to the ICSID Convention allows a signatory state and a national of another signatory state to submit their

¹³⁸ LEGAL TREATMENT OF FOREIGN INVESTMENT, *supra* note 9, at 161-62.

¹³⁹ *Id.* at 163.

¹⁴⁰ SWAN & MURPHY, *supra* note 26, at 774-75; *see also* LEGAL TREATMENT OF FOREIGN INVESTMENT, *supra* note 9, at 161-62. "Compensation will be deemed 'adequate' if it is based on the fair market value of the taken asset as such value is determined immediately before the time at which the taking occurred or the decision to take the asset became publicly known." *Id.* Fair market value can be defined as the "amount that a willing buyer would normally pay to a willing seller after taking into account the nature of the investment, the circumstances in which it would operate in the future and its specific characteristics, including the period in which it has been in existence, the proportion of tangible assets in the total investment and other relevant factors." *Id.*

¹⁴¹ LEGAL TREATMENT OF FOREIGN INVESTMENT, *supra* note 9, at 163.

¹⁴² SWAN & MURPHY, *supra* note 26, at 717. For a detailed discussion of BITs and their use to promote foreign investment, *see* Jose Luis Siqueiros, *Bilateral Treaties on the Reciprocal Protection of Foreign Investment*, 24 CAL. W. INT'L L.J. 255 (1994).

¹⁴³ SWAN & MURPHY, *supra* note 26, at 717. As noted earlier, Cuba has recently entered into BITs with several countries. *See supra* note 26 and accompanying text. The trend towards signing BITs should continue during Cuba's transition and be extended to include the United States and all other important potential trading partners.

¹⁴⁴ Kenneth S. Jacob, *Reinvigorating ICSID With a New Mission and With Renewed Respect for Party Autonomy*, 33 VA. J. INT'L L. 123, 135-38 (1992).

investment disputes to arbitration by the International Centre for the Settlement of Investment Disputes (ICSID).¹⁴⁵ The Convention also establishes an Additional Facility for the Administration of Conciliation, Arbitration and Fact-Finding Proceedings, which is a mechanism for settling certain disputes outside ICSID's jurisdiction under the ICSID Convention.¹⁴⁶

Cuba should become a party to the ICSID Convention so that, if Cuban government agencies or instrumentalities continue to enter into joint ventures with foreign investors, the joint venture agreements can refer contractual disputes to ICSID arbitration. Cuba's participation in the ICSID would provide further assurance to foreign investors that the country is prepared to honor its commitments to them and treat them fairly.

d. Investment Insurance: OPIC, MIGA, and Private Insurers

As an additional incentive for foreign investment, the Cuban government should assist foreign investors obtaining Overseas Private Investment Corporation ("OPIC") or Multilateral Investment Guarantee Agency ("MIGA") coverage. OPIC is a corporation owned by the United States government which offers political risk insurance to U.S. businesses which invest in foreign countries.¹⁴⁷ OPIC also offers insurance against inconvertibility, that is, "the inability of an investor to convert into dollars the local currency received as profits, earnings or return of an original investment."¹⁴⁸ In order for U.S. investors to become eligible for OPIC coverage, the host country (Cuba, in this case) needs to enter into an agreement with the United States which enables the U.S. government to authorize OPIC coverage for qualifying investments in Cuba.¹⁴⁹

MIGA is an investment guarantee agency operated under the auspices of the World Bank.¹⁵⁰ MIGA offers guarantees and reinsurance to eligible investments against losses resulting from four

¹⁴⁵ *Id.* at 126-27.

¹⁴⁶ *Id.* at 126.

¹⁴⁷ RICHARD C. ALLISON & JACK J. COE JR., PROTECTING AGAINST THE EXPROPRIATION RISK IN INVESTING ABROAD § 3.01 (1993) [hereinafter PROTECTING AGAINST EXPROPRIATION RISK].

¹⁴⁸ *Id.* at § 3.02(1)(a).

¹⁴⁹ SWAN & MURPHY, *supra* note 26, at 810.

The most fundamental provision of this agreement is the host government's [i.e. Cuba's] acceptance of OPIC's claim to subrogation—the right in OPIC to compensation from the host government for the funds it has had to pay to the investor. This agreement also characteristically requires that the U.S. investor obtain the approval of the foreign government before OPIC will issue a guarantee. Arbitration is often required in the event of a dispute between OPIC and the host country over the agency's right to receive compensation as subrogee.

Id. at 810-11.

¹⁵⁰ *Id.* at 815.

categories of non-commercial risks: 1) the transfer risk resulting from host government restrictions on currency conversion and transfers; 2) the risk of loss resulting from legislative or administrative actions or omissions of the host government which deprive the foreign investor of ownership or control of substantial elements of his investment; 3) the repudiation or breach of government contracts in cases where the investor has no access to a competent dispute resolution forum, or faces unreasonable delays in such a forum, or is unable to enforce a decision issued in his favor; and 4) the risk of armed conflict and civil disturbance.¹⁵¹ MIGA will not issue a guarantee to an investor without the host government's approval of the guarantee.¹⁵² Cuba's laws should therefore provide for the expedited approval of MIGA guarantees.

Apart from any Cuban government undertakings to assist foreign investors to secure investment guarantees, the investors may also take steps to purchase private investment insurance. Insurance from private companies, such as Lloyd's of London, offers several advantages over OPIC or MIGA investment insurance.¹⁵³ Private insurers frequently cover existing projects, while OPIC only covers "new" projects.¹⁵⁴ Private insurers may also cover a wider range of contingencies, resolve claims more quickly, and indemnify a greater amount of loss than OPIC or MIGA.¹⁵⁵

While obtaining private insurance is the responsibility of the foreign investor, Cuba should avoid adopting laws or regulations that impair the activities of investment insurers. The Cuban government should also cooperate with insurers seeking to settle claims filed by investors under their policies.

4. *Guarantees of Currency Convertibility and Profit Repatriation Rights*

Free convertibility of currency and unrestricted ability to repatriate profits are aspects of a foreign investment regime that are particularly important to investors.¹⁵⁶ Most Central and Eastern European countries have removed restrictions on profit repatriation from their foreign investment regimes.¹⁵⁷ The World Bank Guidelines also

¹⁵¹ *Id.* at 815-16.

¹⁵² Ibrahim F. I. Shihata, *The Multilateral Investment Guarantee Agency*, 20 INT'L LAW. 485, 491 (1986) (quoting art. 15 of the MIGA Convention).

¹⁵³ PROTECTING AGAINST EXPROPRIATION RISK, *supra* note 147, at § 3.03 (quoting art. 15 of the MIGA Convention).

¹⁵⁴ *Id.* at § 3.03[1].

¹⁵⁵ *Id.* All these advantages, however, come at a price. Private insurers generally offer shorter coverage terms and command significantly higher premiums than OPIC or MIGA. *Id.*

¹⁵⁶ See LEGAL TREATMENT OF FOREIGN INVESTMENT, *supra* note 9, at 20.

¹⁵⁷ EVOLVING LEGAL FRAMEWORKS, *supra* note 103, at 8.

emphasize the importance of unrestricted repatriation of profits to foreign investors.¹⁵⁸ Cuba provides such rights to investors under the new foreign investment law.¹⁵⁹ These benefits should be retained in the transition period legislation.

The scope of any future controls that might be imposed on the convertibility of currency held by foreign investors would depend on the Cuban government's macro-economic policies during the transition to a free-market economy. In the interest of fostering foreign investment, however, Cuba should refrain from imposing restrictions on the repatriation of after-tax profits by foreign investors.

5. *Reduction in Pre-Approval Requirements*

Government pre-approval requirements often pose a significant hurdle to foreign investment. Most Central and Eastern European countries have abolished pre-approval requirements and have simplified the procedures necessary to set up an enterprise.¹⁶⁰ Many Latin American countries have also streamlined entry procedures in an effort to facilitate foreign investment.¹⁶¹ The Cuban government should follow these examples and abolish or minimize pre-approval requirements for foreign investors.

Special attention should be paid to the manner in which any required pre-approvals are processed. Cuba's foreign investment legislation should establish a single government agency or institution with pre-approval authority over all foreign investment.¹⁶² Worldwide experience suggests, however, that concentrating pre-approval authority in one government institution leads to problems in the issuance of post-approval licenses and permits to the foreign investor by other government agencies, which often seek to reassert their authority after the pre-approval process.¹⁶³ Future Cuban foreign investment legislation, therefore, should include provisions for the automatic issuance of certain authorizations or permits upon approval of the

¹⁵⁸ LEGAL TREATMENT OF FOREIGN INVESTMENT, *supra* note 9, at 159-60. The World Bank Guidelines prescribe free repatriation of profits, salaries of foreign personnel, and any amounts used for the repayment of debts. *Id.*

¹⁵⁹ Law 77, *supra* note 38, art. 8.

¹⁶⁰ EVOLVING LEGAL FRAMEWORKS, *supra* note 103.

¹⁶¹ Baker & Holmes, *supra* note 129, at 21-25. Mexico, for example, no longer requires government approval for investment in a newly-formed Mexican enterprise if the investment does not exceed \$100 million and meets other criteria. Chile has a "fast-track" approval procedure that allows the Executive Secretary of the Foreign Investment Committee and the Minister of the Economy to approve investments of less than \$5 million. Colombian law requires approval of investments conforming to government criteria within four weeks. If the documentation is not complete by the end of the four week period, the government issues a temporary permit for twelve weeks until the documentation is completed and the approval process resumes. *Id.*

¹⁶² See FACILITATING FOREIGN INVESTMENT, *supra* note 108, at 26.

¹⁶³ *Id.*

investor and prohibitions against lengthy evaluations of projects by institutions that control licenses and permits.¹⁶⁴

Also important are the procedures used to evaluate and approve proposed investments. Project-by-project screening is probably the most cumbersome form of evaluation and the one most likely to hinder foreign investment.¹⁶⁵ Given the importance of stimulating the rapid entry of foreign capital into Cuba, project-by-project evaluations should be abandoned. Instead, a well-defined list of requirements for investment should be set, and if sectors of the economy are to be declared off-limits to foreign investors, those should be clearly identified in the legislation so the identification may serve as a sufficient screen.¹⁶⁶ From the standpoint of a potential investor, a "negative list" describing restricted sectors would be preferable to a "positive list" of sectors open to foreign investment.¹⁶⁷

6. *One-Stop Shopping*

Cuba's Foreign Investment Code should establish a central office before which foreign investors can satisfy all requirements for setting up their enterprises. As noted above, the benefits of a centralized approval system include savings in time and transaction costs for foreign investors and the elimination of investment disincentives, such as duplicative regulations and multiple regulatory entities.

The one stop-shopping concept should also be applied to unifying the foreign investment regulations. Placing all the regulations affecting foreign investment in a single code (or cross-referencing all the regulations affecting foreign investment) would eliminate duplicative or inconsistent regulatory actions. The Foreign Investment Code should also include a residual clause stating that, to the extent not covered by its specific provisions, a foreign investor has the same rights, and is subject to the same rules and regulations, as a domestic person or entity.

A useful tool to foreign investors would be a regularly-updated handbook published by the Cuban Government would contain information about legislation, regulations and procedures relevant to

¹⁶⁴ *Id.* at 28-29.

¹⁶⁵ As noted earlier, every foreign investment venture in Cuba must undergo a protracted approval process that includes personal signoff by Fidel Castro himself.

¹⁶⁶ FACILITATING FOREIGN INVESTMENT, *supra* note 108, at 41.

¹⁶⁷ Louis T. Wells, Jr., *Mobile Exporters: New Foreign Investors in East Asia*, in FOREIGN DIRECT INVESTMENT 173, 189 (Kenneth A. Froot ed., 1993) [hereinafter MOBILE EXPORTERS]. In the 1980s, the government of Indonesia shifted from a rather unclear "positive list" of sectors in which foreign investment would be allowed, to a short and clear "negative list" of sectors in which foreign investment would not be allowed. Thus, a would-be investor could tell with a fair degree of certainty whether a proposal would be accepted or not. The increased certainty provided by this method was found beneficial by investors, particularly small firms. *Id.*; see also LEGAL TREATMENT OF FOREIGN INVESTMENT, *supra* note 9, at 157.

foreign investment.¹⁶⁸ The central office handling foreign investor applications and inquiries should be charged with the task of publishing the handbook and distributing it to prospective investors.

B. Foreign Investment Code Provisions to Meet Specific Economic or Political Objectives

The provisions discussed in this subsection favor foreign investment in particular sectors of the economy by giving investors in those sectors monetary advantages in the form of reduced taxes or tariffs. These types of provisions, however, are controversial and their success in stimulating foreign investment is far from proven. They merit examination, nonetheless, because they are tools available to lawmakers to channel foreign investment into areas where it is most urgently needed.

1. Special Tax Preferences

Special tax preferences, which are a form of subsidy, remain the most common incentive offered to foreign investors.¹⁶⁹ Tax incentives are often used as a form of "signaling," to denote a country's desire to attract foreign investment in a given sector or across the board.¹⁷⁰

Many commentators have noted that special tax incentives, standing alone, do not appear to attract foreign investment.¹⁷¹ The World Bank Guidelines recommend against special tax incentives for foreign investors.¹⁷² Most of the countries of Central and Eastern Europe have rescinded their special tax incentives for foreign investors after having them in place for a few years, and now treat foreign and domestic investors on equal terms.¹⁷³ Indonesia also abolished its special tax incentives in 1985, and the subsequent large inflows of foreign capital into that country suggest that the special tax incentives were not essential to attract foreign investment.¹⁷⁴

¹⁶⁸ LEGAL TREATMENT OF FOREIGN INVESTMENT, *supra* note 9, at 158-59.

¹⁶⁹ INVESTMENT INCENTIVE AND DISINCENTIVES: EFFECTS ON INTERNATIONAL DIRECT INVESTMENT ORGANIZATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT 16 (1989).

¹⁷⁰ JOHN M. KLINE, FOREIGN INVESTMENT STRATEGIES IN RESTRUCTURING ECONOMIES: LEARNING FROM CORPORATE EXPERIENCES IN CHILE 245 (1992) (describing Chile's guaranteed tax rate for foreign investments as a strong signal that foreign investors were welcome in the country).

¹⁷¹ See, e.g., Yitzhak Hadari, *The Role of Tax Incentives in Attracting Foreign Investments in Selected Developing Countries and the Desirable Policy*, 24 INT'L LAW. 121, 123 (1990); Kojo Yelapaala, *In Search of Effective Policies for Foreign Direct Investment: Alternatives to Tax Incentive Policies*, 7 NW. J. INT'L L. & BUS. 208, 212 (1985). Special tax incentives have been criticized for discriminating against domestic investment, complicating tax administration, and substantially reducing revenue. EVOLVING LEGAL FRAMEWORKS, *supra* note 103, at 8.

¹⁷² LEGAL TREATMENT OF FOREIGN INVESTMENT, *supra* note 9, at 160-61.

¹⁷³ Frances Williams, *Eastern Europe Varies Widely on Incentives—Foreign Investors are Offered Fewer Perks*, FIN. TIMES, Sept. 28, 1994, at 6.

¹⁷⁴ MOBILE EXPORTERS, *supra* note 167, at 184.

The experiences of countries which have abolished special tax incentives suggest that such incentives should *not* be included in Cuba's foreign investment legislation, except possibly for investment in infrastructure, high technology, and other areas deemed crucial to the economy in the early stages of the transition. Any tax incentives given should be of only limited duration (three to five years).

2. *Tariff Reductions*

In general, the use of tariffs in Cuba will probably be governed by the rules of the World Trade Organization's General Agreement on Tariffs and Trade (GATT), and those of regional trade agreements that Cuba may join. Beyond those, Cuba's use of tariff reductions to foster foreign investment also hinges on the transition government's overall economic and development policies.

Cuba could, for example, decide to eliminate tariffs altogether, in line with certain economic arguments sometimes made against the use of tariffs in developing countries.¹⁷⁵ The elimination of tariffs may attract foreign investment, particularly in the manufacturing sector, since the entire country would, in essence, become an export-processing zone. The loss of tax revenues from the elimination of tariffs could be offset by additional foreign investment and the consequent expansion of the tax base. Repealing tariffs would also eliminate the often time-consuming collection procedures and allow disbanding the entities charged with tariff collection.

3. *Export-Processing Zones*

If Cuba eliminates import and export tariffs and makes very limited use of tax incentives to foreign investment, the establishment of export-processing zones (EPZs) will not provide a significant further

¹⁷⁵ The two main arguments for tariffs, in addition to revenue generation, are the "optimum tariff theory" and "import-substitution policies." PAUL R. KRUGMAN & MAURICE OBSTFELD, *INTERNATIONAL ECONOMICS* 205, 217, 237 (2D ED. 1991). The optimum tariff theory posits that there is a tariff rate which optimizes national welfare by improving the country's terms of trade to the point where these improvements exceed the costs of production and consumption distortions. *Id.* at 217. Terms of trade gains from tariffs, however, depend on the tariff-imposing country's ability to drive down foreign export prices. *Id.* at 237. Small countries such as Cuba, which cannot affect world prices, do not receive any terms of trade gains from tariffs, thus the tariff actually reduces national welfare.

Import substitution is a policy of encouraging the growth of domestic industry by limiting imports of manufactured goods, primarily through tariffs. *Id.* at 243. Import substitution, however, necessarily limits export growth, since protected import-substituting industries draw resources away from actual or potential export sectors. *Id.* at 245. Import substitution will not help develop a competitive manufacturing sector if there are fundamental reasons, such as lack of skilled labor or resources, why the country lacks a competitive advantage in manufacturing. *Id.* In addition, import-substitution policies may cause the widening of wage differentials between manufacturing and agricultural workers, which results in high migration rates to urban centers and unemployment. *Id.* at 250-52.

boost to foreign investment. If tariffs are retained, on the other hand, EPZs may provide some investment incentives and may be used to encourage investment in coastal areas which would otherwise see little investment in areas such as manufacturing.¹⁷⁶

The success of EPZs in Cuba may depend to a great extent on the macro-economic policies adopted by the Cuban government. If the Cuban government imposes controls on the convertibility of foreign exchange, the establishment of EPZs offering unrestricted convertibility of foreign exchange and repatriation of profits may attract foreign investment to the EPZs in the manufacturing of products for export.¹⁷⁷ Special tax incentives may also attract foreign investors to EPZs, although some data suggests otherwise.¹⁷⁸

4. *Trade-Related Investment Performance Requirements*

Trade-Related Investment Performance Requirements (TRIPs) are, in essence, host government policies which guide foreign-owned firms into engaging in a particular type of activity.¹⁷⁹ The two most common forms of TRIPs are export quotas and local content requirements.¹⁸⁰

Export quotas and local content requirements do not appear to discourage foreign investment in many cases when other factors, such as attractive locations, protected markets, or other incentives offset the costs of the requirements.¹⁸¹ On the other hand, the World Bank Guidelines assert that the imposition of TRIPs deters foreign investment and report that they are becoming rare.¹⁸² Since Cuba probably will not have the resources to adequately implement and monitor a TRIPs program, TRIPs should not be included in Cuba's foreign investment legislation.

¹⁷⁶ The ease and reliability of transportation to the primary export market, however, has been cited as a major factor influencing the investment decision, so the location of the EPZ seem critical. POTENTIAL EFFECTS OF NAFTA ON CBI, *supra* note 75, at 46. A survey of firms which have invested in apparel assembly enterprises in countries which received unilateral trade concessions from the United States under the Caribbean Basin Economic Recovery Act (CBERA) reports that political stability was cited most often as an important determinant of the investment decision. Another important factor cited as influencing the decision to invest in CBERA-beneficiary countries is the lack of controls on exchange rates. *Id.* at 43, 46.

¹⁷⁷ See THE WORLD BANK, EXPORT PROCESSING ZONES 16 (1992) [hereinafter EXPORT PROCESSING ZONES].

¹⁷⁸ For example, host government measures to encourage foreign investment such as special tax incentives, are said not to be significant factors influencing the investment decisions of apparel firms doing business in the Caribbean Basin area. POTENTIAL EFFECTS OF NAFTA ON CBI, *supra* note 75, at 43.

¹⁷⁹ See generally THEODORE H. MORAN & CHARLES S. PEARSON, *Do TRIPs Trip Up Foreign Investment? An International Business Diplomacy Perspective*, in FOREIGN DIRECT INVESTMENT IN THE 1990S: A NEW CLIMATE IN THE THIRD WORLD 28, 30 (1990).

¹⁸⁰ *Id.* at 30.

¹⁸¹ OECD on FDI, *supra* note 73, at 58.

¹⁸² LEGAL TREATMENT OF FOREIGN INVESTMENT, *supra* note 9, at 202.

In addition, the United States views export controls as violating standards of free-trade and creating trade distortions.¹⁸³ The United States also contends that export controls violate the GATT, although a GATT panel upheld the validity of specific export targets in the Canadian Foreign Investment Review Act of 1982.¹⁸⁴ Given that the United States will most likely become Cuba's most important source of foreign investment during a market transition, it is critical that Cuban decision-makers not impose requirements in this area that run counter to U.S. positions, barring extraordinary circumstances.

V. Relationship Between Foreign Investment Legislation and Other Transition Laws

Foreign investment in a country in transition does not occur in a vacuum but, rather, operates within a legal framework that reflects the country's stage of development and the political and economic circumstances of the transition. This section explores briefly several areas of the law that are not specifically related to foreign investment but which may impact on a foreign investor's ability to operate in the country or otherwise affect his decision whether to invest.

The discussion that follows must by necessity be abbreviated and is not intended to examine all the issues that are raised in each area of the law.

A. *Laws that May Encourage Foreign Investment*

1. *Business Organization Laws*

Applying the principle of national treatment discussed earlier, foreign investors should be able to conduct operations in Cuba using the same types of business organization available to Cuban nationals. This principle has been taken to heart in Central and Eastern European countries, which allow foreign investors to use all forms of business organization recognized by local law.¹⁸⁵ The types of business organization available to foreign investors in Cuba should be those recognized by the new Companies Law that Cuba needs to enact early during its transition to a market economy. Corporate laws should

¹⁸³ INTERNATIONAL LAW ON FOREIGN INVESTMENT, *supra* note 128, at 141.

¹⁸⁴ *Id.* at 141-42. The United States argument that export controls violate the GATT has been stated as follows:

Export requirements, to the extent that they lead to exports by subsidiaries that would not have occurred in their absence, have effects similar to export subsidies which artificially increase the supply of the affected product in the world markets and displace more efficient home or third country products and exports of the affected product.

Id. at 142.

¹⁸⁵ For example, corporations, limited liability companies, partnerships, etc. Travieso-Diaz & Escobar on Cuba's Transition, *supra* note 136, at 415.

authorize, at a minimum, those forms of business organization with which foreign investors are most familiar. Cuba could adopt as a model, for example, the business organizations forms accepted by most Latin American countries, and in doing so it would reduce transaction costs for investors interested in doing business in the island.¹⁸⁶

2. Privatization Laws

Many foreign investors going into Cuba will want to participate in the privatization of state-owned enterprises.¹⁸⁷ Privatization is an extremely complex process, which, in the case of Cuba, will be closely tied to the program Cuba develops for resolving the outstanding property expropriations claims.¹⁸⁸

There are advantages to conveying state-owned enterprises to foreign investors as part of the privatization process. Foreign investors bring with them capital resources, management skills, business know-how, and improved technology, plus the ability to incorporate local enterprises into the global networks of production and commerce.¹⁸⁹ Allowing foreign investors to participate in the privatization of state-owned enterprises also enables the country to earn much needed foreign exchange,¹⁹⁰ an important consideration for what will certainly be a cash-strapped Cuba. Encouraging the participation by foreign investors, therefore, should be an important goal of the Cuban privatization program.

Foreign investors are mostly interested in acquiring medium and large enterprises that are being privatized.¹⁹¹ The opportunities for investment in such enterprises, however, may be limited by the potential restitution of some properties to their former owners—which might reduce the number of enterprises eligible for privatization.

The Cuban Government could also elect to limit foreign investor participation in the privatization of certain state-owned assets,

¹⁸⁶ The Latin-American forms of business organization are for the most part similar to those used in the United States and are therefore familiar to U.S. business people. Costa Rica, for example, allows the formation of limited liability companies by individuals, unlimited and limited liability companies, partnerships, limited partnerships, and corporations. Humberto Pacheco A., *Costa Rica, in INVERSION EXTRANJERA EN AMERICA LATINA* 63-67 (Jose Luis DePalma ed., 1991).

¹⁸⁷ For example, Grupo Domos, a Mexican industrial concern, is already involved in a venture to acquire a significant share of Cuba's telephone system. CHARLES W. THURSTON, *IN FROM THE COLD: HOW TO DO BUSINESS WITH CUBA* 53 (1994). Grupo Domos' deal is said to potentially involve as much as \$1.5 billion in investment, and to be part of a \$340 million debt swap agreement arranged by Mexico's state trade bank. *Id.* at 53, 54.

¹⁸⁸ For a discussion of the issues relating to the resolution of expropriation claims in Cuba see generally Travieso-Diaz on Claims, *supra* note 36.

¹⁸⁹ FARID DHANJI & BRANKO MILANOVIC, *PRIVATIZATION IN EASTERN AND CENTRAL EUROPE: OBJECTIVES, CONSTRAINTS, AND MODELS OF DIVESTITURE* 22 (1991).

¹⁹⁰ *Id.*

¹⁹¹ ERNST & YOUNG, *PRIVATIZATION: INVESTING IN STATE-OWNED ENTERPRISES AROUND THE WORLD* 43 (1994).

particularly those in "strategic" sectors of the economy. The original Polish privatization statute, for example, limited the extent of foreign owned stock in privatized companies to ten percent.¹⁹² However, since revamping the country's infrastructure is an urgent goal during the transition period, Cuba should not restrict foreign participation in privatized enterprises, particularly those in strategic sectors such as energy production, communications, and transportation.¹⁹³

The opportunities for foreign participation in the privatization of state-owned enterprises may be limited as a practical matter by the deterioration or obsolescence of the assets of those enterprises.¹⁹⁴ Foreign investors may prefer to invest in new ventures rather than in dilapidated state-owned enterprises.

Whatever the extent of foreign investor involvement in the privatization of state-owned assets, the Cuban government should ensure that investors face as little uncertainty as possible if they choose to become involved in the privatization process. This means that issues concerning title to state-owned assets should be settled very early in the privatization process. In addition, the approval process for the sale of state-owned assets to foreign investors should be made as simple as possible. In the early days of privatization in Poland, for example, the sale of a state-owned enterprise often required approval by the Workers' Council after consent by a general assembly of workers, and also by the Ministry of Ownership Transformation;¹⁹⁵ not surprisingly, these cumbersome approval requirements discouraged foreign investors.¹⁹⁶ Cuba should set up a privatization agency that provides a "one-stop shopping" point of coordination for the privatization of public enterprises.¹⁹⁷ The existence of such an agency would facilitate foreign participation in the privatization process.

¹⁹² David Gordon, *Privatization in Eastern Europe: The Polish Experience*, 25 LAW & POL'Y INT'L BUS. 517, 543-44 (1994).

¹⁹³ The current position of the Cuban Government is to exclude "strategic" industries, such as the electric power industry, from foreign investment activity and presumably from any privatization initiatives. See Pedro Monreal, *Remarks*, at SHAW, PITTMAN, POTTS & TROWBRIDGE'S WORKSHOP ON THE FUTURE OF ECONOMIC REFORMS IN CUBA 85-88 (Apr. 12, 1995), transcript available in Shaw, Pittman, Potts & Trowbridge's Library, Washington, D.C.

¹⁹⁴ Two thirds of Cuba's sugar mills are small and over eighty-five (85) percent were built before 1913. *Confronting the Crisis*, *supra* note 3, at 214. "There are constant grinding stoppages, and industrial yields have gradually declined: 12.5 percent in 1959-65; 11.4 percent in 1966-80; 11 percent in 1981-85; and 10.8 percent in 1986-89." *Id.* The just-completed 1995 sugar harvest of 3.3 million metric tons was the worst in fifty years. *Cuban Closing Out Its Sugar Harvest With Lowest Production in Decades*, J. COM., June 12, 1995, at 4B.

¹⁹⁵ Jackie Ruff, *Job Security in Poland: Economic Privatization Policy and Workplace Protections*, 7 TEMP. INT'L & COMP. L.J. 1, 11 (1993).

¹⁹⁶ *Id.* at 12.

¹⁹⁷ FACILITATING FOREIGN INVESTMENT, *supra* note 108, at 1-3.

3. Intellectual Property Rights Protection

Cuba's ability to provide effective protection for foreign investor intellectual property rights will be a crucial factor in the country's ability to attract many types of foreign investment to the island.¹⁹⁸ In addition, Cuba will need effective laws to protect the rights to its own technological achievements, particularly in biotechnology and related fields.¹⁹⁹

The Cuban Government should therefore strive to provide legal protections for intellectual property rights which meet the prevailing standards in other countries. The United States, in particular, is aggressive in demanding the protection of intellectual property rights owned by its enterprises and individuals and often takes action against foreign governments seen as tolerating the infringement of U.S.-owned intellectual property rights.²⁰⁰

There is no comprehensive, internationally-recognized set of standards for the protection of intellectual property rights which could serve as a model for Cuba.²⁰¹ However, the Uruguay Round of the GATT contains an Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS Agreement) which contains provisions "for the establishment of standards to protect a full range of intellectual property rights, and for the enforcement of those standards both internally and at the border."²⁰² The TRIPS Agreement establishes minimum standards for the protection of intellectual property for patents, trademarks, and copyrights, although several important aspects of intellectual property are not addressed.²⁰³ Cuban intellectual property law should at a minimum seek to meet the standards of the TRIPS Agreement.

The protection of confidential information, trade secrets, and

¹⁹⁸ Intellectual property rights in areas of advanced technology include confidential information, trade secrets, know-how, patents, copyrights, and design rights. See generally Christopher Millard, Mark Owen & Deborah Ishihara, *Intellectual Property Aspects of Technology Transfers*, in INTERNATIONAL TECHNOLOGY TRANSFERS 2 (Harry Rubin, ed. & contrib. ed. 1995) [hereinafter INTERNATIONAL TECHNOLOGY TRANSFERS].

¹⁹⁹ CUBA PROSPECTS, *supra* note 23, at 131. Cuba's VA-MENGOC-BC vaccine, for example, is reportedly the most effective anti-meningococcal vaccine in the world so far. *Id.* at 135.

²⁰⁰ Antonio Mendoza, *Promoting the Transfer of U.S. Technology Across National Borders: The Enemy Within*, 20 N.C. J. INT'L LAW & COM. REG. 97, 99 (1994); see also Tara Kalagher Giunta & Lily H. Shang, *Ownership of Information in a Global Economy*, 27 GEO. WASH. J. INT'L L. & ECON. 327, 335 (1993-94).

²⁰¹ INTERNATIONAL TECHNOLOGY TRANSFERS, *supra* note 198, at 1-2.

²⁰² Giunta & Shang, *supra* note 200, at 335-36. See generally J.H. Reichman, *Universal Minimum Standards of Intellectual Property Protection Under the TRIPS Component of the WTO Agreement*, 29 INT'L LAW. 345 (1995); Peggy E. Chaundhry and Michael G. Walsh, *Intellectual Property Rights: Changing Levels of Protection Under GATT, NAFTA and the EU*, 30 COLUM. J. WORLD BUS. 80 (Summer 1995).

²⁰³ Giunta & Shang, *supra* note 200, at 336-38.

know-how against disclosure or misuse by employees is another important aspect of intellectual property rights protection which is usually addressed by employment contracts and domestic tort laws. Cuba's tort laws should include provisions allowing employers—including foreign investors—to terminate current employees and sue former ones who divulge confidential information, trade secrets, or know-how to competitors, irrespective of whether such rights are included in the employment agreement. In addition, government sanctions should be established against employees who wrongfully divulge confidential information, trade secrets, or know-how. The sanctions could include, for example, withholding unemployment compensation and other benefits.²⁰⁴

4. Tax Laws

A country's attractiveness to foreign investors depends in large part on its system of taxation. As explained in Part IV.C.2 above, during its market transition, Cuba may opt to pursue tax reforms that specifically benefit foreign investors. In any case, Cuba should implement changes to its tax laws that benefit foreign investors indirectly by establishing an equitable and predictable system for all taxpayers. Indeed, experience with tax reform in developing countries shows that a healthy tax system is a pre-requisite to foreign investment, irrespective of whether preferential tax treatment is accorded to foreign investors.

A comparison between the experience of Bolivia in the 1980s with that of present-day Russia is instructive in this regard. Tax reform in Bolivia in 1986 succeeded in bringing inflation down from an annual rate of 12,000 percent to 14 percent in the space of two years.²⁰⁵ The reform also sufficiently stabilized the tax environment to reverse the effects of a fiscal crisis occasioned by a world recession in the early 1980s that had all but cut off the flow of foreign investment.²⁰⁶ In contrast, Russia has created a patchwork quilt of tax laws and implemented piece-meal tax reforms, leading to an overall climate of regulatory uncertainty that deters foreign investment.²⁰⁷

To be supportive of foreign investment, Cuba's tax system should

²⁰⁴ The Costa Rican Labor Code, for example, contains provisions authorizing the termination of compensation of employees who reveal trade secrets or know-how to their employer's competitors. CORPORACION INTERAMERICANA DE INVERSIONES, COSTA RICA, ENTORNO REGLAMENTARIO, INVERSION EXTRANJERA Y PROPIEDAD INTELLECTUAL 57 (1992).

²⁰⁵ Richard M. Bird, *Tax Administration and Tax Reform: Reflections on Experience*, in TAX POLICY IN DEVELOPING COUNTRIES 43-44 (Javad Khalilzadeh-Shirazi & Anwar Shah eds., 1991) [hereinafter TAX POLICY IN DEVELOPING COUNTRIES].

²⁰⁶ *Id.*

²⁰⁷ Jeffrey M. Trinklein, *Russia Makes Significant Changes to Profits Tax, Amends Excess Wages Tax and VAT*, 8 TAX NOTES INT'L 1039 (1994); see also Hans Jochum Horn, *Russia: A Tax Paradise Lost*, 9 TAX NOTES INT'L 331 (1994).

be simple, uniform, centralized, and well-administered. Good administration is important: in the early stages of its transition to a free-market economy Cuba, like many developing countries, will likely face the problem of poor tax administration, which may effectively negate the benefits of even the most enlightened tax code.²⁰⁸ Likely lapses in administration should be compensated for by devising a tax system that features a simple rate structure and few, broad categories of taxes that apply equally to foreign and domestic businesses. Cuban tax legislators would be well advised to use tax exemptions and targeted tax incentives sparingly,²⁰⁹ and to resist populist pressures to implement redistributive measures such as steeply progressive rates.²¹⁰ Close attention should be paid to improving collection techniques and properly screening personnel in order to minimize the possibility of corruption by tax collectors and other officials.²¹¹

It is equally important that the tax system be centralized. During their market transitions some countries, notably Russia and China, devolved taxing power from the central authority to the local governments.²¹² Though perhaps ultimately desirable, early tax decentralization has led in those countries to competing tax initiatives by central and local governments, resulting in an increased overall burden on the taxpayer.²¹³

In addressing the specific tax concerns of foreign investors, elimination of double taxation should be a top priority. Most countries follow the "territorial method" of taxation and levy taxes on all income earned in the country, whether by a citizen or a foreigner. Some countries, however, tax their residents on their world-wide income ("using a residence-based method"), and several countries combine the two methods.²¹⁴ Double taxation results when an

²⁰⁸ Bird, *supra* note 205, at 49.

²⁰⁹ As noted earlier, most countries in Central and Eastern Europe and Latin America have abandoned tax incentives as ineffective in attracting foreign direct investment. See *supra* part IV.C.3; Wayne Thirsk, *Lessons from Tax Reform: an Overview*, in TAX POLICY IN DEVELOPING COUNTRIES 60 (1990).

²¹⁰ For a survey of Latin American countries' success in eliminating complex taxes and redistributive biases see Bird, *supra* note 205, at 47-48.

²¹¹ Charles McLure & George Zodrow, *Tax Reform in Colombia: Process and Results*, in TAX POLICY IN DEVELOPING COUNTRIES 18 (Javad Khalilzadeh-Shirazi & Anwar Shah eds., 1990). Colombian tax reform of 1988 curbed wide-spread corruption among tax administrators, who had been known to extort bribes by threatening to "lose" tax returns. Under the tax reform, the collection responsibility was shifted to commercial banks, thus minimizing the direct contact between taxpayers and tax officials and the resulting potential for abuse. *Id.*

²¹² See Roger H. Gordon, *Economic Reform in the People's Republic of China, 1979-1988 in WORLD TAX REFORM 189-90* (1990). See also 1 BUSINESS VENTURES IN EASTERN EUROPE RUSSIA 2-133, 2-134 (David E. Birenbaum ed., 2d ed. 1994).

²¹³ See Gordon, *supra* note 212, at 190; BUSINESS VENTURES IN EASTERN EUROPE RUSSIA, *supra* note 212, at 2-134.

²¹⁴ Hong Kong, the United States and Germany are examples of the purely territorial method, the residence-based method, and the mixed method respectively. See Chad Leechor & Jack Mintz, *Taxation of International Income by a Capital-Importing Country: The Perspective of*

investor's home country and the host country follow different methods, so that the profits generated by the investment are taxed by the host country under the territorial method, and by the home country under the residence-based method.²¹⁵

The two devices most commonly used to alleviate the double-taxation problem faced by foreign investors are double-taxation treaties and foreign tax credits.²¹⁶ Treaties for the avoidance of double taxation (i.e., bilateral agreements setting the order of taxation) are favored by those countries that follow the territorial principle (e.g., most countries in Western Europe), while foreign tax credits are used by those countries that tax their residents on their world-wide income (e.g., the United States, China and Russia) as a way to offset the amount of foreign tax already paid.²¹⁷ Capital importing countries such as Cuba should use treaties and foreign tax credit statutes to assist investors from countries using both systems.²¹⁸

Finally, Cuba should pursue a tax reform program that emphasizes consistency and advance planning. No changes should be introduced without affording those affected advance notice and opportunity for comment, and grandfathering provisions should be used where appropriate. There should also be no sudden reversals of those reforms already in place, a practice in which for example present-day Russia and Colombia in the 1970s engaged.²¹⁹ Together with sensitivity to the tax pressures faced by foreign investors at home, consistency and ample advance notice would create a predictable tax environment that would encourage foreign investment in Cuba.²²⁰

B. Other Laws Having Potential Effects on Foreign Investment

In addition to those laws that should be expected to have a positive effect on foreign investment, there are other laws that are not directly related to foreign investment, but which may indirectly affect foreign investment by improving the economic climate or, alternatively, by imposing requirements that raise costs or make the investment process more difficult. This section surveys five such types of laws.

Thailand, in TAX POLICY IN DEVELOPING COUNTRIES 103 (Javad Khalilzadeh-Shirazi & Anwar Shah eds., 1991).

²¹⁵ *Id.*

²¹⁶ *Id.*; see also SWAN & MURPHY, *supra* note 26, at 715-16.

²¹⁷ *Id.* at 104.

²¹⁸ *Id.* at 103; see also Javad Khalilzadeh-Shirazi & Anwar Shah, *Introduction and Overview*, in TAX POLICY IN DEVELOPING COUNTRIES xviii (Javad Khalilzadeh-Shirazi & Anwar Shah eds., 1991).

²¹⁹ See Trinklein, *supra* note 207, at 1044; McLure & Zodrow, *supra* note 211, at 5.

²²⁰ See generally Javad Khalilzadeh-Shirazi & Anwar Shah, *supra* note 211.

1. *Economic Restructuring Laws*

Economic restructuring legislation will need to be enacted early in Cuba's transition from a centrally-planned economy to a free-market one.²²¹ Some of that legislation may serve to unleash market forces and thereby foster foreign investment.

An example of an economic restructuring move that would have beneficial impact on foreign investment would be de-controlling prices. Elimination of government controls on prices is one of the basic requirements for the establishment of a free-market economy, and one that has been accomplished in most countries making the transition from socialism in Central and Eastern Europe.²²²

A detailed discussion of economic restructuring laws is outside the scope of this article. However, such laws provide an essential backdrop to any efforts to foster foreign investment in Cuba during its free-market transition.

2. *Worker Benefits and Foreign Labor Restrictions*

Labor laws and regulations,²²³ and the costs they impose on employers, are an important factor in the investment climate.²²⁴ In enacting new labor laws and regulations, the Cuban Government must make a trade-off between providing worker benefits and social safety nets to promote social stability, and cutting operational costs to employers so as to promote foreign investment.²²⁵ It seems likely that the extensive social safety net now in place in Cuba will be preserved to some extent during the country's transition to a market economy.²²⁶ This prospect is reinforced by the experience of most Central and Eastern European countries, which have chosen, or been forced, to preserve their well-developed but costly social safety nets.²²⁷ If Cuba retains a significant social safety net it should take steps to clearly define foreign employer liabilities and responsibilities towards

²²¹ Travieso-Diaz & Escobar on Cuba's Transition, *supra* note 136, at 410-11, 418-19.

²²² Economists tend to agree that price liberalization must be introduced immediately once Cuba starts its transition to a free-market economy. Gradual price liberalization is regarded as counterproductive, since it could lead to spiraling prices and shortages of goods. See, e.g., Ernesto H. Hernandez-Cata, *Long Term Objectives and Transitional Policies—A Reflection on Pazos' "Economic Problems of Cuba,"* in CUBA IN TRANSITION—PAPERS AND PROCEEDINGS OF THE FIRST ANNUAL MEETING OF THE ASSOCIATION FOR THE STUDY OF THE CUBAN ECONOMY, Miami, Fla., 36, 46-50 (Aug. 1991).

²²³ Employee-employer relations, minimum wage provisions, and other standard labor law topics are outside the scope of this paper.

²²⁴ LEGAL TREATMENT OF FOREIGN INVESTMENT, *supra* note 9, at 25.

²²⁵ *Id.*

²²⁶ Travieso-Diaz & Escobar on Cuba's Transition, *supra* note 136, at 409-10.

²²⁷ *Id.*

the labor force and avoid unwritten or poorly defined requirements.²²⁸ These steps should include provisions requiring communicating to foreign investors all social safety net laws to which they may be subject. The Cuban Government may also come under pressure to impose restrictions on the ability of private enterprises to hire foreign employees. Such restrictions could include the need to obtain work permits and the placement of limits on the number of foreign employees allowed at an enterprise.²²⁹ Restrictions on foreign employees, such as work permits, are in use in many countries.²³⁰

In developing the transition period labor laws, provisions which require local labor participation (e.g., mandating the hiring of local management personnel) should give way to allowing investors freedom in their employment decisions because provisions regulating foreign investor hiring practices will probably deter some kinds of investment, particularly those calling for workers with skills in short supply.

3. *Immigration Laws and Restrictions*

As Cuba's transition progresses and the country's political and economic situation settles, foreign investors will probably seek to visit the island in increasing numbers.²³¹ The Cuban Government should take steps to facilitate temporary visits and the long-term or permanent migration of foreign investors.

One important issue which needs to be resolved in developing an immigration regime for foreign investors is the treatment of Cuban expatriates who wish to invest in Cuba. Should they be considered "foreign" investors and be eligible for any special benefits given to such investors?²³² On the one hand, the definition of a foreign citizen should be as broad and inclusive as possible to maximize the inflow of

²²⁸ In Guatemala, for example, employees may accrue benefits which the employer provides without legal or contractual obligation. For example, if an employer establishes a tradition of paying a bonus in addition to a statutory required bonus, such as the Christmas bonus, such a bonus could become an "acquired right." The employee could sue to collect an acquired right bonus if, for example, the enterprise's earnings were down and the employer did not pay the bonus. U.S. DEPARTMENT OF LABOR, FOREIGN LABOR TRENDS: GUATEMALA 10 (1990).

²²⁹ Costa Rica, for example, requires that 90% of the total employees in a given enterprise be Costa Rican nationals, although two managers are exempt from this quota. The Costa Rican government also requires work permits for foreign employees. Robert Harlan Stempler, *Costa Rica: A Nirvana for Export Manufacturers?* 4 TRANSNAT'L LAW. 201, 205 (1991).

²³⁰ Most economists recognize that there are both positive and negative consequences to controlling immigration into a country. In the U.S. the issue has been fiercely debated since the nineteenth century. See STEPHEN H. LEGOMSKY, IMMIGRATION LAW AND POLICY 181 (David L. Shapiro et al. eds., 1992) [hereinafter IMMIGRATION LAW].

²³¹ See *Opening the Door for Business Travel to a Free-Market Cuba*, 1 FREE MARKET CUBA BUS. J. 7 (Shaw, Pittman, Potts & Trowbridge, Spring/Summer 1992) [hereinafter *Opening the Door*].

²³² Travieso-Diaz & Escobar on Cuba's Transition, *supra* note 136, at 414-15.

foreign-based capital.²⁹³ On the other hand, granting Cuban expatriates privileges unavailable to resident nationals could lead to resentment from people on the island. This is an extremely sensitive political issue that is part of the broader question of the citizenship status and rights of those Cuban nationals who have moved abroad and acquired foreign citizenship.²⁹⁴

One component of the foreign investor immigration treatment is the visa structure for business travelers. A business visa structure during Cuba's market transition will likely follow one of four patterns:

- a) No visa requirement for short-term business trips (A visa would be required only if the trip was to extend beyond the designated period—several countries, such as Chile and the Czech Republic, have implemented this type of visa structure);
- b) No visa requirements for business travel, unless the foreign national will be employed during the trip (several Western European countries have a visa structure along these lines);
- c) A visa structure similar to that of the United States, under which there would be several categories of business visas corresponding to the nature of employment performed in the host country and the duration of the stay; and
- d) A requirement that all business visitors obtain a visa, with different eligibility criteria depending on the purposes and intended length of stay.²⁹⁵

In developing its business visa structure, the Cuban Government should keep in mind several important considerations regarding foreign investors. First, and probably most importantly, foreign investors should have the ability to employ foreign personnel, particularly for key positions.²⁹⁶ The Cuban government should therefore refrain from unduly limiting the number of foreign personnel a company can bring into the country, or imposing unreasonable time limits on their visas. As noted earlier, there will be an acute shortage of skilled management personnel in Cuba during the transition to a market economy, so a large number of foreign managers will be necessary to operate foreign investors' enterprises until the local population acquires the requisite management and business skills.

Second, the Cuban business visitor visa structure should not

²⁹³ Under Cuba's constitutions, both pre- and post-revolution, a Cuban citizen who becomes a citizen of another country loses his Cuban citizenship. CONSTITUCION DE LA REPUBLICA DE CUBA, art. 15 (CUBA 1940), *reprinted in* 1 CONSTITUTIONS OF NATIONS 612 (Amos J. Peaslee ed. & trans., 2d ed.) [hereinafter CONSTITUTION]; CONSTITUCION DE 1992, *supra* note 22, art. 32. Thus, unless the laws are changed, Cuban expatriates will need to be classified as foreign investors.

²⁹⁴ *Id.*

²⁹⁵ *Opening the Door, supra* note 231, at 8.

²⁹⁶ *See* LEGAL TREATMENT OF FOREIGN INVESTMENT, *supra* note 9, at 159.

establish special visa categories for particular classes of foreign investors. An example of this type of visa is the "alien entrepreneur" visa program in the United States, which reserves a certain number of immigrant visas for investors "who establish new commercial enterprises in the United States, invest at least \$1,000,000 . . . and employ at least ten Americans."²³⁷ This type of special incentive is warranted only if a restrictive business visa structure is in place, which should not be the case in Cuba during the transition to a market economy. Both large and small investors should be allowed easy access to the island.

Finally, the business visa structure during the transition period should be kept simple. This approach would reduce time and transaction costs for foreign investors, and thus encourage foreign investment. In addition, a simple business visa structure would reduce the cost and complexity of administering the program, another important consideration given Cuba's lack of resources.

4. *Environmental Laws*

During the early phase of its transition to a market economy, Cuba may refrain from imposing major new environmental requirements or assessing liabilities for past environmental damage.²³⁸ Significant environmental legislation may not be put in place until several years after the transition to a market economy, when the economy has stabilized and recovery is on its way.²³⁹ Given the extent to which environmental degradation has already occurred in Cuba, however, the enactment of wide-ranging environmental legislation is likely to be inevitable. In addition, Cuba's growing tourism industry will require a high level of environmental quality control (i.e. clean beaches, unpolluted coastal waters, etc.) and, consequently, increased environmental regulation.

The need to comply with Cuba's environmental laws will be a factor that sophisticated foreign investors will include in their investment decisions.²⁴⁰ Pre-investment planning often includes examining existing and imminent environmental laws to find ways of structuring the investment so that compliance with the laws is achieved while minimizing its impact on the cost of the projects.²⁴¹ Adequate

²³⁷ IMMIGRATION LAW, *supra* note 230, at 196; IMMIGRATION AND NATIONALITY ACT § 203(b)(5), 8 U.S.C. § 1153(b)(5) (1990).

²³⁸ Travieso-Diaz & Escobar on Cuba's Transition, *supra* note 136, at 421.

²³⁹ *Id.* at 422.

²⁴⁰ Anecdotal evidence suggests that businesses increasingly factor environmental issues into their foreign investment decisions. See, e.g. Norman E. Gelber, *Apparel Dominates Caribbean Conference*, BOBBIN, Feb. 1993, at 76 (comment by a Levi Strauss & Company's executive).

²⁴¹ Frederick R. Anderson, *Environmental Aspects to Foreign Investment in Latin America*, in INVESTMENT AND TRADE IN ARGENTINA, BRAZIL, CHILE, MEXICO AND VENEZUELA (1992), at 151, 154-55 (PLI Commercial Law and Practice Course Handbook Series No. 643, 1992).

environmental compliance plans help prevent environmental disasters, allow proposed projects to proceed successfully through the pre-approval review process, and in case of a legal challenge, help convince the decisionmaker that the project meets environmental standards.²⁴²

Additional environmental compliance issues will be faced by foreign investors who become involved in the privatization of state enterprises. The main questions in those cases will have to do with the extent to which an investor acquiring a state enterprise will assume liability for environmental damage or hazards created by the enterprise while in the hands of the state.²⁴³ In Czechoslovakia, for example, uncertainty over responsibility for environmental liabilities incurred in the past by state enterprises raised concerns with foreign investors that participated in the country's privatization program.²⁴⁴ The Czech government has tried to deal with this issue by promising investors limited indemnification for environmental liabilities which have not been identified at the time a venture is negotiated.²⁴⁵ Cuba will need to develop clear rules for determining the extent to which investors acquiring privatized enterprises are subject to liability for past environmental damage.

5. *Alternative Dispute Resolution*

The existence of effective dispute resolution mechanisms is an important factor in a foreign investment decision since the expectation of prompt and fair resolution of disputes bears on the safety of an investment. An effective judicial system in Cuba would go a long way towards assuring an investor that his/her investment is secure. However, the Cuban judicial system will probably be overloaded and have little experience in adjudicating international business disputes during the country's transition to a market economy. Thus, foreign investors will likely favor contractually-agreed arbitration to resolve disputes that arise from doing business in Cuba.²⁴⁶

Arbitration is increasingly used to settle international investment disputes.²⁴⁷ In the Western Hemisphere, three treaties establish substantive law and procedures for international arbitration: 1) the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (U.N. Convention); 2) the Inter-American

²⁴² *Id.* at 152. The impact of growing environmental consciousness in the Caribbean Basin cannot be understated. Exxon, for example, scrapped an oil drilling project in the northern jungle of Guatemala due to criticism by environmental groups. Exxon had sunk approximately \$21 million into the project. Chris Brogan, *Overtures Made to Oil Explorers*, 59 PETROLEUM ECONOMIST, June 7, 1992.

²⁴³ EVOLVING LEGAL FRAMEWORKS, *supra* note 103, at 55.

²⁴⁴ *Id.*

²⁴⁵ *Id.*

²⁴⁶ Travieso-Diaz & Escobar on Cuba's Transition, *supra* note 136, at 400-01.

²⁴⁷ SWAN & MURPHY, *supra* note 26, at 958.

Convention on International Commercial Arbitration (Inter-American Convention); and 3) the ICSID Convention.²⁴⁸ The Inter-American Convention "essentially replicates the . . . [U. N. Convention], with the major difference [being] that the Inter-American Convention provides for a mechanism to administer international commercial arbitrations in the [Western] Hemisphere and, in addition, provides for rules of procedure."²⁴⁹ The ICSID Convention, as mentioned earlier, only applies to disputes between investors and the host state.²⁵⁰

Cuba's accession to the various international arbitration conventions (which are not mutually exclusive) would set up a viable dispute resolution mechanism to handle foreign investor claims during Cuba's transition to a market economy. This mechanism would be particularly well-suited to the transition period, given that the Cuban judiciary system will then be ill-equipped to deal with foreign investor disputes.

VI. Conclusion

Cuba has recently introduced a number of economic reforms and is likely to implement additional measures to create a favorable environment for foreign investment. Cuba has also sought to make attractive opportunities available to foreign investors, and has succeeded in bringing investments to certain areas of its economy, notably tourism. A new foreign investment code, providing for limited liberalization of the investment rules, has just been enacted.

Despite these advances, foreign investment in Cuba remains a difficult, high risk proposition. Unless and until there is a significant relaxation of the government controls and investment restrictions that are now in place, it is unlikely that there will be a sufficient influx of foreign investment to turn the economy around. Accordingly, Cuba's political leaders during the transition should place a high priority on creating a foreign investment structure—in the form of a modern Foreign Investment Code, related laws, and appropriate administrative mechanisms—that make the decision of a prospective foreign investor to go into Cuba easy to reach and just as simple to carry out.

²⁴⁸ Charles Robert Norberg, *Symposium: Current Issues in International Commercial Arbitration: Recent Developments in Inter-American Commercial Arbitration*, 12 J. INT'L. L. BUS. 86 (Spring/Summer 1991). The U.N. Convention has been ratified by sixteen Western Hemisphere countries (including Cuba), the Inter-American Convention by thirteen, and the ICSID Convention by ten. *Id.* at 89.

²⁴⁹ *Id.* at 89.

²⁵⁰ BARRY E. CARTER & PHILLIP R. TRIMBLE, *INTERNATIONAL LAW* 339 (1991).