Foreign Investment in a Post-Conflict Environment

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Overview

1. Background
2. Bringing Foreign Investment to Post-Conflict States
3. The Case Study of Iraq
4. Conclusions

Benefits of Foreign Investment for Post-Conflict States

- Attracting needed capital
- Increasing financial resources for development
- Infrastructure development
- Generating employment opportunities and training
- Transfer of technology
- Providing a powerful "demonstration effect"
Key Considerations

**Foreign Investors**
- Physical Safety
- Investment Security
- Stability of Post-Conflict Governments

**Host Country**
- Attract favorable foreign investment
- Retain ability to regulate in the public interest
BRINGING FOREIGN INVESTMENT TO POST-CONFLICT STATES

Issues to Consider

1. Presence of Investment Opportunities
2. Legal Protections
3. Corruption
4. Physical Security
5. Political Risk Insurance

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Presence of Investment Opportunities

- Two key areas:
  - Natural resources in the host State
  - Infrastructure projects related to rebuilding of the country
BRINGING FOREIGN INVESTMENT TO POST-CONFLICT STATES

Presence of Investment Opportunities: Natural Resources

- Among this week’s Economist headings
  - Iraq’s Kurdish oil: Kurdistan goes glug glug
  - Sierra Leone and its diamonds: Digging in the dumps
  - Fighting in Nigeria’s Delta: Getting desperate

Economist, May 30-June 5, 2009
Presence of Investment Opportunities: Infrastructure

- A State should adopt policies to attract foreign investment for needed infrastructure projects
- **Example: Telecommunications in Afghanistan**
  - Transitional Government adopted an open telecommunications policy
  - Foreign investors created leading telecommunications operator in Afghanistan: Roshan
  - Roshan provided new telecommunication technology, created 25,000 jobs and is the largest taxpayer in Afghanistan
Legal Protections

- Judicial infrastructure likely being rebuilt
- Avoid local courts – provide for arbitration to resolve disputes
- Select applicable law carefully
Legal Protections: Bilateral Investment Treaties

- Consider any applicable Bilateral Investment Treaties (BITs) for protections against acts of the host State
- Protections contained in BIT Provisions
  - Providing for binding third-party arbitration between investors and host State
  - Guaranteeing fair/equitable treatment, full protection and security
  - Restricting host state’s right of direct/indirect expropriation
  - Requiring national and MFN treatment for investments
  - Requiring host State to observe any commitments it may have entered regarding investments
  - Guaranteeing right to transfer investment/returns into freely convertible currency
Legal Protections: Local Laws and Contractual Protections

- Constitutions or foreign investment laws may provide important protections against acts of the host State.
- Investment agreements themselves may contain general/specific promises to investor.
- If no BIT, imperative to have an arbitration clause in contracts with the host State:
  - Should include appropriate waivers of sovereign immunity.
Corruption

The Transparency International Corruption Perceptions Index measures the perceived levels of public-sector corruption in a given country and is a composite index, drawing on different expert and business surveys. The scores range from zero (highly corrupt) to ten (highly clean).
BRINGING FOREIGN INVESTMENT TO POST-CONFLICT STATES

Corruption

- Undermines good governance, democracy and development
- “Grease the wheels” by paying bribes to government officials?
  - Negative association between FDI flow in host country and corruption in that country
  - “Helping hands” often outweighed by “grabbing hands”
  - Cannot guarantee paying a bribe will yield desired outcome
Combating Corruption by Promoting the Rule of Law

- Deterrent effect through criminalization of bribery and corruption
- Administrative law can help prevent corruption
  - Can ensure greater transparency
  - Necessary administrative changes range from:
    - Improving pay and working conditions of government workers
    - Monitoring government employees
  - Establishment of anti-corruption commissions
Corruption: Consequences to Foreign Investors

- Consequences under law of home state (e.g. FCPA)
- Consequences to being able to pursue claims arising from investment before an international arbitral tribunal

  “This Tribunal is convinced that bribery is contrary to the international public policy of most, if not all, States…. Thus, claims based on contracts of corruption or on contracts obtained by corruption cannot be upheld by this Arbitral Tribunal.”

  *World Duty Free v. Kenya*, ICSID Case No. ARB/00/7, Award (Oct. 4, 2006)

  That corruption may be a “generally accepted practice” is not acceptable justification

  *ICC Case No. 3916* (1994)
Physical Security

• Characteristics of post-conflict countries:
  – Destroyed basic infrastructure
  – Weakened currency exchange rate
  – Seriously diminished human resources
  – Damaged institutions

• The status of physical conflict and the threat of resumed violence as a deterrent
Physical Security: The Case of Basra

- 70% of Iraq’s oil reserves
- Sole deepwater port
- Fear of violence when British handed authority to Iraqi authorities.
- “Charge of the Knights”: rid the city of Sadr-loyalist Mahdi army. Ended 2 years of rival gang wars.
- Hope amidst the uncertainty: proposal by ArcelorMittal and positive assessment by KPMG.
Political Risk Insurance

- Protection for foreign investors
  - Overseas Private Investment Corporation (“OPIC”)
  - Multilateral Investment Guarantee Agency (“MIGA”)
    1. Currency Transfer
    2. Expropriation and Similar Measures
    3. Breach of Contract
    4. War and Civil Disturbances
  - Private Insurance
Political Risk Insurance: The MIGA Effect

- MIGA: “a visible manifestation of hope”
- MIGA’s Afghanistan Investment Guarantee Facility (“AIGF”)
  - New Business Opportunities in Afghanistan
  - Allay investor concerns about political risk
  - Facilitate small and medium-sized investments
- Iraq signs MIGA Convention in 2007
Investment Climate in Iraq

- Violent groups:
  - “Industrial strength” criminal gangs
  - Independent militias
  - Insurgency groups

- Resulting instability:
  - Devastated economy with high unemployment
  - Lack of a framework for effective governance
  - Widespread corruption

- Oil: the clearest transition to a stable economy open to the global marketplace
Evolving Potential?

• Improvements in Iraq
  – Changes to economic policies: pension reform, renewed commitment to WTO accession
  – Iraqi Investment Law (2006): opening the economy to foreign investment
  – Oil & Gas Law (2007): a critical tool for rebuilding the economy around the resource
  – Increased efforts to attract investment & increase oil production:
    • Enhanced foreign ownership rights
    • Production-sharing agreements: direct profit share instead of fixed fees
## The Case Study of Iraq

### Legal Protections

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<tr>
<th><strong>Signatory to:</strong></th>
<th><strong>Not a Signatory to:</strong></th>
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THE CASE STUDY OF IRAQ

Legal Uncertainty

Article 111:
Oil and gas are owned by all the people of Iraq in all the regions and governorates.

Article 110:
The federal government shall have exclusive authorities in the following matters:

Article 115:
All powers not stipulated in the exclusive powers of the federal government belong to the authorities of the regions and governorates that are not organized in a region. With

Article 112:
First: The federal government, with the producing governorates and regional governments, shall undertake the management of oil and gas extracted from
Conclusions

1. Know your investment
2. Something went wrong: you find yourself in local court of law
3. Political risk insurance
4. Uncertainty over political/legal landscape in addition to security
5. Be mindful of local interests