PART ONE

Certain preliminary issues

1

Foreign investment in politico-economic perspective

The legal regime of foreign investment in Sudan and Saudi Arabia, as in other countries, cannot operate in isolation from politico-economic factors general to the international arena; nevertheless, such a legal regime also reflects national policy, and it is, accordingly, necessary at the outset to describe not only the general factors, but also Sudanese and Saudi national policies towards foreign investment.

1. The new trends in the international investment climate

There was much controversy surrounding the international law relating to foreign investment. Such controversy was at first due to the conflict among many forces released at the end of the Second World War. The ending of colonialism prompted forces of nationalism, which swept the Third World. Many developing countries were at one time colonies, mostly of industrialized Western powers from where foreign investment traditionally comes. Accordingly, developing countries chose to cling to their independence and were suspicious of any foreign relationships which might seem to endanger the newly obtained sovereignty. The newly independent states agitated not only for the ending of the economic dominance of the former colonial powers within their territories but also for a new world order which would permit them to regulate and control all economic activities in their own territories and to have access to world markets on an equitable basis.[1]

It was not possible at all for all nations to agree on international law rules governing foreign investment during the last decades of the twentieth century, due to ideological conflicts resulting from the Cold War between the two superpowers. The Non-aligned Movement, which arose in response to this rivalry, exerted pressures to ensure that each newly independent state had complete sovereignty over its economy. The emphasis of developing countries on their economic nationalism was articulated in several statements of principles in United Nations resolutions. These resolutions have tended to formulate new doctrines on establishing a new international economic order as spelled out in particular in the resolutions on the Declaration on the Establishment of a New International Economic Order,[2] and the Charter of Economic Rights and Duties of States, 1974.[3] The essence of this is the claim that every state has the right to full and permanent sovereignty over its natural resources and that every state has the right to exploit these natural resources. This comprehends the right of every state in accordance with its own legislation to exploit these natural resources by nationalization of enterprises in return for compensation and that foreign investment disputes should be settled in the national courts according to local law. These documents have also emphasized that transnational corporations should not interfere in the internal affairs of investee states.

The spirit of these declaratory principles was respected in the United Nations Report of Eminent Persons.[4] This report addressed itself to a number of problems relating to the activities of multinational corporations and foreign private investment. It stressed the need for a code to regulate the activities of multinational corporations through which a good portion of foreign private investment is channelled to developing countries. In accordance with the Group of Eminent Persons' recommendation,[5] the Economic and Social Council of the United Nations established the Commission on Transnational Corporations to deal with issues concerning multinational enterprises, and in particular to formulate their code of conduct.[6] Until the mid-1980s, many developing countries viewed multinational corporations with suspicion, and tended to curtail their freedom of action through outright prohibitions, limitations on the industries in which they were allowed to operate, restrictions on profit remittance and capital repatriation or the imposition of stringent performance requirements. This topic and other similar issues are also under extensive discussion in the United Nations Conference on Trade and Development (UNCTAD) and in the North–South dialogue and others like the WTO, in which fora the developing countries are seeking to restructure the whole world economy and the international financial institutions in a way that takes note of their concerns. This move has tended to encounter resistance from the industrialized countries, which have often favoured the status quo.[7]

But since the capital and technological needs of the developing countries are so great, and cannot at present be met from domestic funds, they have recognized the importance of foreign private capital in exploiting their natural resources so as to achieve their economic development goals through quick industrialization.[8] Accordingly, they invite and welcome foreign capital, provided that it is kept under control and does not dominate their economies and impinge on their sovereignty. This new pragmatic attitude towards foreign investment has been augmented by the recent developments in the international arena, the most important of which has been the disintegration of the Soviet Union. This development has resulted in the disappearance of the Cold War and the demise of the socialist and the communist doctrines, which are antagonistic to foreign investment. The debt crisis in the 1980s has added fuel to the needs of the developing countries for the inflow of foreign capital to their economies. There is now a perception of mutual need that has been accentuated by recent trends in the international economy, which has shifted towards compromising stances to accommodate mutual interests. The outcome of this swift change of attitude has been the replacement of the rhetoric of economic nationalism by a new regime based on adoption of free market philosophy in which the private sector plays an active role both in investment and development.

Most developing countries now welcome and invite foreign investments and have liberalized considerably their rules and regulations (investment codes) in this respect. Similarly, there is now a much more widespread acceptance of the principle of national treatment of foreign investment. The liberalization trend has also meant a dramatic decline – even virtual disappearance – of nationalization of foreign affiliates since the peak reached in the mid-1970s. On the contrary, there is now a widespread trend towards privatization. Finally, an increasing number of countries are revising their intellectual property regimes and adopting new competition laws.

It has been reported by UNCTAD that these numerous and diverse changes in policies at the national level in respect to all aspects related to foreign direct investment and transnational corporations' activities are a significant part of the context of discussions about a possible multilateral framework on investment. This is also the case because the liberalization trend is strong in all regions of the developing world and in the economies in transition, having gone further in Latin America, in part because policies in that region used to be very restrictive before the recent changes.[9]

The liberalization of foreign direct investment has been complemented by the signing of an increasing number of bilateral investments and avoidance of double taxation treaties. Increasingly, these treaties are no longer between developed and developing countries alone, but also between developing countries and between these countries and countries with economies in transition. At the regional and multilateral levels too, an increasing number of agreements deal with investment issues.[10]

Indeed, and more generally, the situation is now one of competition over foreign direct investment, with the incentives to attract such investment becoming more widespread and generous. Developing countries now perceive foreign direct investment as making a positive contribution to their development. Generally, changes in the investment climate have been part and parcel of a broader set of reforms that include the opening up of the economy to foreign trade and greater emphasis on development strategies in attaining international competitiveness, deregulation and globalization.[11] The establishment of the World Trade Organization (WTO) has symbolized the institutional framework of these developments, which has contributed towards the liberalization of the international investment climate. The WTO is no longer limited to the elimination or reduction of restrictions to international trade but extends henceforth to investments in the territories of its members.[12]

The swift changes in the world economy have in the last decade of the previous century engendered wide-ranging transformations in the developing world both on economic and political levels. Thus, a wave of multiparty democratic regimes have emerged in countries once ruled for decades by totalitarian regimes, especially in Latin America, Eastern Europe and Africa. The outcome of these transformations has been the creation of globalized norms based on respect for human rights and freedoms. These developments have encouraged political stability, which has helped in creating a favourable investment climate.

Undoubtedly, the revolution in computer information technology as displayed by the Internet has speeded up the globalization process, especially in the field of electronic commerce, which has helped considerably the movement of capital across borders.

At regional level, there have been certain events which have left a negative impact on the investment climate in the Middle East, the most important of which were the two Gulf wars, one between Iraq and Iran in the 1980s, and the other between Iraq and the allied forces resulting from the

Iraqi invasion of Kuwait in 1990. These two wars had negative effects on the investment climate in terms of instability and drainage of financial resources diverted to finance the wars, especially with respect to Saudi Arabia and Kuwait, which were compelled to spend most of their reserves in buying arms to liberate Kuwait from the Iraqi occupation and to defend their territories against future threats from Iraq.

However, despite the havoc wrought by the two Gulf wars, there have been some positive developments in the investment climate due to the joint efforts of the Arab League, the Federation of the Arab Chambers of Commerce and the Inter-Arab Investment Guarantee Corporation in convening since 1980 successive yearly conferences of Arab businessmen and investors. At these conferences the participants expressed their willingness to direct their efforts towards joint Arab action to promote investments in the Arab World. The outcome was the establishment of specialized multimillion joint venture companies in different economic sectors subscribed to by investors from all Arab countries. These efforts to promote investment were complemented by additional initiatives by the Inter-Arab Investment Guarantee Corporation (whose membership comprises at present all Arab countries), which in addition to encouraging joint ventures among Arab investors, has also embarked upon the activity of compiling collections of all business and investment laws of the Arab countries, publishing investment guides and furnishing investment and export credit guarantees to Arab investors and exporters against non-commercial and commercial risks respectively for the promotion of inter-Arab trade and investment in the Arab region.[13]

2. Investment patterns in the international investment climate

(a) Direct participation, joint ventures and production-sharing agreements

As a result of widespread deviation from the concepts of welfare state and economic nationalism to free market patterns, there has been a rapid increase in direct private investment participation replacing the involvement of the state, whose role has been reduced to that of a regulator and to undertaking the building of the basic infrastructure. At present, foreign direct investment can be admitted in many economic sectors without any mandatory local participation, especially in non-strategic activities. In some instances the pattern of joint ventures between foreign and local investors still prevails.

In the oil sector, the traditional concession agreements are gradually giving way to production-sharing agreements such as that concluded by Sudan with the Chevron Company (which has been replaced by another agreement which we shall discuss later[14]), which is modelled on the agreements concluded by Indonesia, the pioneer in this field. The advantage of this kind of arrangement is that it enables the co-operation of foreign capital in countries not willing to accept direct foreign capital in the traditional form. Similarly, foreign investment nowadays takes the pattern of licensing arrangements, co-operative agreements, investment contracts, whether self-liquidating or restricted to certain functions to be performed by the multinational company, contracting and service agreements, especially in the mining sector, and disinvestment patterns.[15]

(b) Triangular arrangements

This is the most recent feature of foreign investment patterns in developing countries. As in Sudan, it combines Western technology and expertise with OPEC capital for the development of the non-oil developing countries.[16]

Indeed, OPEC can participate in various ways with Western firms in investment in non-oil developing countries. They may purchase shares in parent companies or even in their subsidiaries. By so doing, they can influence the types and amounts of investments undertaken by the parent companies in non-oil developing countries. The acquisition by Kuwait and Iran, respectively, of shares in a British and a German firm, apparently assumed this form.[17]

OPEC may also acquire a dominant interest in developing countries jointly with Western firms whose contribution in the investment project will be in the form of supplying management, technology and trade names in return for equity shares.[18] At present, there are several investment projects of this type. Egypt, for instance, has succeeded in erecting a vehicle assembly plant which has been installed in a duty-free zone. The annual production capacity of the project was expected to be 10,000 Land-Rovers for Arab markets. This project combined OPEC capital of about US$50 million provided by Saudi Arabia with British technical know-how and Egyptian manpower.[19] A similar project for the construction of a 'float process glass' manufacturing plant, to supply the Egyptian and other Arab markets, was recently negotiated between the Kuwait Investment Company, Egypt and the United Kingdom company Pilkington.[20]

(c) Four-cornered arrangements

Again, more than three parties may be involved in an investment project one of them being an international institution such as the International Finance Corporation (IFC), which adds to the attractiveness of a project for potential Arab investors. The financing schedule envisaged for a proposed $62 million chemical fertilizer plant in Jordan is of this type. The American firm constructing it will take a 25 per cent share of the capital, Jordan 50 per cent, the IFC 5 per cent and remaining 20 per cent was allotted to the public and the rest of the Arab world.[21] This pattern has increased recently, especially in the Islamic world where the Islamic Development Bank (the membership of which comprises all Islamic countries) has established the Islamic Finance Corporation, a replica of the IFC.

3. The role of international organizations in improving the investment climate

Global and regional[22] organizations, governmental or non-governmental,[23] have to a great extent directly or indirectly contributed to improving the investment climate in developing countries, at least in the following respects.

(a) Drafting of investment conventions and codes

International organizations have made extensive studies of the drafting of conventions, and codes, for the encouragement and protection of foreign private investment. With the exception of the World Bank Convention on the Settlement of Investment Disputes between States and Nationals of other States, the convention establishing the Multilateral Investment Guarantee Agency (MIGA)[24] and the investment conventions sponsored by the Arab League,[25] the North American Free Trade Agreement (NAFTA) and the Islamic Development Bank, none of the proposed conventions or codes has yet been agreed upon. Nonetheless, these draft conventions and codes must have a persuasive effect on the drafting of

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More Information

national investment laws, as well as bringing to light discrepancies amongst legal instruments, thus spurring perhaps a movement towards a general consensus in the future on regarding the shaping of the law on foreign investment protection. The most important endeavour in this respect is the set of guidelines on foreign investment formulated by the World Bank. The guidelines, preceded by a study of the existing instruments on foreign investments, are designed to contribute to the evolution of acceptable principles of international law and indicate the need for reaching a consensus on the international rules on protection of foreign investment, and the weight of the World Bank would be instrumental in moving in this direction (see below, p. **183**).

(b) Rendering of technical advice and research

International organizations have played a direct role also in ameliorating the investment climate by rendering technical advice and conducting studies and researches in favour of developing countries, thus helping them to pursue properly thought-out economic policies and drafting of encouragement investment codes. This task is usually performed by the United Nations specialized agencies such as the UNCTAD, UNIDO, the World Bank, the United Nations Centre on Transnational Corporations (UNCTC), the Organization for Economic Co-operation and Development (OECD) and the European Economic Community (now the European Union).[26] These studies furnish potential foreign investors with sufficient data for feasibility studies. Furthermore, the very rendering of the study or the evaluating of the economic potentialities of a developing country by an international organization may add to its credibility in the eyes of foreign entrepreneurs.

(c) Sharing in investment with private investors

Certain international organizations, such as the World Bank and its affiliates, either finance investment projects fully or in participation with local or foreign investors.[27] The establishment of development banks and funds, especially the OPEC Special Fund and the development funds of the Arab oil-rich countries such as Kuwait, the United Arab Emirates and Saudi Arabia, have helped to finance major investment projects, particularly in the infrastructural sector. Also, the accumulation of surpluses of oil money in the hands of the Arab countries has led to the formation of many Arab financing institutions which provide on a commercial basis credit facilities and syndicated loans to potential investors.[28] These financing institutions are designed to recycle Arab money to poorer countries, a strategy which should work favourably for Sudan. This direct involvement in the investments process by these international organizations and financing institutions has a positive psychological effect on the participation of foreign investors and persuades others to follow suit. It also strengthens the investors' belief in the profitability of an investment.

The size of the impact of these international politico-economic factors on the investment climate and the legal regime of foreign investment in Sudan and Saudi Arabia will be examined below.

4. Sudanese and Saudi Arabian foreign investment policies

(a) Sudan[29]

(i) Foreign capital and socialism in Sudan

The flow of foreign private capital to Sudan was to a great extent adversely affected by the 21 October Revolution in 1964, which ended the Abboud military regime. Indeed, that revolution marked a turning-point in Sudan's economic and social development. Socialist slogans calling for a state-non-economy and the nationalization of foreign trade and property were publicly raised by the communists and in other local socialist quarters. Though this did not ripen into any hard state policy at that time, yet it had a negative effect on foreigners, who began to liquidate their businesses in Sudan. Accordingly, the flow of foreign private capital was at that time much discouraged.

In 1970 these socialist principles were actually implemented by the dissolved Revolutionary Command Council of the '25 May Revolution, 1969', which nationalized all commercial banks and more than seventy major companies.[30]

(ii) Openness policy

After an abortive left-wing coup in July 1971, it became necessary to attain political stability. This could only be achieved by the active participation of large numbers of people in the government's administration and the shaping of its policy. These measures were vital for the success of the