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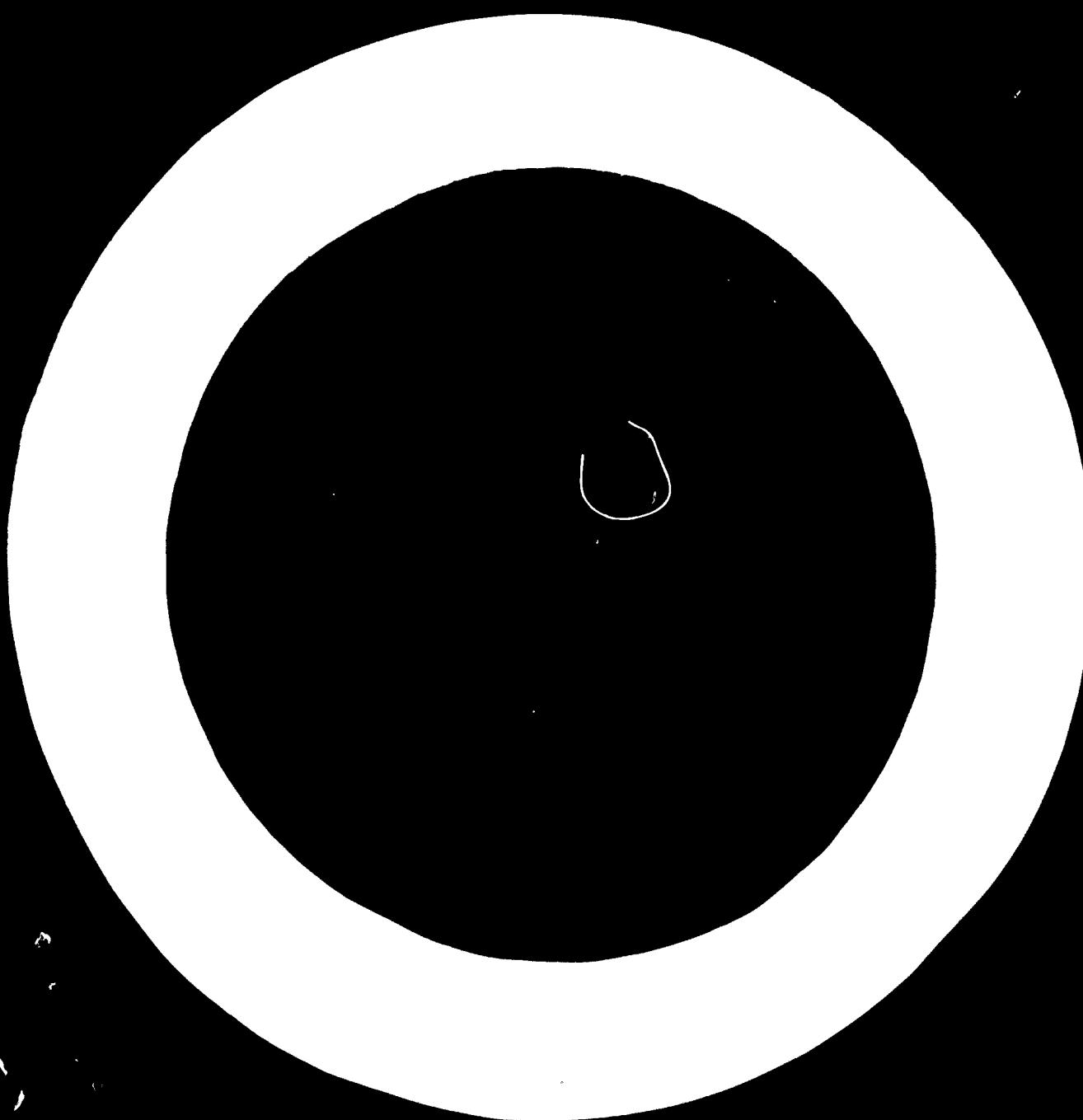
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ISSUE PAPER NO. 9

MEASURES TO FACILITATE FOREIGN INVESTMENT^{1/}

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MEMORANDUM FOR THE SECRETARY OF STATE

Investment in Latin America

1. It is the opinion of the Economic Commission for Latin America that the principal economic information available on investment in Latin America indicates that the trend towards diversification of foreign capital is continuing, and that there is no evidence of a general decline.

Investment in Latin America
1970-1971
Foreign Direct Investment
Latin American Countries

II. INVESTMENT POLICIES

1. It is generally recognized that the economic role of foreign investment in most developing countries is best at the level of projects for a satisfactory rate of return or profitable utilization of resources, and that these are therefore needed to achieve maximum efficiency. Similarly, most developing countries recognize the need to have incentives for foreign investment in the form of modern technological, management skills, etc., and to avoid excessive taxation in any way of obstructing these needs.
2. The purpose of this paper is to discuss the measures which a country will take to attract foreign investment, and if the country expects an inflow of foreign investment in an initial period, to examine these measures in the inter-related areas of fiscal, monetary, legal, and other measures considered in earlier ILOP Papers. Their incentive value depends on the extent to which they facilitate foreign investment and minimize the risks involved in the eyes of potential investors.

III. SURVEY OF MEASURES

3. A range of measures which can facilitate the attraction of investment can be taken to facilitate foreign investment. This section attempts, as far as possible under the following headings:

A. What different forms can foreign investment take?

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- (1) See profile to this document, published (Note No. 126) by Ministry of Foreign Affairs, Directorate General of Economic and Social Affairs, 15 January 1969.

III. What instruments can be used to promote
foreign investment?

1. Financial instruments

1) Direct or indirect utilization of
local or foreign capital.

2) What different forms can foreign investors take?

3) What instruments of financial control of a developing
country are available to foreign investors?

- (a) Direct investment after foreign control of
the enterprise;
- (b) A joint venture between local and foreign
partners;
- (c) Profits remitted in the form of equity
shares or loans;
- (d) In addition international financial
institutions and governments sometimes
channel funds for promotion of industrial
projects through a local industrial financing
institution.

4) The advantage of the joint venture form of direct investment
is the transfer, control of the enterprise is left a foreign enter-
prise the industrial experience, technology, and managerial skills
are fully involved in the operations of the project. Port-
folio investment and funds channeled through financial institu-
tions - for on-lending to industrial projects usually only contribute
to a greater volume of financial resources available for industrial
development. The issue arises which of these forms is the most
appropriate for developing countries? A further point can be
considered at this point. The background figures show that some
developing countries have encouraged direct investments in which a
foreign company is granted a majority participation. The issue
is what are the initial terms to investors before they rapidly
exit from the nation.

5) Many developing countries today face heavy external debt
~~problems~~. It is generally recognized that the cost of

servicing foreign investments in industrial projects over a period of years turns out to be more attractive than financing projects by the Government. This is because the long-term perspective of industrial investors makes it easier for governments to have clear and stable policies. It is also important to have stable economic conditions, sufficient investment in infrastructure, debt-service cover under export credits, and a natural break in the cost of capital for investment.

The following can be taken as suitable for an answer:

7. Measures to facilitate foreign investment can include the following:

- (i) An adequate legal framework;
- (ii) Assurances and guarantees;
- (iii) A favorable policy on the remittance of capital and dividends;
- (iv) Fair treatment under international tax agreements;
- (v) Fair trade without employment of foreign exchange;
- (vi) An adequate legal framework;

8. The existence and effective operation of a "double legal" framework can facilitate the entry of foreign investors in developing countries. There are two sets of legal frameworks. The first is a general set of laws and regulations under which both domestic and foreign investors must operate. The second is a special set of rules applicable to foreign investors.

9. In many developing countries, there cannot be a fully developed national Foreign Investment Law without some form of foreign investors. Such laws usually indicate that foreign investors will be granted the same opportunities and incentives as domestic investors. In addition, a number of the considerations listed below are included.

10. The issue arises: is the establishment of a suitable legal framework including a clear policy statement of rules affecting foreign investors an essential precondition for attracting foreign investment?

3.3. Investment and guarantees

3.3.1. The World Bank's view of some developing countries
is that they are willing that the Government will not
make any legal requirements or if this is proved necessary
to make it national interest (or some similar phrase), adequate
protection to a fair and equitable basis (or some similar phrase)
and that the basic values. I think a sufficient guarantee
is that if the developer it is willing to do so the Government of the country
in which the development is located

3.3.2. The World Bank guarantees have been, during the United
States of America, and a number of European countries, have signed
financial investment guarantee schemes with a number of developing
countries. The issue arises: whether these treaties give effective
rights relating to the foreign investor?

3.3.3. The experience which some businesses in the industrially
advanced countries have attached to bilateral investment insurance
schemes has led to the study of more extensive multilateral schemes.
Nothing is known to details here. An issue of principle can be raised:
whether desirable that further action in this field be conducted on a
multilateral basis?

3.3.4. International guarantee bonds are frequently a pre-
condition of course. Governments of an industrially advanced country
afforded by loans investments made by its own business enterprises in
the relevant developing country. The oldest and largest of these
programmes is operated by the United States of
America and Japan, the Federal Republic of Germany and more recently
Australia and Denmark offer similar programmes. The issue
whether international multilateral programme for these programmes a
multilateral framework is desirable. If so, what action
can be taken to take to ensure that such programmes apply
multilaterally.

3.3.5. The World Bank's background papers show that a majority of the 20
developing countries whose experience has been studied are signatories
to the International Convention for the Settlement of Investment
Disputes. It would suffice therefore if this general scope of

Creating a favourable condition for foreign investment

(iii) A favourable policy on the repatriation of capital and dividends

16. The different types of incentives available to foreign investors in the United Kingdom all aim at increasing the rate of profit on large industrial projects. However, it is increasingly becoming less effective for a foreign investor if he is required to remit only that part of the profits which he & the UK government share in a developing country. It is also considered better for foreign enterprises to charge royalties or other fees for the technical know and management skills made available by the project. The ability to remit these is also important. Finally, some countries will place importance on freedom to remit capital in the event that they wish to liquidate their interest in the project.

17. The Foreign Investment Law of a developing country includes policy statements designed to reassure potential foreign investors on these points. The law must also make it clear whether by themselves effective or does not make it effective to maintain a record of the country on this type of investment in accordance with general balance of payments principles.

(iv) Favourable treatment under international agreements

18. The fact that the profits and other income of a foreign investor are in principle subject to the taxes of both his home country and the developing country raises some special difficulties. The foreign investor must consider the combined effects of local systems when he calculates the effective tax burden on a complicated investment. It is in the interest of the Government of a developing country to take what action it can to overcome any deterrent effects which may result. In particular, the Government needs to ensure that tax concessions provided at the time when are not frustrated when the remitter income is taxed in the home country of the foreign investor.

- the number of developing countries (e.g., Jamaica) and the difficulty of harmonizing tax treatment in the Federal system. In addition, there may be difficulties in the incentive to attract foreign direct investment or tax incentives to those countries, so benefits granted shall not be compromised. However, the situation will be different if developing countries have not paid due attention to this problem. The issue could be the incentive, legal, encouraged policy, investments, and influence of friendly tax arrangements?
2. Who is a skilled person will also be discussed in detail and will be referred to other and more detailed discussions (2).

(a) Potentiality or flowout of foreign personnel

3. The country background paper show that most of the developing countries would have some regulations which affect the employment of foreign personnel in industry, enterprises established by a foreign investor. The general law or criteria. Is a favorable policy for the importation of foreign scientific, technical and medical personnel an acceptable alternative to foreign investment policy?
4. If the advised minimum standards for foreign investor specifies that he employ foreign managers and technicians as he deems appropriate, or does he also recognize that it is in his interest to reward trainee high a proportion of local personnel as possible? Can a government set rigid rules when the technology used varies so greatly from project to project?

5. In developing countries where a system is in operation to control the inflow of foreign exchange, foreign personnel can be adversely affected either by delays or by restrictive general rules designed to limit their utilization in mind. This is expressed under the

- (b) Trade protection, see pages 20 - 21 of United Nations Conference in Economic Cooperation. The whole system could be modified to take account of the development of the economy and the new tax treatment between developed and developing countries, see Annex 13, page 20, 21, 22, 23, 24, 25, 26, 27, 28, 29, 30, 31, 32, 33, 34, 35, 36, 37, 38, 39, 40, 41, 42, 43, 44, 45, 46, 47, 48, 49, 50, 51, 52, 53, 54, 55, 56, 57, 58, 59, 60, 61, 62, 63, 64, 65, 66, 67, 68, 69, 70, 71, 72, 73, 74, 75, 76, 77, 78, 79, 80, 81, 82, 83, 84, 85, 86, 87, 88, 89, 90, 91, 92, 93, 94, 95, 96, 97, 98, 99, 100, 101, 102, 103, 104, 105, 106, 107, 108, 109, 110, 111, 112, 113, 114, 115, 116, 117, 118, 119, 120, 121, 122, 123, 124, 125, 126, 127, 128, 129, 130, 131, 132, 133, 134, 135, 136, 137, 138, 139, 140, 141, 142, 143, 144, 145, 146, 147, 148, 149, 150, 151, 152, 153, 154, 155, 156, 157, 158, 159, 160, 161, 162, 163, 164, 165, 166, 167, 168, 169, 170, 171, 172, 173, 174, 175, 176, 177, 178, 179, 180, 181, 182, 183, 184, 185, 186, 187, 188, 189, 190, 191, 192, 193, 194, 195, 196, 197, 198, 199, 200, 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genuine savings from earnings of foreign enterprises?"

24. The Background Papers show that a number of developing countries grant employment permits for a relatively short period of time (e.g. one year) and require this to be renewed regularly thereafter. The issue arises: can such formalities be a significant factor to foreign investors?

C. What other factors influence the decision of a foreign investor?

25. A number of measures have been considered above which help to facilitate an inflow of foreign investment. Some of them are designed to ensure that the different types of incentive measure considered earlier in the Seminar can be fully effective for the decision of the foreign investor. The issue arises: have these measures by themselves taken into account the factors which induce a foreign investor to invest in a particular country?

26. One could ask points can be made: that is that no mere enactment of liberal legislation will not be effective by itself. Its effectiveness will also depend on the way in which the rules are administered. The issue arises therefore: how much does the past record of fair, speedy and effective administrative action, particularly enacted influences the decision of potential foreign investors?

27. Another general issue which arises is: is stability the only motivating force in the foreign investor's decision? It has been written on this subject. Experience suggests that many of the foreign foreign companies intend to gain a foothold in the country where they see a good potential market in the future and the danger of competing firms obtaining a large share of the market can be accelerated by the introduction of higher tariff or other measures to protect the local market from imports?

28. Foreign investors usually look at the role which the private sector plays in the Nation's industrial development and the Government's attitude towards private investment in general and foreign investment in particular. The issue arises whether is it sufficient for a government to take policy initiatives, favouring private sector development, or does the image of the country and its past record of the economy? Can one event such as the nationalization

and the other may be a serious determining factor whether or not investment is made?

The following points are considered to be of adequate interest to merit discussion. Among the proposed topics, the following are considered to be of particular interest:

- (a) The foreign exchange position, especially when it will never be possible to get a favorable currency for determining the cost of imports.
- (b) The availability of labor.
- (c) The availability of capital.
- (d) The political stability of the country.
- (e) The tax treatment of foreign investors.

III. SUBJECTS FOR DISCUSSION

A wide range of issues have been raised in this paper. In order to make the session devoted to this subject of maximum value, it is suggested that discussion might concentrate on the following subjects:

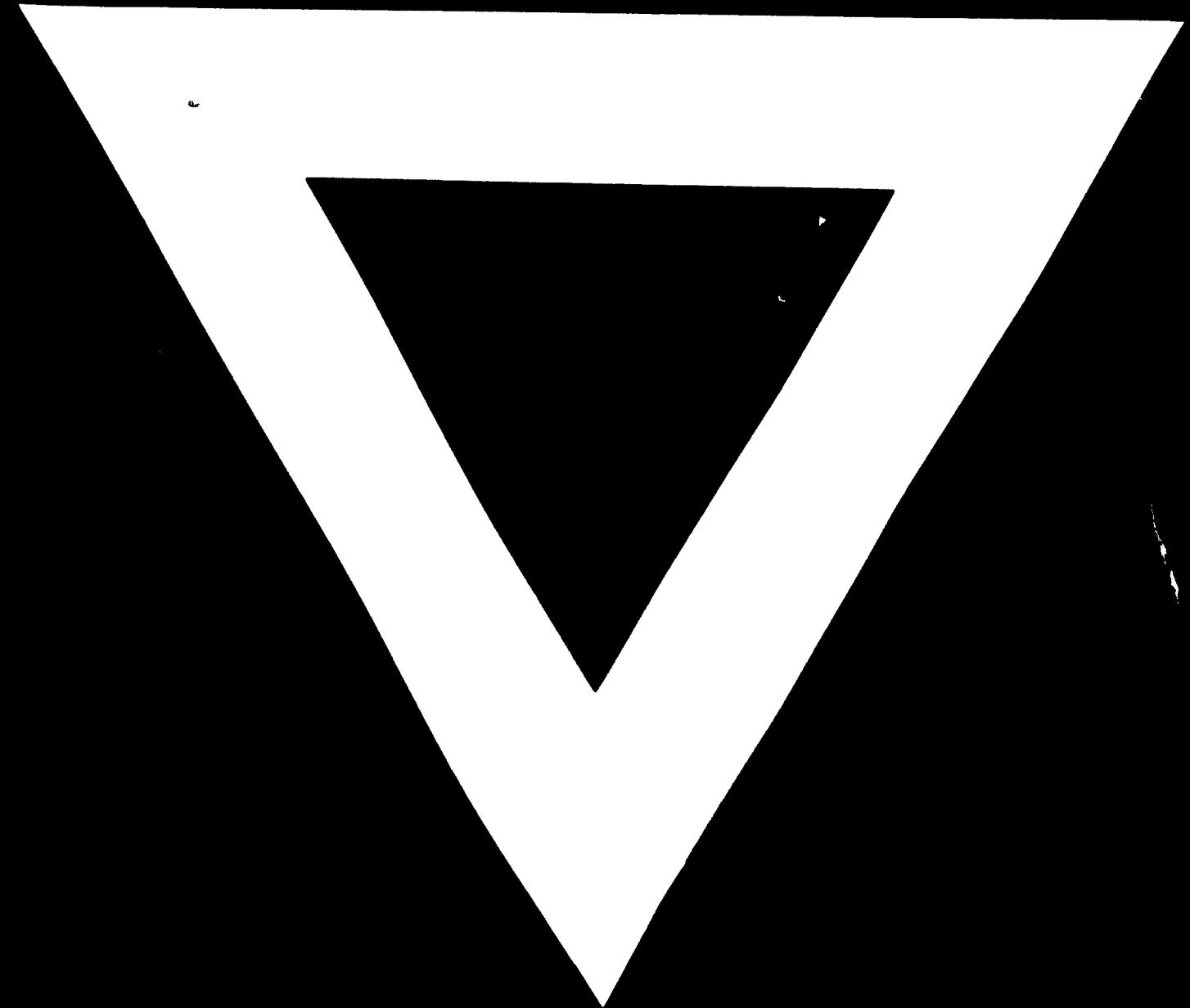
- (1) What are the experiences of countries represented at the meeting? Participants might indicate:
 - (a) What volume of foreign investment has been attracted to the industrial sector in the last five years;
 - (b) What form of foreign investment has taken;
 - (c) What are the major measures taken by the Government to attract foreign investment;
 - (d) Whether their country has a sufficient network of international tax agreements to make such investments effective;

Other specific topics of general interest might be discussed, including:

- (2) Why the incentive legislation of some countries is limited to substantial amounts of foreign investment; without reference to development financial entrepreneurship?

It is asked that never the place be left open on the availability of a foreign investor. If so, how can he be welcomed with one of the following and financed with local funds?

- (g) Are there sound economic reasons for limiting foreign equity participation in most industrial projects to 50% or less? Are there sound business reasons for a foreign investor requiring a majority control of the equity of a local enterprise (i.e., greater than 50%)?
- (h) Are there any other issues in which the interests of the foreign investor and the receiving country may be in conflict? If so, how can they be harmonized?



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