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Foreign Investment in Cuba: 'Sin Prisa, Pero Sin Pausa'

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May 7, 2015

While recent direct negotiations geared at normalizing relations with the U.S. were taking place behind closed doors, Cuba was simultaneously hosting a very open discussion about the adoption of a new Foreign Investment Law (No. 118/2014), which became effective during the summer of 2014.The main purpose of this law is to attract foreign capital, technology and markets in which mutual interests may be pursued. Since the adoption of the law, the Cuban Ministry of Foreign Trade and Investment has promoted what it perceives as the key differentiating factors for investing on the island: the country's legal framework and its tax incentives, the political stability and geographical location in the center of an expanding Caribbean market, the safety for foreign personnel and, most significantly, Cuba's highly qualified workforce.

In an attempt to avoid the organizational problems and social issues that were encountered in the 1990s when Cuba first opened up to foreign investment, the Cuban Ministry of Foreign Trade and Investment created a Foreign Investment Opportunities Portfolio in collaboration with the business departments of each Cuban ministry. The main goal is to help identify areas and projects where investment is sought. Of course, until the U.S. embargo laws are lifted, U.S. investors will not be able to take advantage of the new legal framework and business opportunities unless, and to the extent, they obtain the necessary licenses from the U.S. Office of Foreign Assets Control (OFAC).

The Opportunities Portfolio, which may be developed either in the Special Development Zone of Mariel (a port with its own special regimen and policies, located 45 minutes west of Havana) or in other parts of the country, showcase a variety of possible investments in the following sectors and industries: the agro-food industry, where one of the main priorities is the replacement of imports, particularly food, with local goods; construction; biotechnology and the development and manufacturing of medicines; the sugar industry and its byproducts; renewable energies; packing and packaging; telecommunications; tourism and real estate; and infrastructure investment and industry.

The total value of these proposed investments is nearly $9 billion, but there is the potential for even more investments than those already identified. Legal experts in Cuba emphasize the idea that the opportunities will extend beyond those included in the Opportunities Portfolio, which is supposed to be updated every year.

One of the reasons that these new Cuban investment opportunities could be attractive to foreign investors is that investments in Cuba could provide access to other markets in which the country has strategic alliances, including South America, Africa and Asia. Bearing in mind the relatively small size of the Cuban market, the government is focused on exporting goods that are produced there. Biotech, for example, could be one of the sectors that most benefits from foreign investment expansion into Cuba.

The Legal Framework

The law defines foreign investment as: "[d]irect investment, in which the foreign investor participates as a shareholder in a joint venture or in a totally foreign capital company; or makes contributions to international economic association agreements, thus participating, in an effective manner, in the management of the business" and "[i]nvestments in equities or other securities or bonds, either public or private, which do not fit the definition of direct investment."

Currently the law allows foreign investments in all sectors, except for health and education services and the armed forces. Foreign investors may participate in this process as:

- **A shareholder in a joint venture**—a Cuban commercial company that adopts the form of a corporation with registered shares in which one or more Cuban investors and one or more foreign investors participate as shareholders.
- **A foreign enterprise**—foreign investors can set up in Cuba as individuals acting on their own behalf, a Cuban affiliate of the foreign entity or a branch of a foreign entity.
- **A party to an international economic association agreement**—an agreement between one or more national investors and one or more foreign investors for the realization of activities fitting an international economic association even without forming a new legal entity distinct from that of the parties.

The law also offers protections to foreign investors, promising that such investments will enjoy legal security and may not be expropriated "unless such action is executed for reasons of public or social interest in accordance with the provisions of the Cuban Constitution, the international treaties signed by Cuba on investments and the legislation in force, with appropriate compensation for their commercial value established by mutual agreement and payable in freely convertible currency." This provision does not include any reference to confiscation or nationalization.

The law requires that disputes that arise out of foreign investments be resolved in accordance with the contracts underlying the investments, except in the case of (1) conflicts arising from the inaction of the governing bodies of the legally established entities; or (2) disputes related to the winding-up, dissolution and termination of such entities, which will be resolved in Cuban courts.

Tax Incentives

Tax incentives have been presented as one of the most appealing features of Cuba's new legal framework. The incentives, however, would only be available to foreign investors who become partners in joint ventures or parties to international economic association agreements. Thus, companies that do business in Cuba but are fully owned by foreign capital will not benefit from the following tax exemptions:

- Exemption from personal income taxes for the revenues received from the business dividends or profits.
- Exemption from profit taxes for a period of eight years from the date of the company's incorporation. The tax exemption period also may be extended by the Council of Ministers, which is the highest executive body of power in Cuba.
- Exemption from customs taxes for the import of equipment, machinery and other materials during the investment process.

Additionally, more substantial tax exemptions are offered to those foreign investors considering operating in the Special Development Zone of Mariel (Law Decree 313, Extraordinary Official Gazette No. 23). Companies also should be aware that when a foreign investment venture involves the exploitation of natural resources, whether renewable or not, the Council of Ministers may decide to increase the profit tax rate by up to 50 percent.

Real Estate

One of the most favorable potential investment areas is real estate. Under the law, foreign investments may include the possibility of obtaining ownership of the real estate or other property rights. This aspect has not been highly publicized, but provides that investments in real estate can be directed to housing and buildings, either for private or tourist-related purposes; to housing or the offices of foreign legal entities; or to real estate development for tourist purposes.

For example, foreign banks currently doing business on the island are not allowed to purchase property for their representative offices; they may only lease office space. According to some sources consulted in Cuba, the possibilities for foreign investors to buy property on the island, at the moment, are limited to the construction of golf courses and real estate for housing. Even in the Special Development Zone Mariel, which has a faster approval system, only a surface right is granted for specified terms of up to 50 years, with the possibility of renewal, depending on the characteristics of the business.

Risks for Foreign Investors

Foreign investors interested in doing business in Cuba are paying close attention to two important developments in Cuba and in the U.S.:

1. The potential adoption of a single currency unifying the two currencies currently circulating in Cuba. This measure is largely supported by Cuban economic experts, as it will likely improve the island's economy. The measure is expected to pass in the near future.

2. The anticipated normalization of relations between the U.S. and Cuba, and the potential lifting of the U.S. embargo. Because of the embargo, foreign investors doing business on the island are not allowed to conduct transactions in U.S. dollars.

Non-U.S. foreign entities that do business in Cuba consider violating the U.S. embargo as one of the key risks faced by foreign companies doing business on the island. Therefore, non-U.S. foreign entities doing business on the island should seek legal advice from law firms from their countries of origin, law firms from the U.S. (for assistance with the OFAC regulations) and from Cuban law firms (to establish the company's presence in the Cuban market). Beyond the standard sovereign risk analysis, another risk to be taken into account by investors is the fact that this new legal framework is still very new and, therefore, there is no developed domestic practice for interpreting and enforcing the new provisions of the law.

As investors monitor developments, new regulations could help improve Cuba's business and investment climate as part of the market-oriented changes conceived to update the island's economy. Many wonder if those rules will include a response to the new OFAC regulations issued on January 16 that allow certain U.S. trade and commercial transactions with Cuba. Others speculate that the Cuban government will only show, for now, its attractiveness to U.S. investors as a mechanism to expedite the lifting of the embargo. Only time will tell.

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