Private Investors Abroad– Problems and Solutions in International Business in 1969

Foreign Private Investment in a Developing Nation: An Indonesian Perspective

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Private Investors Abroad—Problems and Solutions in International Business

Foreign Private Investment in a Developing Nation: An Indonesian Perspective

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INTRODUCTION

The subtitle of this article immediately raises a question. What makes an Indonesian perspective on the problem of foreign investment so special? I believe the fact that Indonesia is one of the few countries in the world that has moved full cycle from rejection of foreign private investment to a new acceptance may have some bearing on the general topic. This shift has led to an unusual focus on Indonesia and its economic potentials as the new opening area of investment opportunity.

Starting from 1958, our conflict with the Dutch led the Indonesian Government progressively to seize most of the foreign enterprises on Indonesian soil. The growing emphasis on an anti-imperialist struggle led the Government to recast the economy into what might best be called a "command economy" that was supposed to operate by government fiat, in support of a radical foreign policy that was far beyond our national strength. It eventually led to Indonesia's isolation from the rest of the world, a total breakdown of the economy, and in 1965 to the collapse of the governmental power structure. Out of the ensuing turmoil, a government has emerged that is characterized by sobriety, a sense of realism, and a commitment to the priorities of monetary stabilization and economic development.

THE NEW POLITICAL ORIENTATION

The utopian fervor, the insistence on trying to build an ideal society for Indonesia in hostility to all the rich and powerful countries in the world, and the radical economic nationalism that masked an inflated xenophobia, have now been replaced by a general climate of economic realism and pragmatism, an openness to the outside world, an awareness of the importance of international economic cooperation, and a recognition of the vital role of private enterprise in the improvement of the economy. Hence, a much more positive evaluation of the role private foreign capital could and should play in Indonesia's economic development.

This, of course, does not mean that the basic attitudes that underlie the phenomenon of economic nationalism have all disappeared. The present economic leadership of the country is just as committed to prevent the re-establishment of foreign economic domination, and is no less intent on maintaining control over national resources and economic development and on securing the equality of Indonesia in her economic relations with the outside world. However, this leadership is guided by a realistic understanding of the basic laws of economics and of the dynamics of a modern global economy, and fully realizes the need for the assistance of foreign private capital, skill, and experience for accelerated development. At the same time, it has a much greater confidence in the possibilities of accommodating the sometimes conflicting interests of national development and the operations of private foreign enterprise as profit-making organizations. The return of the foreign enterprises taken over by the former regime to their original owners, and the Foreign Investment Law promulgated in the beginning of 1967, are manifestations of this new, realistic orientation.

Before we go into a brief discussion of the legal aspects of this Foreign Investment Law, it seems that one prior question should be answered—How stable is Indonesia's present political and economic course? The question can be answered in a number of ways. One could point to the firmness of the commitment to economic development priorities of the present leadership, or to the political courage that it has shown in putting through the painful stabilization policies that were called for. One could also point to the organizational as well as the ideological weakness of the oppositional forces in the country. But, to me, the most important factor that should be brought out is the emergence of a new post-independence, post-revolutionary generation into the political arena. It is this generation that has formulated, and is implementing and supporting, the policies that emanate from this new economic orientation. Because the members of this generation have never known the pain and humiliation of colonial subjugation, their outlook on the world is much freer, and their self-confidence more natural. And equally important, this generation is fully familiar with modern science and technology and the possibility of their application to our problems.

Because the new economic realism is a very essential part of the new values that motivate this new generation of leadership, we can now look at the course that Indonesia has taken, both in its own economic and political development, and in its relations with the outside world, as a movement of growth—a growth of which the direction is stable.

Let us now have a look at some of the legal aspects of the Foreign Investment Law.

MAIN ISSUES OF INTEREST TO THE FOREIGN INVESTOR

In deciding whether to initiate investment in a given country after having carefully considered the business

prospects, the prospective investor is concerned, in the first instance, with the safety of his capital and with the availability of protection against a variety of risks, including that of expropriation. A second broad category of issues which he must consider deals with the modes of entry, the organizational structure in which to carry on the venture, and the facilities made available to him for effectively managing his business operations. The third major area of interest concerns the facilities for the repatriation of capital profits and dividends.

I shall discuss the main points concerning these three broad categories of issues, but I think we must recognize that even more important than the specific legal provisions concerning these matters is the so-called investment climate, the state of government and public opinion on the role and the rights of the foreign investor in the host country. Many of the problems will not arise, particularly in the area of security of investment, if the investment climate is a hospitable one. Even if they do arise, it will not be difficult to reach a compromise or to find an interpretation of the laws or regulations that will fit the mutual needs of the parties if there is goodwill on both sides.

Nevertheless, it is important that the legal structure be reasonably adequate to permit the foreign investor to enter and carry forward his enterprise with the confidence that he will not likely encounter serious difficulties, as long as he comports himself in a reasonable manner and with full recognition of the fact that investment is a two-way street.

Security of Investment

The legal safeguards provided by the host country, of course, do not operate in isolation from the safeguards provided by the capital exporting countries, such as investment guarantees, and those provided by the inter-

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national community under both customary international law and international institutions or agreements. The international system may also include bilateral treaties between the host country and the capital-exporting country.

In considering the safeguards provided by the Indonesian legal system, I think you will wish to bear in mind that our commercial code is still fundamentally based on legislation the Netherlands introduced in Indonesia to deal with the problems of so-called Europeans and those assimilated to the European Group for legal purposes. There has been considerable discussion in Indonesia concerning the philosophy underlying our legal system following the abolition of colonialism. For example, there is a current of opinion that holds there should now be only one legal system in Indonesia instead of the dualism that characterized our society in the colonial era, and that the system should be based on adat (customary) law. However, the fact remains that our laws dealing with commercial and financial problems, particularly insofar as they affect foreigners and large-scale ventures, generally are clearly derived from Western models or, at least, have a strong Western component.

Thus, the Agrarian Act of 1960 introduced radical changes in land law, including unification of the law and the elimination of the dualism that had differentiated between land rights in the Western sphere and land rights in the customary law sphere. While the new agrarian act is purportedly based on customary law, it is, in fact, thoroughly modernized by the introduction of Western concepts such as titles in land ownership, the distinction between real and personal rights, and a system of compulsory registration, which will ultimately be applied to non-Western as well as Western-held land. The law also restricts the right of absolute ownership of land to Indonesian citizens.

The derivation of our commercial law from Western models is undoubtedly reassuring to potential foreign investors, since it is easier for them to understand and to feel comfortable with a legal system that is familiar to them.

Returning to the problem of security of investment, you will find that our system provides for two basic safeguards on which investors tend to rely, namely laws governing the circumstances under which expropriation may be carried out and the right of access to an independent judiciary.

The Foreign Capital Investment Law (Law No. 1 of 1967, dated January 10, 1967) sets out the broad framework of conditions under which foreign investment is welcomed and protected in Indonesia. It covers the other two broad categories I have mentioned (i.e., facility of entry and management, and repatriation of capital and profits), as well as that of security of investment. The latter is specifically provided for in Chapter VIII, Articles 21 and 22. Article 21 stipulates that

> "the Government will not carry out comprehensive nationalization/revocation of ownership rights of the foreign capital enterprises nor take steps to lessen the right to control and/or manage the enterprises concerned, except if it is declared by law that the interests of the State require such a step."

This means that an Act of Parliament is required before such nationalization can be undertaken.

It may be useful to know that the Indonesian law also contains extensive provisions concerning expropriation which are applicable in the event of isolated or individual takings, as contrasted with the comprehensive measures envisaged in the passage quoted.

The law to which I refer is known as the Expropriation Ordinance of 1920 (Official Gazette 1920 No. 574), enacted, of course, under the colonial administration. Like other Western laws of a similar character, it is appli-

cable to the usual cases where the right of eminent domain is to be exercised, as where a local plot of land is condemned by the government for purposes of constructing a highway or other public works.

Reverting to the provisions of Article 21, it should be noted that comprehensive nationalization is not to be undertaken unless it is in the interests of the state, that is, it is not to be undertaken as a punitive measure or on some other arbitrary basis.

Article 22 of the law then stipulates a series of further safeguards, namely, that the government is obligated to provide compensation, either on the basis of an agreement which is in accord with applicable principles of international law, or, if no such agreement is reached, then by means of a binding form of arbitration. It is further stipulated that the arbitration committee will consist of three persons, one selected by the Government, one by the foreign investor, and an impartial arbitrator to be chosen jointly by the two parties.

It is also possible to stipulate further provisions in the arrangements between the Government and the foreign investor concerning the procedures to govern such arbitrations, such as the method of selecting the third arbitrator in case of a deadlock. In particular, since the Indonesian Government has become a party to the World Bank-sponsored Convention on the Settlement of Investment Disputes between States and Nationals of Other States, it would be possible to stipulate that the arbitration should take place under the terms of this Convention.

In the event that the taking of property should be carried out under the general laws concerning eminent domain, any dispute would be determined in the Indonesian courts, subject, of course, to any further redress that may be available under customary international law or under treaties.

As you are all aware, an additional safeguard is avail-

able to foreign investors under the United States Investment Guaranty Program, which provides guarantees both against specific risks (inconvertibility, expropriation, and war, revolution, or insurrection) and against extended risks (various risks of a commercial character). My government entered into an exchange of notes with the United States Government that enabled this program to go into effect, and has approved the application of this program to many ventures.

Facility of Entry and Establishment of Legal Entity

The Foreign Capital Investment Law specifically governs the issues concerning entry, the establishment of a foreign entity, operation and management, and incentives for investment. It provides ample latitude for foreign investors to enter and operate without great difficulty.

The effect of the new law is to open most fields of business activity to foreign capital. The only fields of investment which are completely closed to foreign capital are those which fulfill a vital function in national defense (Article 6(2)). Other fields to which access is restricted, but may nevertheless be entered provided that the foreign investor does not exercise full control, are referred to in Article 6(1). These are fields of vital importance to the country, such as harbors, public utilities, atomic energy, and mass media. Indonesian control adequate to permit foreign investment might be achieved in these areas, not only by permitting local capital participation but also by such means as government supervision over the quality and cost of service, or by the so-called sale-and-lease-back arrangement, under which ownership of the venture is turned over to the government, which then leases the property to the foreign investor, as in the case of the I.T. & T. investment in telecommunication.

Investment is envisaged as taking the form of equity participation, at least in order to qualify for the inducements offered under the 1967 law (Article 1).

The period of time during which a permit under the foreign investment law is valid is not to exceed thirty years (Article 18). However, the government would commit itself to a discussion of the practices to govern operations beyond the first thirty years within two years of the end of the first thirty-year period. Furthermore, the government is also prepared to renew the thirty-year period at periodic intervals, provided that certain standards established by the government have been met, such as additional input of capital and the Indonesianization of personnel and capital. This kind of telescoping arrangement makes it possible for a company to obtain a longer period and thus continue to have before it a full period of thirty years of assured eligibility.

Article 3 of this law stipulates that an enterprise that carries on most of its operations in Indonesia should be a legal entity established under Indonesian law and be domiciled in Indonesia.

Article 4 provides that the government may stipulate the areas in which foreign capital enterprise are to operate.

Management

Under Chapter IV, Articles 9–13, the foreign investor is granted full authority to appoint the management of enterprises in which his capital is invested, and in particular to use foreign managerial and technical employees for positions that cannot yet be filled by Indonesian personnel. Other employees are to be recruited from among Indonesian citizens, and the foreign investors are obligated to organize facilities for the training and education of Indonesian citizens, within and outside the country, with a view to gradually replacing foreign employees with Indonesian citizens. However, the law

and the implementing regulations do not as yet specify requirements lying between, on the one hand, the investor's full right to appoint the management of his enterprise, and, on the other hand, his obligation to recruit Indonesian personnel. With more experience, quantitative criteria may be applied either by regulations covering particular fields of activity or as part of investment agreements with the Government.

Land

Article 14 provides that foreign capital enterprises are granted the following rights with respect to land: the right of construction, the right of exploitation, and the right of use. Under the Agrarian Law, mentioned above, the absolute ownership of land is not enjoyed by foreigners. The provisions in the Foreign Capital Investment Law represented a new concession, since the rights thereby granted were not previously available to foreigners. The explanatory notes on Article 14 of the Foreign Capital Investment Law state that the rights granted are in accordance with the provisions of the Agrarian Law, that construction rights are granted for a maximum of thirty years, subject to extension for an additional twenty years, that exploitation rights are granted for a maximum of twenty-five years (in the case of certain crops, for thirty years), subject in both cases to the right of extension for another twenty-five years.

Facilities and Incentives

I need not emphasize that the new law has been designed to attract foreign capital to Indonesia for investment in projects which will contribute to the healthy development of the Indonesian economy. Accordingly, it offers a combination of incentives and accommodations that can stand comparison with those offered by other developing nations.

Part of the approach taken to attract new projects is to offer specific incentives, consisting of the following:

(1) exemption from tax on corporate profits for a period of up to five years, and exemption from the dividend tax on profits during those years;

(2) full authority to select management and to recruit or use foreign technicians and experts for positions that Indonesian manpower is not yet capable of filling;

(3) the offer of land at advantageous terms, carrying with it rights of building and exploitation formerly denied to foreign business enterprises;

(4) exemption from import duties for equipment, machinery, tools, and initial plant supplies; and

(5) exemption from the capital stamp tax on the introduction of foreign capital for investment.

In addition, the Ministry of Finance is granting duty-free privileges for the importation of raw materials for the first two years of operation. Also, expatriate workers are granted free import duty for food parcels up to $100 per month.

Furthermore, the law gives the government the discretion to grant additional benefits by reduction of the corporate tax rate to a rate that may be anywhere from 50 percent down to zero for a period not exceeding five years after the initial tax holiday period, by permitting the investor to offset losses during the exemption period against profits in any ensuing year for tax purposes, by allowing accelerated depreciation, and in other ways deemed desirable and appropriate (especially for large projects of great importance to the economy).

Facility for Withdrawal of Capital and Profits

Article 19 specifies that the foreign investor is granted the right to transfer capital in its original currency at

investment that may increase foreign exchange earnings, such as mining, agricultural exports, etc.; (2) investment that makes possible import substitutions; and (3) investment that, while not directly affecting the volume of foreign exchange, nevertheless is of a quick-yielding character, increases employment opportunities, introduces new technology, or brings in modern equipment. These directives also spell out in greater detail the provisions concerning relief from taxation, transfer of profits, and dividends, and capital repatriation.

It should be borne in mind that there are also laws relating to specific fields of investment, and that a number of ministries have issued policy statements outlining the terms and conditions under which foreign investment may enter and the specific opportunities for foreign investment. With respect to these matters, I think it should be noted here that mining and petroleum undertakings are open for investment only under so-called contracts of work. This is based on the fact that the ownership of these resources is specifically reserved to the state so that investment is permitted only under the conception that the investor acts as the agent of the government in carrying on his operations. Nevertheless the contractor is given full responsibility for conducting all stages of operation, including the marketing of products for, and on behalf of, the government.

Participation of Domestic Capital

Another point of considerable importance to Indonesia is the encouragement the law gives to include domestic capital in the financial plans of new ventures organized by foreign capital. Domestic participation is not required as a condition of entry for foreign investors, but it gives the foreigner some legal advantages. For example, if a venture originally organized entirely by foreign capital does offer its shares to Indonesian participants at a later date, the proceeds of sale may be trans-

ferred back into the original currency of the investment, as if the proceeds of the sale were earnings or other funds eligible for transfer under other provisions of the law. In addition, in enterprises in which foreign capital participates with local capital, the benefits of the foreign investment law otherwise held out for foreign capital will be available, on a proportionate basis, to the investors who enter into joint investment undertakings with Indonesians.

The effort to create a place for local capital has resulted in a policy of not permitting the full tax holiday of the foreign investment law to any investment of less than $2.5 million unless provision is made for local capital participation in the venture. Applications for permits to invest under the law that include participation by Indonesian capital receive priority consideration, and other advantages may well be created in the future.

CURRENT INVESTMENTS

Although the new investment law has been in effect for a relatively short period (almost two and one-half years in June 1969), the response of foreign investors to Indonesia's invitation to invest in that country has been encouraging. A large number of United States, European, Japanese, Australian, and other companies have accepted the challenge and have started with their operations to assist Indonesia to build up the country. Some twenty foreign oil companies, including major oil companies of the United States, have concluded exploration and production contracts. It is estimated that by 1970 when these new contracts will have begun to show results, the total oil output should reach about one million barrels a day, as compared with 520,000 barrels a day in 1967. In the field of mining, five large companies are prepared to invest for the exploitation of copper, nickel, tin, and bauxite. Twenty-five companies are working in the field of forestry, and fifty-five in the manufacturing sector.

As of the first quarter of 1969, 129 proposals from foreign investors had received the approval of the Government, representing a projected capital investment of $570 million, including $236 million for mining (petroleum excluded), $99 million for forestry, and $86 million for manufacturing. United States investment accounts for 45 percent of total projected investment ($273 million): Eleven companies are operating in the field of manufacturing, with an investment outlay of $26.7 million; three in the field of mining, with an investment of $229.5 million; two companies in forestry with $3.3 million, and nine others in various fields with an outlay of $14 million, making a total of twenty-five companies. This does not include the foreign bank branches and oil companies. Countries following the United States lead are: Canada, South Korea, the Netherlands, Japan, and others. It may also be interesting to note that out of the 129 ventures, eighty-three of those ventures are in the form of joint enterprises, forty-one are straight investments, and five are operating on the basis of contract-of-work.

It may be interesting to note that, according to a recent statement by A.I.D. to one of the Congressional Subcommittees, eighty-five preliminary guarantee applications have been made to date by American investors under the A.I.D. investment guarantees program. These cover a wide variety of industrial interests, particularly in the extractive industries. Smaller private United States ventures are being planned in such labor-intensive industries as electronics assembly and pharmaceutical manufacture, while other United States investors are interested in lumber production and land development. Four major United States commercial banks have opened branches in Djakarta. Thus far, A.I.D. has issued eighteen specific risk guarantees valued at almost $83 million and one extended risk guarantee ($4 million).

A.I.D. will begin in fiscal year 1970 a geological survey

project under which a team from the U.S. Geological Survey will help train Indonesian geologists to chart mineral resources throughout the country, an important prerequisite to effective development of Indonesia's natural resources by domestic and foreign investors alike.

We realize that foreign aid, foreign technical assistance, and foreign private investment by themselves can never make a viable economy in a country, but their role in a period of recovery can be crucial. Foreign investment is therefore expected to play an important role in the implementation of Indonesia's Five Year Development Plan, which was started in April this year. This Five Year Plan gives priority to (1) agriculture, particularly food production; (2) the development of mining and encouragement of industries that produce equipment and inputs for the agricultural sector and the processing of agricultural products; (3) the strengthening of infrastructures, particularly transport and communication. The main objective of the plan is a simple one, namely to raise the standard of living for a future growth by way of food and clothing, improvement of infrastructure, provision of better housing, and an increase of employment opportunities. In this plan, emphasis is also given to rural and regional development.

This Five Year Plan will also provide the context within which the government-to-government aid to Indonesia provided by the Inter-Governmental Group on Indonesia, which includes the United States, Japan, the Netherlands, Germany, Australia, France, the United Kingdom, Italy, and Belgium, will be coordinated. The consultations on which Indonesia's aid requirements are determined within the IGGI are based on assessments by the World Bank and the International Monetary Fund. In addition, the IMF has been most active in advising the Government on monetary and fiscal affairs while the Bank is assisting Indonesia in planning development programs and preparing capital projects.

TRANSITION AND EVOLUTION

Indonesia is a latecomer among the developing countries in dealing with foreign investment. We are still in a transitional period, and are still in the process of gaining the experience needed to guide us further in the area of codification and regulation. That part of our legal system that concerns modern economic activities of both domestic and foreign origin is, therefore, still in the process of readjustment and evolution. This process of adaptation to developmental goals is not only a theoretical one, but necessarily evolves in response to new problems and new experiences. We will also have to keep under constant review other laws that have a bearing on the general investment and business climate. At present, this is the case, for instance, with Indonesian corporation law. With technical assistance from the International Monetary Fund, we are in the process of reforming our tax laws. Besides this, the agrarian law and the labor law will at some point have to be related more closely to our developmental goals.

Corporation Lawyers: Role and Style

While generally no American corporation makes a move without consulting its lawyers, the role Indonesian lawyers play in the activities of our business corporations is much less pronounced. The heavy reliance on legal counsel by American corporations is related to the importance of litigation and judicial procedures in the resolution of conflict in this country. In Indonesia, such conflicts are most of the time resolved through administrative procedures and adjustments. This is, of course, not characteristic of Indonesia alone. It applies also to many European countries.

This difference in role may be one of the reasons why many Indonesian administrators are often somewhat

puzzled when, in the course of negotiations, they are faced with elaborate stipulations raised by legal counsel of American corporations in anticipation of contingencies that might arise in the future. In part, this puzzlement stems from their unfamiliarity with the role legal counsel plays in the activities of business corporations in the United States. In part, this may be the result of an important difference in societal setting. American business and legal counsel are used to operating in a society that has been stable for quite some time, and there is therefore a considerable degree of predictability of future responses and implications, once a particular course of action is decided upon. Lately, some doubts have arisen about this purported stability and predictability, but that is beside the point.

The attitudes that have been shaped by this condition still persist. Indonesian people, on the other hand, are trying to build toward stability. They are working from a situation in which the horizon of visibility and predictability is still limited, though clearly expanding. And though these officials may be able to see the validity of the points raised, they are quite often not in a position to answer. Why? Not because they are lacking in goodwill or because they are technically incompetent, but often simply because no one can entirely foresee the broader setting that will eventually develop—partially thanks to the operations of foreign enterprises—in which these problems will have to be answered. Any assurances given at this stage are bound to have only limited validity. Also, no government can afford to prejudice its future policy options by making premature commitments on the basis of hypothetical situations.

But even more important in this connection may be the differences in attitude that center around the concept of "good faith" in Indonesian commercial law. The central position of this concept in Indonesia has led to a lesser concern with protective clauses spelled out for

specific contingencies than is the case in the American tradition.

An understanding of these differences may make it easier for an American lawyer to communicate while negotiating in Indonesia. Conversely, a greater familiarity on the part of Indonesian government officials, businessmen, and lawyers with American practices and the special role of legal counsel in business activities would be helpful too.

It should also be realized, however, that in the evolution of the Indonesian commercial legal system, adaptations will have to be made that will enable it to bridge differences not only with the American legal system and its practices, but also with those of other countries, like Japan, Australia and Western and Eastern Europe, each with its own legal culture. The tendency of some American lawyers to try to impose on us American legal concepts with regard to such issues as corporate laws and tax laws, seems to us sometimes rather excessively one-sided. Often, we are faced with demands for contractual guarantees as regards taxation, foreign exchange regulations, and so forth, for the entire duration of the contract. There have been cases where we have indeed compromised on these points, as for instance in the case of certain mining contracts covering large investments. But it should be realized that the insistence on such waivers undermines the strength of the legal system as a whole, including the protection of foreign investment in general.

This would obviously be against the long-run interests of foreign investors. For example, some of the waivers requested involved bypassing the foreign exchange system, which was developed in cooperation with the International Monetary Fund as an integral element of our economic stabilization program. It seems to us that the interests of foreign investors would not in the long run be served by weakening that mechanism. We sometimes

even find ourselves in the ironic position of having to explain to prospective American investors the reasons why we object to the suspension of the operation of market forces, and why we consider it important to keep competition open when excessive protective measures are insisted upon. In order to meet this kind of problem more adequately, we have asked the World Bank to help us develop optimal criteria for both the investors and for Indonesia, which could be generally applied in this connection. All this, I hope, will explain why we take the position that would-be investors should accept both the existing legal framework and the way in which it will develop in the future.

The long-range protection for foreign private capital lies in the *stability* of a favorable business and investment climate. This is only possible if, as in Indonesia, the incentives and accommodations of foreign investment are also made available on a nondiscriminating basis to domestic investors. In fact, the rapid development of national businesses should be seen as directly in the interest of foreign investment as well.

FOREIGN INVESTMENT AND THE POLITICAL CLIMATE

The stability and continuity of a political climate that is favorable to foreign investment will very much depend on the willingness and the capability of foreign enterprises to develop linkages with the environment in which they operate, with the business community, the universities and other teaching institutions, as well as with the intellectual community in general. By involving local business in some of the spin-off activities of these enterprises, through technical assistance, through the utilization of local raw materials, the stimulation of local servicing facilities and of manufacturing of components and spare parts, through making available staff mem-

bers for teaching purposes in order to accelerate the transfer of technology, organizational, and managerial skills at all levels, and by taking an interest in the development of small and medium-sized indigenous business firms in their localities, the foreign companies could very well become a catalytic and accelerating factor in the development of the society in which they operate.

The positive contribution that foreign business could make, not only to economic development, but to a healthy political growth as well, without in any way assuming a political role, should therefore not be underestimated. I think it is quite possible for private foreign business to play this role without endangering its primary role as a profit-making organization. In this manner, foreign private business will avoid the danger of becoming an alien enclave in a stagnant and increasingly hostile environment. In this kind of integration with the patterns of national development, its best protection lies.

If foreign investment comes to be seen by a majority of the political public as insensitive to national aspirations, as an obstacle to national development, or as an alien element pursuing ends that are contrary to the national interest, political pressures against the purely legal safeguards are bound to develop. It is of the greatest importance that private foreign business operating in an underdeveloped country should develop the capacity to identify with the developmental goals of the nation, and develop such forms of cooperative endeavor with national business that it is regarded as an ally, an accelerator, and a catalyst of national development whose continued presence is beyond doubt in the national interest as well.

Ultimately, the protection of foreign private investment lies in the rapid development of an indigenous commercial and entrepreneurial middle class and the development of a community of business interests between them and foreign enterprises in their country. Any

contribution private foreign business could make to that end would provide additional long-range security for its investment.

FOREIGN INVESTMENT IN THE GLOBAL SETTING

There is, however, an even wider setting, almost within the same time span, within which the security of private foreign investment in developing countries inevitably will have to be considered as well. The determinants here are the population explosion, the question of international poverty, and the need for generalizing economic development throughout the world.

It is, of course, a truism to state that the world is becoming increasingly interdependent. There are few economic or political decisions, taken in the national context, that will not evoke international repercussions, and vice versa. The world is also rapidly becoming smaller and more and more crowded. The world population is expected to double in the next thirty years. The increasingly uneven density of population in various parts of the world, on top of widening inequalities in the distribution of wealth, is bound to create important shifts in the balance of forces, as well as tremendous tensions in the world during the coming decades. But before everything else, if civilized life is to be maintained, mankind must be able to answer the very elementary questions of how are we going to feed that population; how to produce enough to clothe them and to meet other essential material needs the world over. The rapid population increase, especially in the poor nations, will therefore have to be met by an increased economic production capability and, especially, by a much more extensive involvement of the poor nations themselves in those productive processes.

If we—that is, mankind as a whole—fail to organize ourselves for this purpose, the tensions that inevitably

will develop in the poor nations will destroy the possibility of their evolution towards increasingly open societies capable of rational and creative relationships with the outside world. In this way, the international order itself, including the security of the rich nations, will be in danger. Our capacity to organize ourselves for this task will very much determine the shape and the quality of our life by the time we enter the twenty-first century, if we ever reach that point. This however will require a major redirection of world resources and the striking of a new balance—globally—between expenditure for armaments, and for the combatting of domestic and international poverty. For this, a reassertion is needed of the political will to bring about such a reorganization of global priorities and such a redirection of world resources.

The search that is now taking place the world over for those forms and methods that would be most advantageous to promote the transfer of private capital, skill, and managerial capability from the developed countries to the new nations, is a crucial one. The experience of the first United Nations Development Decade has shown that unless there is such a greater flow of capital throughout the world, especially of private capital to the developing countries, there is little prospect of an adequate response to this problem. One can only hope that private business the world over can develop the capacity, the ingenuity—over and beyond short-term considerations of profit—to develop the forms and modalities that will make such an expanded role possible as well as profitable. After all, business corporations are the natural repositories of the technology, the skills, the organizational and managerial capacity for this very task.

It is equally true that an increased application of private capital to generate worldwide development will by itself not be sufficient. Unless the flow of government-

to-government developmental funds in the form of foreign aid is continued at adequate levels for some time, there is no prospect that infrastructure development in a number of new nations can proceed sufficiently so as to enable private capital to play its productive and socially creative role. Much will also depend on our conceptual and operational capability to move in this direction. We need to develop a more adequate and consistent system of rights and responsibilities, of incentives, safeguards, and guarantees of various kinds on the side of the developed, as well as of the poor, nations. We will have to search for more adequate forms and methods that can facilitate in a substantial way the transfer of capital and other resources. The scope and the capabilities of existing multilateral development agencies like the World Bank, and regional development banks as well, will have to be reexamined in this connection. Likewise, it will be necessary to reexamine the access of underdeveloped countries to international capital and bond markets, and the development of an internationally coherent tax system related to international development needs. Attention should also be given to the role that international corporations are increasingly playing in internationalizing development. The extra-national character of the decision centers of these companies poses important problems, and, in the words of Philip de Seynes, United Nations Under Secretary General for Economic and Social Affairs, calls for the development of a new system of international law with greater economic content.

It may not be possible for the profit motive alone to bring about the substantially stepped-up role of private capital sufficiently to deal with the population explosion and the problems of poverty that may tear the world apart. What may be needed as well is a clearer understanding of the magnitude and the urgency of the problems that the whole of mankind will have to face twenty

to thirty years from now, and a clearer vision of the kind of world in which we *do* want to live. I think it is important for all of us, in discussing problems connected with the security of foreign investment and the legal safeguards for the protection of foreign investment in developing countries, that we do so with a full awareness of the magnitude and the urgency of the role that has to be played by private capital, and the urgency for private capital and the governments of the developed, as well as the underdeveloped, countries together to create the conditions to make this possible, if we are to come to grips with the problems that will determine the total global environment in which all of us, including private capital, will have to live in the relatively near future.

Being myself totally innocent of a training in law, I will not presume to give you a breakdown of the challenges posed to those in the legal profession who are involved in the activities of business corporations. These challenges certainly go far beyond the legal aspects of foreign investment problems in the time frame of the present. Still, it is from this perspective that I invite you to look at the problem of investing in a developing nation.