

# CAT ON A HOT TIN ROOF: THE STATUS OF CURRENT FOREIGN INVESTORS IN A POST-TRANSITION CUBA

Matias F. Travieso-Diaz and Armando A. Musa

One of the most important means within the control of Cuba's current government to obtain foreign capital is to promote foreign direct investment ("FDI") in the country. Even though firmly adhering to a socialist political and economic framework, Cuba has taken a series of measures in the last decade to promote FDI as a way to cope with the economic difficulties that have afflicted the country since the disappearance of the Socialist bloc.<sup>1</sup>

Cuba's efforts to attract foreign investment have resulted in the inflow of substantial amounts of foreign capital by way of FDI. In the event of a political and economic transition in Cuba from a socialist regime to a free-market society, these investments may come under attack by a successor Cuban government as well as from private parties in Cuba and abroad. This paper analyzes the future risks that current investors in Cuba may face under a non-socialist government

and the extent to which the provisions of Cuban law (both current and future) may determine the outcome of challenges to the rights of these current investors.

## FOREIGN INVESTMENT IN CUBA AFTER REVOLUTION

A significant amount of foreign investment, largely by U.S. nationals, was in place in Cuba at the time of the triumph of the Cuban Revolution in 1959. During the 1959-63 time period, Cuba expropriated the assets of foreign nationals in the country.<sup>2</sup> After the expropriations of the early years of the Revolution, foreign investment disappeared from Cuba for three decades. In August 1992, in an effort to foster foreign investment, Cuba amended its Constitution to make important changes to the property regime, including an express authorization for foreign investors

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1. Cuba's need to attract FDI is a direct consequence of the disappearance of Socialism in Eastern Europe. Prior to 1990, Cuba depended on the Socialist bloc (mainly the Soviet Union) for over 80% of exports and imports, and for the financing of the economy through loans and subsidies. The demise of the Socialist bloc had a catastrophic impact on Cuba, which suddenly lost its markets, its sources of supply, and its credit and financing mechanisms. Banco Central de Cuba, *Cuban Economy in the Special Period 1990-2000* (hereinafter "Special Period") at 7-8.

2. The history of the expropriation process is described in detail in Michael W. Gordon, *The Cuban Nationalizations: The Demise of Property Rights in Cuba* 69-108 (1975) (hereinafter "The Cuban Nationalizations"). For a more detailed discussion of the expropriation claims issue, see Matias Travieso-Diaz, *The Laws and Legal System of a Free-Market Cuba* (hereinafter "Laws and Legal System"), Quorum Books, 1997, Chapter 4. The expropriations led to the submittal of claims by the affected parties before their respective governments. In the United States, a federal agency known as the Federal Claims Settlement Commission ("FCSC") received evidence of, and assessed claims by, thousands of U.S. nationals whose properties in Cuba were confiscated. The FCSC certified 5,911 claims with a total value of \$1.8 billion in 1960 dollars. Investments by nationals of other countries amounted to \$350 million by Spanish nationals and approximately \$10 million each for nationals of France, Canada and Switzerland. Michael W. Gordon, *The Settlement of Claims for Expropriated Foreign Private Property Between Cuba and Foreign Nations other than the United States*, 5 Law. Am. 457 (1973).

to own property and be able to convey it to the state or to third parties.<sup>3</sup>

Another important step towards the development of a foreign investment regime took place on September 5, 1995, when Cuba's National Assembly approved the Foreign Investment Law, Law No. 77 of 1995 ("Law 77").<sup>4</sup> A number of the changes instituted by Law 77 represented steps forward that liberalized somewhat the investment regime in the country. Law 77 defined three permissible types of foreign investment: joint ventures ("*empresas mixtas*"), international economic associations, and companies with totally foreign capital.<sup>5</sup> On December 6, 2000 the Executive Committee of Cuba's Council of Ministers officially recognized two new forms of FDI: production contracts ("*contratos de producción cooperada de bienes o la prestación de servicios*") and management contracts ("*contratos de administración productiva*").<sup>6</sup>

A joint venture is a legal entity consisting of one or more Cuban parties and one or more foreign investors. The contributions of each participant and the breakdown in stock ownership are agreed upon before governmental approval is granted, and are reflected in the joint venture agreement and the decree approving the joint venture. The Cuban party generally supplies real estate and labor, while the foreign investor provides capital, technical resources, and know-how (both technical and managerial). The

joint venture is legally independent from the investing entities, and must register with the Cuban Chamber of Commerce to attain official status.<sup>7</sup> Profits earned by the joint venture are distributed to the investors according to their respective ownership share.

The formation of international economic associations ("IEAs") does not require the establishment of a legal entity separate from the contracting investors. IEAs are normally established because the contracting parties can meet a common objective through cooperation. Each party agrees to make specific contributions to the IEA, but no capital is set aside. The parties must, however, agree to a profit sharing arrangement and a tax payment plan. The two most common forms of IEAs are production contracts and management contracts (the two forms of FDI formally sanctioned by the Cuban government in December 2000).

All modalities of foreign investment in Cuba could potentially be subject to adverse action following a political transition in the country. However, joint ventures are the investment mechanisms most exposed to such actions because in joint ventures the foreign investor often develops facilities or otherwise spends money directly in the country and is thus more vulnerable to adverse governmental or private action.

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3. *Constitución de la República de Cuba* (1992), Gaceta Oficial (Aug. 1, 1992) (hereinafter "1992 Constitution.") Art. 23 of the 1992 Constitution states: "El Estado reconoce la propiedad de las empresas mixtas, sociedades y asociaciones económicas que se constituyen conforme a la Ley. El uso, disfrute y disposición de los bienes pertenecientes al patrimonio de las entidades anteriores se rigen por lo establecido en la Ley y los tratados, así como por los estatutos y reglamentos propios por los que se gobiernan."

4. *Ley Número 77 de la Inversión Extranjera*, Gaceta Oficial, September 6, 1995. For an online English translation of Law 77, see <http://www.latintrade.com/newsite/content/cprofiles/data-ext.cfm?d=2001&c=9>.

5. Law 77, Art. 12.

6. Acuerdo No. 3827 (December 6, 2000), Executive Committee, Cuban Council of Ministers, Foreign Trade No. 4/2001 (Havana, April 2001): Cuba (hereinafter "Foreign Trade") at 43-44. These forms of "investment" are not altogether new, since a number of joint ventures have in the past included this type of activity. (For example, in the tourism sector, many of the "joint ventures" have been in fact management contracts in which the foreign participant has provided mainly management know-how and has become responsible for managing the operations of the tourist facility.) See Joan Marsan, *Cuba Now or Later, Hotels* (November 1999), available online at <http://www.hotelsmag.com/1199/1199cuba.html>. According to the decree that legitimized these forms of investment, they were officially endorsed because they were shown in practice to provide "favorable economic results for each of the contracting parties," thus meriting legal recognition." Foreign Trade at 43.

7. Resolution No. 26 of the Cuban Chamber of Commerce, issued on December 5, 1995, created a Registry of enterprises with foreign participation. Being listed in that Registry is a prerequisite to doing business in Cuba. Resolución No. 26—Reglamento del Registro de Inversiones Extranjeras, Cámara de Comercio de la República de Cuba, *Gaceta Oficial* (Dec. 15, 1995), p. 504-506.

As will be further discussed below, Law 77 contains express guarantees against the uncompensated expropriation of the property of foreign investors, and commits the state to protect investors from claims by third parties founded on the expropriation of their assets by Cuba, in the event those claims are upheld by the Cuban courts.<sup>8</sup> The compensation to be paid under these provisions is to be in freely convertible currency, although the amount and terms of payment are left to negotiation by the parties or, in case of disputes, by an experienced international organization chosen jointly by the investor and the MINVEC.<sup>9</sup>

In another effort to provide assurances of legal protection to foreign investors, Cuba has signed over 60 bilateral investment agreements (“BITs”) with other countries.<sup>10</sup> The BITs, which are intended to protect and promote foreign investment, address four main topics: (1) conditions for the approval of foreign investments, (2) state treatment of foreign investors, (3) expropriation, and (4) resolution of disputes be-

tween the foreign investor and the host country. The BITs that Cuba has negotiated generally follow the international norms and standards for such agreements.

### CURRENT STATUS OF FOREIGN INVESTMENT<sup>11</sup>

A total of approximately 540 enterprises with foreign participation have been established in Cuba.<sup>12</sup> Starting in 2001, however, both the total number of new ventures and the total amount of new foreign investment have declined precipitously.<sup>13</sup> Currently, well under 400 remain in operation.<sup>14</sup>

As of 2002, Spain had the largest number of investors (104); Canada followed with 70; Italy was next with 57; and 18 enterprises had French investors.<sup>15</sup> Of the then existing enterprises, 83 were involved in basic industry, 75 were in tourism, and 40 were in construction.<sup>16</sup>

The amount of FDI in Cuba is relatively small, particularly in comparison to foreign investment in other countries in Central America and the Caribbean.<sup>17</sup>

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8. Law 77, Art. 3, 5.

9. Law 77, Art. 3.

10. *Foreign Investment in Cuba*, Centro de Promocion de Inversiones, MINVEC, January 2002, available at [http://www.wdsweb.com/cuba2002/ppt/senti\\_Fri.ppt](http://www.wdsweb.com/cuba2002/ppt/senti_Fri.ppt) (hereinafter “Foreign Investment”); see also, Cuban Embassy in Syria, *La Inversion Extranjera*, available online at <http://www.embacubasiria.com/a000031s.html>. For a detailed discussion of Cuba’s BITs, see Matias F. Travieso-Diaz and Jorge Pérez-López, *The Contribution of BITs to Cuba’s Foreign Investment Program*, 32 *Georgetown L. & Pol. Int’l Bus. J.* 529 (2001) (“Cuba’s BITs”). Capital-exporting countries negotiate BITs to protect the economic interests of their nationals and create mechanisms for the resolution of investment disputes, so as to reduce the possibility of arbitrary action by the host country. United Nations Conference on Trade and Development, *Bilateral Investment Treaties in the mid-1990s* (Geneva: UNCTAD, 1998), p. 10.

11. For a detailed discussion of the current status and outlook of foreign investment in Cuba, see Matias F. Travieso-Diaz and Charles P. Trumbull IV, *Foreign Investment In Cuba: Prospects and Perils*, 35 *Geo. W. Univ. Int’l L.R.* 903 (2003) (hereinafter “Prospects and Perils”).

12. Omar Everleny Pérez Villanueva, *La Inversión Extranjera Directa en Cuba: Evolución y Perspectivas*, Centro de Estudios de la Economía Cubana, Universidad de la Habana, 2001 (hereinafter “Pérez 2001.”)

13. FDI in Cuba was reported as dropping to \$38.9 million in 2001 from over \$400 million the year before. Foreign Investment in Cuba falls, EU Wants Reform, Reuters, July 8, 2002.

14. As of 2002, Cuba reported that there were slightly over four hundred foreign business concerns operating in the country. Paolo Spadoni, “*Foreign Investment in Cuba: Recent Developments and the Role in the Economy*,” in *Cuba in Transition—Volume 12* (2002) (hereinafter “Spadoni”), available online at <http://lanic.utexas.edu/project/asce/pdfs/volume12/spadoni.pdf>. However, by the end of 2003 the total number had dropped to 342. *Number of foreign concerns doing business in Cuba down for 2003*, CUBANET (March 19, 2004), available online at <http://www.cubanet.org/CNews/y04/mar04/23e5.htm>.

15. Foreign Investment.

16. Foreign Investment.

17. Robert David Cruz, *Foreign Direct Investment in Post-Castro Cuba: Problems, Opportunities and Recommendations*, Institute for Cuban and Cuban-American Studies, University of Miami (2003) at 4.

Foreign investment to date totals only \$1.9 billion.<sup>18</sup> In addition, most investors bring in limited amounts of capital; seventy-five percent of all investment is for less than \$5 million. Despite the relatively small amount of foreign investment, the presence of foreign capital has benefited the Cuban economy. In 2000, enterprises with foreign investors exported \$757.5 million worth of goods.<sup>19</sup> In 2001, enterprises involving foreign investors accounted for approximately 16.5 % of the country's total revenues from all sources.<sup>20</sup> In 2000, the total sales of goods and services reached \$1.748 billion.<sup>21</sup>

### POTENTIAL THREATS TO EXISTING FOREIGN INVESTMENTS IN CUBA IN THE EVENT OF A CHANGE IN THE COUNTRY'S POLITICAL SYSTEM

This section discusses the potential risks faced by foreign investors who are doing business in Cuba at the time the country makes a transition to free-market, democratic rule. For purposes of this section, we will assume that the current legislation pertaining to foreign investment remains in effect at the time adverse actions are contemplated. This is a realistic assumption because it would appear unlikely that legislation affecting the status and rights of foreign investors will

be enacted early in the transition given its relatively low priority compared to other more pressing legal and economic reforms.<sup>22</sup>

Nobody can predict with certainty how a post-transition Cuban government will treat existing foreign investments on the island. Nevertheless, there are several threats that could be faced by foreign investors. Whether such threats would materialize is in large part a function of the attitudes and policies of a post-transition government.<sup>23</sup> The threats that could be faced by current foreign investors can be divided into two broad categories: state actions and private actions.<sup>24</sup> Adverse state actions might go as far as the confiscation of income producing properties in which foreign investors have interests. But even if the post-transition government does not engage in outright confiscation, it could nevertheless issue laws and regulations that increased the cost or difficulty of doing business in Cuba by those currently investing in the island.<sup>25</sup> Furthermore, despite existing contractual relationships between enterprises controlled by the Cuban government and foreign investors, a transition government might repudiate those relationships or seek to terminate them. Finally, as the post-transition Cuban government seeks to resolve the outstanding expropriation claims, current foreign investors might become dispossessed of their assets or,

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18. Oficina Nacional de Estadísticas, *Anuario Estadístico de Cuba*, August 2001 (hereinafter "Anuario Estadístico"). Foreign investment figures vary widely, in part because many estimates include projected or proposed investments in addition to those in place. Carmelo Mesa-Lago, "The Cuban Economy in 1999-2001: Evaluation of Performance and Debate on the Future" in *Cuba in Transition*—Volume 11 (Aug. 2001), 4 (hereinafter "Mesa-Lago 2001").

19. Everlery Pérez Villanueva, *Cuba: An Overview of Foreign Investment* (February 2002), available online at <http://www.carleton.ca/economics/cep/cep02-04.pdf> (hereinafter "Pérez 2002") at 9.

20. Spadoni at 18.

21. Spadoni at 18.

22. See, e.g., Matias F. Travieso-Diaz and Steven R. Escobar, *Cuba's Transition to a Free-Market Democracy: A Survey of Required Changes to Laws and Legal Institutions*, 5 DUKE J. COMP. & INT'L L. 379 (1995) ("Law Changes") for a discussion of the key legal reforms that will need to be implemented during the early phases of Cuba's transition.

23. The nature of the threats to foreign investors and the extent to which investors can protect themselves from adverse governmental action will depend in good measure on the type of transition that Cuba experiences. If the transition is gradual and takes place over a period of many months or years, the investors might be able to take defensive measures such as discontinuing further investments and seeking (if feasible) to liquidate their investment.

24. This article addresses only those actions taken by the state or private parties within the confines of the law. In a turbulent transition environment, there could be unlawful acts of individuals against the economic assets or the persons of foreign investors. Protection against such unlawful acts can only be expected if the transition government ensures that the rule of law prevails in the country. See *Law Changes* at 393-94, 408-09.

25. This practice is often referred to in the literature as "creeping expropriation" and was engaged in by the Cuban government in the 1959-60 period as a prelude to the actual expropriations that followed shortly thereafter. See *The Cuban Nationalizations*.

if keeping the subject property, be assessed taxes or fees to finance the resolution of outstanding expropriation claims. The post-transition government might also, either to raise more revenue or out of a desire for retribution, increase taxes in a way that would have a direct negative effect on the bottom-line of foreign investors.

Current foreign investors may also face threats from private actors who might lodge legal claims and challenges against them based on various legal theories. For example, persons or enterprises whose property was expropriated by the Cuban government and has since been transferred to enterprises involving current foreign investors, might seek compensation directly from investors in the form of rents or damages. In addition, Cuban employees of current foreign investors might seek damages for alleged violations of fair labor standards, and other parties injured by the actions of investors might resort to the courts to seek redress for harms allegedly suffered at the hands of such foreign investors.

Regardless of whether these potential adverse actions by the government or private parties are successfully litigated or otherwise resolved, their assertion would likely result in the imposition of substantial legal and commercial costs upon affected foreign investors.

### Adverse State Actions

**Expropriation or Confiscation:** The potential expropriation or confiscation<sup>26</sup> of foreign investor property after a democratic transition in Cuba has

been raised in two contexts: first, in connection with claims raised by former property owners for the restitution of their expropriated assets; and second, as a punitive measure in retribution for the perceived collaboration of the investors with the current regime.

**Settlement of Property Claims:** As discussed above, in the first few years of the Revolution, the Cuban government seized nearly all private property in the country, and provided no compensation for the takings. As a result, there are outstanding claims by former property owners that could compete with the rights of foreign investors who have entered into joint ventures or other forms of investment that use or benefit from the expropriated properties.<sup>27</sup> Depending on what approach the Cuban government takes to addressing the pending expropriation claims, foreign investors could see their interests in joint ventures and other investment vehicles subject to expropriation by Cuba. Thus, for example, if the Cuban government decides to grant restitution to the former property owners of the assets taken from them in the 1960s, such a solution would require expropriation of the assets now held by some joint ventures with foreign investors.

There are conflicting views on whether Cuban law and international law principles require the restitution of expropriated assets to their former owners.<sup>28</sup> Whichever viewpoint is adopted, however, it is likely that in a number of instances the state will decide to return to the former owners title to a property that is

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26. Confiscation is the seizure of private property by the state without compensation, usually to punish the person whose property is seized for who he is or for what he has done. Confiscations are ordered for political, religious, legal or other reasons relating to the person subjected to the taking, and not to the property itself. For example, forfeiture is confiscation of specific property or deprivation of rights as punishment for a breach of contract or a crime. BLACK'S LAW DICTIONARY 778 (Rev. 4th Ed. 1968). Expropriation, on the other hand, is the taking by the state, subject to compensation, of specified property for some public purpose, with the taking being independent of the acts or identity of the owner. The state, may for instance, reclaim private land for public use by eminent domain and thereby expropriate the land from its owners. *Id.* at 616.

27. For a discussion of potential approaches to resolving the expropriation claims by U.S. nationals and others, see Matias F. Travieso-Diaz, *Some Legal and Practical Issues in the Resolution of Cuban Nationals' Expropriation Claims Against Cuba*, 16 U. PA. J. INT'L BUS. L. 217 (1995); Matias F. Travieso-Diaz, *Alternative Remedies In A Negotiated Settlement Of The U.S. Nationals' Expropriation Claims Against Cuba*, 17 U. Pa. J. Int'l. Bus. L.659 (1996).

28. Compare, e.g., Oscar M. Garibaldi and John D. Kirby, *Property Rights in the Post-Castro Cuban Constitution*, in EXPROPRIATED PROPERTIES IN A POST-CASTRO CUBA: TWO VIEWS, Institute for Cuban and Cuban-American Studies, University of Miami (2003) at 25 (suggesting that the expropriations carried out by the Cuban government in the early days of the Revolution violated the 1940 Constitution and international law and therefore restitution of the assets to the former owners is the required remedy) with Matias F. Travieso-Diaz, *Alternative Recommendations for Dealing with Confiscated Property in Post-Castro Cuba*, *id.* at 77-81 (arguing that the expropriations were effective in passing legal title to the state, thus restitution of the assets to the former owners is not mandatory but is only one of a number of ways of dealing with the properties at issue.)

the subject of a joint venture or other investment vehicle involving a foreign investor. In those instances, the state will have to provide adequate compensation to the investor in the manner described below.

**Punitive Expropriations:** While undeniably the Cuban government has the power (within certain limits) to expropriate the assets of private parties,<sup>29</sup> the Cuban Constitutions—both before and after the Revolution—require that any such expropriations be accompanied by the payment of adequate compensation.<sup>30</sup> The same result is dictated by the express provisions of Law 77.<sup>31</sup> Therefore, should a transition government in Cuba decide to expropriate the assets of foreign investors, it would have to develop measures to compensate the investors for the taking of their property.

Payment of such compensation could only be arguably avoided if the Cuban Constitution and the Foreign Investment Law were amended to change the le-

gal requirements for expropriating the assets of foreign investors and eliminate the obligation to provide compensation in the event of expropriation. Such a change, however, would be problematic as inconsistent with the long held principle of Cuban law prohibiting *ex-post facto* laws.<sup>32</sup>

**Confiscation:** The discussion above suggests that the taking of the property of current foreign investors by a Cuban transition government, if it could be lawfully accomplished, would have to be accompanied (or followed in short order) by the payment of adequate compensation. Another question is whether there is any basis under Cuban or international law for a successor government to confiscate the assets of foreign investors and offer no compensation to them.

Current<sup>33</sup> and pre-Revolutionary<sup>34</sup> Cuban law prohibit confiscation of property except as punishment for illegal behavior. Indeed, a number of laws were

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29. Art. 25 of the current (1992) Cuban Constitution states: “Se autoriza la expropiación de bienes, por razones de utilidad pública o interés social y con la debida indemnización.” (Expropriation of assets is authorized, for reasons of public utility or social interest, and subject to proper indemnification.) A transition government would therefore have to make some public interest showing in order to justify the expropriation of the assets of foreign investors.

30. *Id.* Likewise, Art. 24 of the 1940 Constitution stated: “No other natural person or corporate entity shall be deprived of his property except by competent authority, for a justified cause of public utility or social or national interest. The procedure for the expropriations and the methods and forms of payment will be established by law, as well as the competent authority to declare the cause of public utility or social or national interest and the necessity for the expropriation.”

31. Art. 3 of Law 77 states in relevant part: “The foreign investors within Cuban national territory enjoy full protection and security and their assets cannot be expropriated, except for reasons of the public good or in the interest of society, as declared by the Government, in accordance with the Constitution of the Republic, current legislation, and international agreements covering the mutual promotion and protection of investments undertaken in Cuba. In the case of expropriation, indemnification is made in freely convertible currency and is equal to the commercial value established by mutual agreement.”

32. The current Cuban Constitution states in Art. 61 that “Las leyes penales tienen efecto retroactivo cuando sean favorables al encausado o sancionado. Las demás leyes no tienen efecto retroactivo a menos que en las mismas se disponga lo contrario por razón de interés social o utilidad pública.” (Penal laws can be given retroactive effect if they are favorable to an indicted or convicted person. All other laws may not have retroactive effect unless the laws stipulate otherwise for reason of social interest or public utility.)

Art. 22 of the 1940 Constitution had an even stronger prohibition against *ex-post facto* laws: “No other laws [other than penal laws favorable to the offender] shall have retroactive effect unless the law itself so provides for reasons of public order, social utility, or national necessity, as may be expressly stipulated in that law by a vote of two-thirds of the total number of members of each legislative body. If the basis of the retroactivity should be impugned as unconstitutional, it shall be within the jurisdiction of the tribunal of constitutional and social guarantees to decide upon the same, without the power of refusing to render decision because of form or for any other reason.

Art. 22 goes on to state that “In every case the same law shall concurrently establish the degree, manner, and form of indemnification for injuries, if any, and of retroactivity affecting rights legitimately acquired under the protection of prior legislation.” Moreover, “[t]he law giving the protection afforded by this article shall not be valid if it produces effects contrary to the provisions of Article 24 of this Constitution [which prohibits uncompensated expropriations].

33. Art. 60 of the current (1992) Constitution states: “La confiscación de bienes se aplica solo como sanción por las autoridades, en los casos y por los procedimientos que determina la ley.” (Confiscation of property can only be applied as a penal sanction, in the cases and under the procedures established by law.)

34. Art. 24 of the 1940 Constitution unequivocally declared: “Confiscation of property is prohibited.”

enacted by the Cuban Revolutionary Government since its advent to power in 1959 confiscating the property of whole classes of people for alleged criminal activities.<sup>35</sup> However, the Cuban government has not ordered the outright confiscation, under color of law, of the assets of individuals not charged with a crime against the state.

A transition government would thus have to define what conduct by a foreign investor would constitute a crime justifying the confiscation of the investor's property. Presumably, and setting aside any instances in which a foreign investor may have engaged in common criminal activities, the theory under which such confiscation might be attempted would be that by investing in the country the investor collaborated with the previous administration's illegal acts. That theory has been applied from time to time to dispossess those who were seen as cooperating or being part of deposed regimes; for example, it was applied in Czechoslovakia in 1945 to confiscate all farmland belonging to Germans or Hungarians,<sup>36</sup> and in 1950 by China against foreigners in response to hostile acts by investors or investors' states.<sup>37</sup> However, punitive confiscations based on something other than individual culpability for illegal acts are viewed as violating basic principles of justice.<sup>38</sup>

Another theory that has been propounded is that underlying the Helms-Burton Act.<sup>39</sup> Section 4(13) of that statute states that a person "traffics" in confiscated property if "that person knowingly and intentionally—

- (i) sells, transfers, distributes, dispenses, brokers, manages, or otherwise disposes of confiscated property, or purchases, leases, receives, possesses, obtains control of, manages, uses, or otherwise acquires or holds an interest in confiscated property, (ii) engages in a commercial activity using or otherwise benefiting from confiscated property, or (iii) causes, directs, participates in, or profits from, trafficking (as described in clause (i) or (ii)) by another person, or otherwise engages in trafficking (as described in clause (i) or (ii)) through another person, without the authorization of any United States national who holds a claim to the property."<sup>40</sup>

Together with that definition is that of "confiscated property", which is broadly said to include "the nationalization, expropriation, or other seizure by the Cuban Government of ownership or control of the property, on or after January 1, 1959—(i) without the property having been returned or adequate and effective compensation provided; or (ii) without the claim to the property having been settled pursuant to an international claims settlement agreement or other mutually accepted settlement procedure."<sup>41</sup>

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35. Law 78 of February 13, 1959, *published in* Gaceta Oficial, February 19, 1959; Law 438 of July 7, 1959, *published in* Gaceta Oficial, July 7, 1959; Constitutional Reform Law of December 22, 1959, *published in* Gaceta Oficial, December 22, 1959; *see generally*, Agustín de Goytisolo, *On the Continued Good Standing of Pre-Castro Legal Entities: Ubi Lex Non Distinguit, . . . Nec Nos Distinguere Debemus*, paper presented at the 6<sup>th</sup> Annual Meeting of the Association for the Study of the Cuban Economy, August 8-10, 1996, *available online at* <http://lanic.utexas.edu/la/cb/cuba/asce/cuba6/59Goytisolo.fm.pdf>.

36. Sophia von Rundstedt, *The Restitution of Property After Communism: Germany, the Czech Republic and Poland*, 4 Parker Sch. J. of Eastern Eur. Law 261, 269 (1997).

37. Pat K. Chew, *Political Risk and U.S. Investments in China: Chimera of Protection and Predictability*, 34 Va. J. Int'l L. 615, 626-27 (1994).

38. von Rundstedt, at 281-82. It has been held by U.S. courts that Cuba's *de facto* confiscations of the assets of U.S. companies operating in Cuba violated international law because Cuba carried the expropriations for purposes of retaliation against the U.S. government. *Banco Nacional de Cuba v. Sabbatino*, 193 F.Supp. 375, 384 (S.D.N.Y. 1961), *aff'd*, 307 F.2d 845 (2d Cir. 1962), *rev'd on other grounds*, 376 U.S. 398 (1964); *Banco Nacional de Cuba v. Farr*, 272 F.Supp. 836, 838 (S.D.N.Y. 1965), *aff'd*, 383 F.2d 166, 184-85 (2d Cir. 1967), *cert. denied*, 390 U.S. 956 (1968).

39. Cuban Liberty and Democratic Solidarity (LIBERTAD) Act of 1996," Pub. L. No. 104-114, 110 Stat. 785, *codified as* 22 U.S.C. Chapter 69A, also known as the "Helms-Burton Law" (hereinafter "the Helms-Burton Act")

40. *Id.*, Section 4 (13)(A).

41. *Id.*, Section 4(4).

These definitions are used in Title III of the Helms-Burton Act to impose sanctions on third country nationals (i.e., foreign investors in Cuba) who do business that involve properties expropriated from U.S. nationals. Thus, in Section 301,<sup>42</sup> Congress finds that “it is in the interest of the Cuban people that the Cuban Government respect equally the property rights of Cuban nationals and nationals of other countries.”<sup>43</sup> The Congress also makes the following additional findings in Section 301 of the Act:

- “the Cuban Government is offering foreign investors the opportunity to purchase an equity interest in, manage, or enter into joint ventures using property and assets some of which were confiscated from United States nationals;”<sup>44</sup>
- “this ‘trafficking’ in confiscated property provides badly needed financial benefit, including hard currency, oil and productive investment and expertise to the current Cuban Government and thus undermines the foreign policy of the United States;”<sup>45</sup>
- “the international judicial system, as currently structured, lacks fully effective remedies for the wrongful confiscation of property and for unjust enrichment from the use of wrongfully confiscated property by governments and private entities at the expense of the rightful owners of the property;”<sup>46</sup>

- “international law recognizes that a nation has the ability to provide for rules of law with respect to conduct outside its territory that has or is intended to have substantial effect within its territory;”<sup>47</sup>
- “the United States Government has an obligation to its citizens to provide protection against wrongful confiscations by foreign nations and their citizens, including the provision of private remedies;”<sup>48</sup> and
- “to deter trafficking in wrongfully confiscated property, United States nationals who were the victims of these confiscations should be endowed with a judicial remedy in the courts of the United States that would deny traffickers any profits from economically exploiting Castro’s wrongful seizures.”<sup>49</sup>

Based on these findings, Section 302 makes any person that “traffics” in property confiscated by the Cuban Government on or after January 1, 1959, liable for money damages to any U.S. national who owns the claims to such property and grants U.S. district courts jurisdiction over such actions where the amount in controversy exceeds \$50,000.<sup>50</sup> Thus, subject to certain limitations,<sup>51</sup> the Helms Burton Act imposes strict liability on third parties held to be trafficking in confiscated properties in Cuba against which a U.S. national holds a certified claim. Assum-

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42. 22 U.S.C. §§ 6081-6085.

43. 22 U.S.C. § 6081, finding number 5.

44. *Id.*, finding number 6.

45. *Id.*, finding number 7.

46. *Id.*, finding number 8.

47. *Id.*, finding number 9.

48. *Id.*, finding number 10.

49. *Id.*, finding number 11.

50. 22 U.S.C. § 6082.

51. Suits by certified claimants against third parties are subject to a \$50,000 floor on the amount in controversy; that floor is computed on the principal value of the claim “exclusive of interest, costs, and attorneys’ fees.” Section 302(b), 22 U.S.C. § 6082(b). Another limitation on the ability of certified claimants to sue is a two-year statute of limitations.

Suits under Title III of the Helms Burton Act are currently being held in abeyance under authority granted to the President by Section 306(b)(1), which allows the President to suspend the right to bring an action under Title III for discrete periods of six months by determining and reporting in writing to the appropriate congressional committees that such suspension is necessary to the national interests of the United States and will expedite a transition to democracy in Cuba.

ing jurisdiction can be asserted over the defendant under the rules of United States courts, all that the plaintiff needs to establish to prove liability is that the defendant was “trafficking” in the properties at issue after plaintiff’s right of action accrued under the statute, and that the last act of trafficking occurred two years or less before the initiation of the action.

It is interesting, however, that in defining “trafficking” in “confiscated property” and establishing judicial remedies in the United States against third-country investors doing business that involves expropriated properties in Cuba, the Helms-Burton Act does not cite to any Cuban domestic law, or to any international law principle that proscribes the conduct of such third parties; to the contrary, the above cited finding 8 in Section 301 recognizes that “the international judicial system, as currently structured, lacks fully effective remedies for . . . for unjust enrichment from the use of wrongfully confiscated property by governments and private entities at the expense of the rightful owners of the property.” Whereas, as discussed below, unjust enrichment could arguably be raised in Cuba as a cause of action for damages against third country investors by the state or former owners of the property involved in the investment, there appears to be no basis in international or Cuban domestic law for confiscating the assets of such investors.

Indeed, the activities of most foreign investors in Cuba (e.g., participating in the building and operation of hotels) will be shown to be common business acts, sanctioned by the Cuban laws and encouraged by the Cuban government. Such commercial acts

may not be easily associated directly with oppression, human rights abuses or other political crimes by the host government. For that reason, confiscation of the investors’ property just for having participated in economic activities in the country would appear to be a punitive confiscation contrary to Cuban law as well as international practice.

**Effect of BITs:** Another factor to consider in determining the validity of any expropriations or confiscations of the assets of foreign investors is that, as discussed earlier, Cuba has entered in over sixty bilateral investment treaties with other countries, including most capital-exporting nations other than the United States.<sup>52</sup> All of these treaties contain provisions specifying that expropriation of investments of the parties will be made only for reasons of public utility in accord with domestic law, on a non-discriminatory basis, and pursuant to compensation that is immediate, adequate and effective.<sup>53</sup> If Cuba chooses to expropriate foreign holdings, it must do so in accordance with its domestic law and the provisions of the various treaties in force.<sup>54</sup> In particular, the BIT provisions regarding the amount and form of payment become applicable and ordain that payment for the value of the expropriated assets be made in accordance with the Hull formula or a similar formulation.<sup>55</sup> Failure to abide by these requirements may trigger dispute resolution provisions in the BITs and eventually lead to international arbitration between the investor and the Cuban government or give rise to country-to-country disputes under the terms of the BITs.<sup>56</sup>

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52. *See* Cuba’s BITs.

53. *Id.*

54. As noted earlier, both Art. 25 of the current Cuban Constitution and Law No. 77 recognize the right of the State to expropriate foreign investments, but only “for reasons of public utility or social interest” and subject to the payment of compensation for “the commercial value” of the property being expropriated.

55. The various BITs include different descriptions of the compensation formula, but they all have in common the requirements that the payment must be prompt and adequate and based on the fair market value of the investment at the time of the taking.

56. This does not necessarily mean that the investor would prevail in the dispute or that Cuba would be required to pay damages for the taking of the investor’s property. The question whether foreign investors in Cuba have acquired good title to their assets is one that will need to be decided in the Cuban courts; the answer to that question would in part dictate the ultimate outcome of any investor-initiated arbitration.

Thus, the existence of these BITs provides some assurance to investors from the countries that signed the BITs with Cuba that a transition Cuban government will not take measures that adversely affect the investment without providing adequate compensation and giving serious consideration to the consequences of such a step.

**Contract Termination:** The contractual arrangements between a foreign investor and a Cuban government entity are formal agreements resulting from often protracted negotiations. A joint venture, for example, is a legal entity consisting of one or more Cuban parties and one or more foreign investors. The contributions of each participant and the breakdown in stock ownership are agreed upon before governmental approval is granted, and are reflected in the joint venture agreement and in a governmental decree approving the joint venture.<sup>57</sup>

The duration of a joint venture or other form of foreign investment in Cuba is specified both in the agreement itself and in the governmental decree approving it.<sup>58</sup> Therefore, one simple way in which a transition government can terminate its joint venture agreements with foreign investors is to allow them to lapse by not extending them past their expiration dates. This alternative would be effective and relatively easy to implement, except for the need to liquidate the enterprise and dispose of the liquidation proceeds in accordance with the provisions of the

joint venture agreement or other agreement between the foreign investor and its Cuban partner.<sup>59</sup>

In addition to causing the liquidation of a foreign investor enterprise by allowing the term of its authorization to expire, the Cuban government could proceed unilaterally to order the termination of the venture. A number of examples of such terminations have taken place under the current Cuban government.<sup>60</sup> Although, hopefully, a transition government will have high regard for the law and for its contractual commitments, nothing prevents the government from terminating the joint venture for convenience and paying appropriate termination charges, as would be the case in an expropriation situation. Only where there has been a failure by the foreign partner to carry out its contractual commitments would there be a basis for a default termination, and even then the investor should be entitled to recover the value of its investment, minus such damages as may result from its default.<sup>61</sup>

**Civil or Criminal Actions by the State:** In addition to (or instead of) actions against the foreign investors directed at terminating its business activities, the state could bring a tort action against foreign investors for unjust enrichment or for damages (such as environmental harm) caused by their activities in Cuba. Alternatively, the state could bring criminal prosecution against the investor on some theory that links its activities with unlawful acts of the current

57. Prospects and Perils at 923-25.

58. Law 77, Art. 24(1). According to Art. 2(b) of Law 77, authorization by the Executive Committee of the Council of Ministers that allows an enterprise with foreign capital to operate in Cuba does so for "a specified period of time." Art. 4(1) allows the extension of such authorization, provided an application is properly made. Extension of the authorization is discretionary with the Cuban government; if not granted, Art. 4(2) directs that the enterprise be liquidated and the foreign investor receive its share of the liquidation proceeds.

59. *Id.*, Art. 13(3).

60. José de Cordoba and Carla Vitzthum, *For Jilted Engineers From Canada, Cuba Wasn't a Cheap Date*, *The Wall Street Journal* (June 28, 1999), p. A1, A21; Fábregas I Guillén, *La ley de la inversión extranjera*, p. 36; José Fernández González, *Cuba: Del socialismo al Fascismo—Un español dentro de la revolución cubana 1980-1996* (Puerto Rico, 1996), p. 75-81; Islands of Capitalism, p. 199; Juan O. Tamayo, *Crackdowns, Restrictions Sour Investors on Cuba*, *The Miami Herald* (June 10, 1999), p. 22A.

61. There are no express provisions in Cuba's Civil Code to cover a termination for default situation. However, Art. 269 of the Civil Code provides that, where a contract provides for the imposition of liquidated damages if there is a default by one of the parties, such damages may be equitably reduced if the contractual obligation has been performed partially or with defects. Ley No. 59, *Código Civil* (July 16, 1987), *Gaceta Oficial* (Oct. 15, 1987) (hereinafter "Civil Code"), Art. 269. Therefore, the concept of partial compensation in the event of default is implicitly recognized by Cuban law.

government or constitutes criminal behavior under Cuban law.

**Civil Actions:** Chapter V of Title I of the Civil Code provides for recovery of damages for unjust enrichment, which occurs when “value is conveyed from one party to another without legitimate cause.”<sup>62</sup> The party who is guilty of *unjust enrichment* must provide restitution to the other party, including returning any property taken, providing indemnification for the property’s value if such return is not feasible, providing compensation for the benefits or gains achieved from the misappropriation of the property, and paying damages as appropriate.<sup>63</sup> The party guilty of unjust enrichment must also account for the loss or damage of the property from the moment he became aware that he had no right to the property.<sup>64</sup> The Code makes no distinction whether a cause of action for unjust enrichment would be available to the state as well as to private parties, and there is no reason to believe it would not be available to both.

If the state sought to pursue an unjust enrichment action against a foreign investor it would have to establish, however, that the benefits reaped by the foreign investor through its activities in the island were attained “without legitimate cause.” Given that such benefits were obtained through activities undertaken in partnership with the state and pursuant to explicit governmental approval, it might be difficult for the transition government to establish that there was an inherent illegality to the acts of the investor without enacting *ex-post facto* laws declaring such agreements

and approval null and void after the fact. As discussed above, the state’s ability to issue such *ex-post facto* laws to the detriment of a former (or current) business partner is doubtful.

Whereas the state may have difficulties in prevailing in an unjust enrichment action against its former (or current) foreign investor partner, there may be a basis for actions by a transition government against a foreign investor whose business activities in Cuba have caused damage to the country or its citizens. Prime among the potential civil actions that a transition government might bring against a current foreign investor would be those for ecological or other environmental damage caused by the investor’s operations in the country. Chapters XI through XIII of Cuba’s Environmental Law provide for administrative, civil and criminal sanctions against those who violate environmental laws and regulations.<sup>65</sup> These provisions of existing law should provide the basis for requiring current investors to shoulder the costs of remediation of environmental damage caused by their activities.<sup>66</sup> And, while the foreign investor might try to shift all or some of the blame to the state for the damages caused by its activities, such a defense would have to go to the facts of how and why the environmental damage was caused rather than to the legal basis for imposing liability.<sup>67</sup>

**Criminal Actions:** Some have argued that current foreign investors should be subjected to criminal liability for the “illegal exploitation of [Cuban] workers.”<sup>68</sup> It has been argued that not only does the af-

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62. Civil Code, Art. 100.

63. *Id.*, Art. 101.1 through 101.5.

64. *Id.*, Art. 102.

65. Ley 81 del Medio Ambiente, arts. 67-75, in Gaceta Oficial, July 11, 1997 (“Ley del Medio Ambiente”); see also, Matias F. Travieso-Diaz, *Key Environmental Legislation for Cuba’s Transition Period*, 21 U. Pa. J. Int’l Bus. L. 331, 345-46 (2000) (“Key Environmental Legislation”). While the law provides no enforcement details, it establishes a principle for imposing liability upon foreign investors for environmental damages caused by their activities.

66. Key Environmental Legislation at 370.

67. Some of the provisions of the Ley del Medio Ambiente are vague enough to be perhaps unenforceable. *Id.* at 345. However, arts. 81-88 and 95-96 of the Civil Code provide a potential independent basis for establishing liability of foreign investor under a tort theory of action for the damages caused by its business activities. See discussion, *infra*.

68. Alberto Luzárraga, *Socialist Cuba—The Nullity of the Foreign Investment Contracts Due to an Illicit Cause: To Defraud the Cuban Worker*, page 254, 11<sup>th</sup> Annual Proceedings of the Association for the Study of the Cuban Economy (hereinafter “Luzárraga”).

affected employee retain a direct private right of action against the current foreign investor, but that the Cuban state itself, acting in its *parens patriae* capacity,<sup>69</sup> retains the right to bring suit on behalf of the Cuban people against the alleged foreign investor accomplice.<sup>70</sup>

The prospect of bringing criminal prosecution against current foreign investors might satisfy an urge to seek retribution for moral wrongs against the Cuban worker.<sup>71</sup> However, pursuing such a course of action would require the government to repudiate, after the fact, the legal and business framework under which current foreign investments were made and find the actions of the investors to be not only morally reprehensible but indeed criminal. Apart from the legal difficulties pointed out above, criminalization of conduct that was sanctioned by the laws at the time it was undertaken might seriously undercut the transition government's efforts to create a stable political and legal environment for foreign investment, with clear legal rules, robust protection of property rights, and a firm commitment to and respect of the

rule of law, necessary ingredients for a welcoming business climate.

**Increased Taxation:** A transition Cuban government will likely re-evaluate Cuba's current tax policies<sup>72</sup> and modify them to remove their rigidity and better align them with the government's policy objectives.<sup>73</sup> At the time this is done, the government may decide to subject all foreign investors (both current and those who start doing business in Cuba after the transition) to the same tax treatment.

On the other hand, the transition government might decide that it would be unfair to have those who profited economically from the exploitation of the Cuban people during the previous regime to be placed on an equal footing with post-transition investors.<sup>74</sup> Under such "worst-case" scenario (from the current investors' standpoint), current investors would be taxed more heavily than post-transition investors in an effort to recapture some of the unjust gains derived by pre-transition investors. Adverse tax treatment could take, for example, the form of higher tax rates, lower tax credits, denial of deductions and

69. The term "parens patriae" means "parent of the country" in Latin. The legal doctrine of parens patriae conceives of the state "in its capacity as provider of protection to those unable to care for themselves". . . as a "doctrine by which a government has standing to prosecute a lawsuit on behalf of a citizen, esp. on behalf of someone who is under a legal disability to prosecute the suit." Black's Law Dictionary (8th Ed. 2004).

70. Luzárraga states that the "worker retains his civil action to demand damages from the party that employed him subject to abusive conditions. He may demand his back wages plus legal interest, at the rate applied by the international market for the type of work performed, plus any other punitive damages that are deemed appropriate. And the Cuban nation is also a party that can claim damages inasmuch as the system described perpetuated a tyranny and instituted an unfair system of employment that subjected its citizens to a demeaning work relationship."

71. At least some Cuban workers who are employed by foreign ventures manifest not feeling exploited by the arrangement between their employer and the Cuban government. See Prospects and Perils at 935-38.

72. Cuba's basic taxation framework consists of Law 73—The Tax Systems Law, Gaceta Oficial (August 1994), and Decree-Law 169 (January 1997). Decree-Law 169 granted primary taxation authority to the Ministry of Finance, and created the National Office of Tax Administration (ONAT).

73. An example of the rigidity of the current Cuban tax system is the "10% maximum cost deductibility rule." In determining taxable income, the current tax regime allows for the deduction of only 10% of purchased inputs. For example, if a micro-enterprise owner incurs a \$1,000 expense on purchased inputs and has gross receipts of \$2,000, he/she is allowed a deduction of only \$100 in computing taxable income, thereby imposing a tax on 95% of gross receipts. In contrast, with respect to business activities, U.S. tax code § 162 allows for full deduction, with some exceptions, of all "ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business." See generally Archibald R. M. Ritter & J.A. Turvey, *The Tax Regime for Micro-Enterprise in Cuba*, Carleton University's Department of Economics' Carleton Paper Series number 99-04, February 2000, available online at <http://www.carleton.ca/economics/cep/cep99-04.pdf> (visited on February 12, 2004) (hereinafter "Tax Regime").

74. This assumes that a transition Cuban government will decide to grant preferential tax treatment to post-transition investors as a means of attracting foreign investment to Cuba. However, granting tax incentives as a means to attract foreign investment has been questioned as being of dubious efficacy and wasteful of the state's economic resources. See discussion *infra*.

exemptions or, conversely, failure to grant current investors tax benefits for which post-transition investors could qualify, such as tax deferrals, lower applicable tax rates, higher tax credits, greater deductions, and tax holidays.<sup>75</sup> However, a survey of the literature turned up no documented instances in which a successor government chose to discriminate economically between pre-transition and post-transition foreign investors. Of course, the transition Cuban government could nevertheless decide to set such a precedent. But such an arguably backward-looking<sup>76</sup> action by the transition Cuban government is not likely to go unchallenged by the affected foreign investors who might charge the Cuban government with violating its commitments against discriminatory treatment of foreign investors under its various contractual agreements and BITs.

On the granting of investment tax incentives, some Eastern European countries such as Hungary, Poland, and the Czech Republic initially opted, during their transitions, to grant tax incentives for foreign investors in the hopes of stimulating foreign investment.<sup>77</sup> Those tax incentives, however, turned out to be rather short-lived.<sup>78</sup> In fact, many have argued that the granting of preferential tax treatment to foreign investors actually has a negligible impact on at-

tracting foreign investment<sup>79</sup> in addition to depriving the successor government of much-needed revenues to finance post-transition projects. Therefore, it is possible that a transition Cuban government will determine that its short-term need to raise the necessary tax revenues to finance a variety of post-transition projects—such as the resolution of expropriation claims—outweighs any potential negative economic effect on current foreign investors.

Obviously, current foreign investors would advocate for a tax policy that subjects them to the same treatment as other investors. And if the authors had to make a policy recommendation, it would be that equitable tax treatment (whether or not the government's tax policy involves tax incentives) for all investors is the approach that reflects the soundest economic development policy and the one most consistent with the obligations that Cuba has assumed by entering into BITs with a large number of foreign countries.

### Adverse Private Actions

**Claims by Former Property Owners:** Former property owners whose assets were expropriated by the Cuban government without compensation could in principle assert a number of claims against foreign investors who have conducted business utilizing or oth-

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75. The ultimate “worst case scenario” would be one in which a transition government terminates the contracts of current investors and forces them out of the country. However, assuming that a successor Cuban government harbors ill will towards pre-transition foreign investors, such ill will could arguably be more productively manifested by means of higher taxation (thereby generating additional revenue for the Cuban government) than by contract termination, asset expropriation or other punitive measures discussed earlier.

76. Eric A. Posner and Adrian Vermeule, *Transitional Justice as Ordinary Justice*, 117 Harv. L. Rev. 761, 766 (January 2004) (hereinafter “*Transitional Justice*”) (arguing that although many writers in the literature conceive of transitional justice as “backward-looking”, it could (and should) be understood in “forward-looking” terms).

77. Matias F. Travieso-Diaz and Stephan M Bleisteiner, *Some Lessons for Cuba from the Legal Changes in Eastern Europe*, 3 U. Miami Y.B. Int'l L. 173, 205-209 (1995) (hereinafter “*Some Lessons*”). For instance, with respect to certain key industries identified by Hungary, the successor government went so far as to grant a 100% tax exemption on income earned by foreign investors during the first five (5) years, and reduction of the exemption to 60% for the next five years. However, such tax incentives have been criticized, among other reasons, for being virtually meaningless in most cases because it usually takes several years before a foreign investor is able to turn a profit and thus benefit from the tax holiday. See Cheryl W. Gray and William W. Jarosz, *Law and the Regulation of Foreign Direct Investment: The Experience From Central and Eastern Europe*, 33 Colum. J. Transnat'l L. 1, 36-40 (1995) (hereinafter “*Law and Regulation*”).

78. Matias F. Travieso-Diaz and Alejandro Ferrate, *Recommended Features of a Foreign Investment Code for Cuba's Free Market Transition*, 21 N.C.J. Int'l L. & Com. Reg. 511, 545-46 (Summer 1996) (hereinafter “*Recommended Features*”).

79. Jeffrey M. Padwa, *Joint Venturing in Hungary: Negotiating Certainty in an Era of Reform*, 15 Suffolk Transnat'l L.J. 222 (Fall 1991) (hereinafter, “*Padwa*”); Yitzhak Hadari, *The Role of Tax Incentives in Attracting Foreign Investments in Selected Developing Countries and the Desirable Policy*, 24 Int'l Law. 121, 123 (1990); Kojo Yelapaala, *In Search of Effective Policies for Foreign Direct Investment: Alternatives to Tax Incentive Policies*, 7 Nw. J. Int'l. L. & Bus. 208, 212 (1985).

erwise involving the expropriated assets. Such claims could include, among others, tort claims for damage or diminution of value of the property and unjust enrichment.<sup>80</sup> Both of these causes of action are recognized by the current Cuban Civil Code.

**Claims by Former Property Owners:** Chapter IV of Title I of the Civil Code imposes an obligation on one who causes damage to another to provide remedy, including restitution, repairs of physical damage to property, recovery of monetary damages, and recovery for “daños morales” such as injury to reputation, pain and suffering, psychological impairment, and the like.<sup>81</sup>

With respect to restitution, the obligation of the tortfeasor is to return the improperly taken property and provide compensation for physical impairment of property or diminution in its value.<sup>82</sup> This right of recovery, however, does not apply to a third party who may have acquired the property in good faith.<sup>83</sup>

A former property owner who seeks to bring a tort claim against a foreign investor who has made use of the investor’s property would have to overcome several obstacles. First, if the expropriation by the Cuban government was effective in passing title to the state,<sup>84</sup> the former property owner would be limited to whatever compensation is granted by the transition government under its program for the resolution of outstanding property claims. Since one of the main objectives of a claims resolution program is to end as quickly as possible all litigation relating to the expropriated property, the program may well bar actions by the former owners against third parties such

as foreign investors. Second, even if the expropriation by the state was unlawful and legally ineffective, the property owner may not have a claim against the foreign investor, since the investor may have acquired his interest in the property in good faith (an open legal and factual issue) and his conduct may have been lawful under Law 77 and other laws and decrees in effect at the time of the investment. Third, the former property owner would need to prove as a matter of fact what damages he suffered as a result of deterioration or other impairment of his property, and establish that those damages were caused by the acts or omissions of the investor—potentially a difficult task, since most foreign investments have occurred in the last decade, and the expropriations occurred over forty years ago, so the properties in questions had been under the sole control of the state for at least three decades prior to the initiation of the foreign investor’s activities.

For these reasons, it appears that a tort action by a former property owner against a foreign investor for damage or diminution in value of his property would encounter serious difficulties.

**Unjust Enrichment:** A cause of action for unjust enrichment by a former property owner against a foreign investor who has used the property is based on the assumption that such use was without legitimate cause, *i.e.*, unlawful. Therefore, the first obstacle that a former property owner would have to overcome as a matter of law would be a determination whether the investment activity, in all cases sanctioned by the current Cuban government and in most cases under-

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80. Since there is no contractual relationship between the foreign investors and the previous property owners, those claims based on contract theories such as unpaid rents would probably not be applicable.

81. Civil Code, Art. 81-83.

82. *Id.*, Art. 84.

83. *Id.*

84. It is open to debate whether the expropriations carried out by Cuba were effective in transferring title to the properties in question to the state. *See* n. 30, *supra*. For a discussion of the legal issues involved with the Cuban Government takings of private property, including the validity and legal effectiveness of the expropriations, *see* Matias Travieso-Diaz, *Some Legal and Practical Issues in the Resolution of Cuban Nationals’ Expropriation Claims Against Cuba*, 16 U. Pa. J. Int’l Bus. L. 217 (1995).

taken under an agreement with a government enterprise or instrumentality, was unlawful. In addition, as discussed above, suits by former property owners against third parties may be barred by the claims resolution law. Finally, the former owner would have to overcome evidentiary obstacles such as proving the amount and basis of his damages, including the amount of “rent” he would be owed for the use of the property.

From the foregoing, it appears that suits by former property owners against foreign investors arising out of the investors’ use of the property would have a number of legal and factual obstacles to overcome. Current foreign investors should however be aware that such suits are possible and, unless barred by law, likely in the event of a transition to a government that permitted such suits to be prosecuted.

**Actions by Third Parties:** The potential legal exposure facing current foreign investors is not limited to legal actions initiated by former property owners. There is a universe of other potential tort claimants living or otherwise acting within Cuba who—perhaps taking a cue from their litigious neighbors to the north—will be ready to pounce upon deep-pocketed foreign investors in efforts to seek legal redress for a wide range of injuries (economic and/or

physical) allegedly suffered at the hands of foreign investors at a time when such legal actions were not legally or politically feasible. Such actions might be initiated in Cuba or, arguably, in U.S. courts.<sup>85</sup>

For example, Cuba has recently signed contracts with over a dozen foreign companies to prospect, explore, and if significant oil deposits are discovered, drill for oil off Cuba’s waters.<sup>86</sup> Although this form of foreign investment is potentially very profitable, it is also quite risky from a liability perspective.

The potential environmental damage and public health risks posed by mining operations have been well documented.<sup>87</sup> Some examples of potential negative side effects include pollution of the water supply resulting in a wide range of human illnesses and the death of aquatic life, as well as many other forms of more generalized ecological damage. The adverse effects on the environment of the economic activities of the current Cuban government, acting often in conjunction with foreign investors, have been widely reported and are likely to continue.<sup>88</sup>

Oil production and transport activities pose similar (if not greater) risks as mining operations. An oil spill off Cuba’s coast could have a devastating impact upon an island nation that relies so heavily on tourism for foreign currency.<sup>89</sup> Individuals or entities<sup>90</sup>

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85. See, e.g., Amy Discoll, *Club Med Sued In Miami Over Use of Land in Cuba*, The Miami Herald (July 9, 2004), involving a family who brought suit against the Paris-based Club Med in U.S. District Court for “unjust enrichment” and on several other grounds in connection with Club Med’s investment in expropriated property in Cuba. The theory relied upon by the plaintiffs for filing suit in South Florida is that Club Med has substantial business contacts with Florida, and therefore general jurisdiction in Florida is appropriate.

86. Simon Romero, *Spanish Seek Oil Off Cuba, as Americans Watch Silently*, The New York Times (July 6, 2004); Larry Luxner, *Drilling for Black Gold, Spain’s Repsol-YPF Helps Cuba Search the Waters Off its Coast for Oil*, The Miami Herald (June 28, 2004).

87. A’an Suryana, *Mining Operations Put Environment at Risk*, Jakarta Post (June 5, 2002), available online at [http://www.ecologyasia.com/NewsArchives/Jun\\_2002/thejakartapost.com\\_20020605.G02.htm](http://www.ecologyasia.com/NewsArchives/Jun_2002/thejakartapost.com_20020605.G02.htm) (last visited on July 10, 2004).

88. Sergio Díaz-Briquets & Jorge Pérez-López, *Conquering Nature: The Environmental Legacy of Socialism in Cuba* (University of Pittsburgh Press (2000)); José R. Oro, *The Poisoning of Paradise: The Environmental Crisis in Cuba* (1992); Carlos Wotzkow, *Naturaleza Cubana* (1998); Agencia Ambiental Entorno Cubano (AAMEC), Informe Anual de la AAMEC: *Situación Ambiental de Cuba, 1997*(1997); República de Cuba, Ministerio de Ciencia, Tecnología y Medio Ambiente, Consulta Nacional Rio +5, Taller “Medio Ambiente y Desarrollo” (1997); María D. Espino, *Environmental Deterioration and Protection in Socialist Cuba*, in *Cuba in Transition—Volume 2* (1992).

89. See, e.g., *A U.S. federal judge has ordered Exxon Mobil Corp. to pay \$4.5 billion in punitive damages plus \$2.25 billion in interest because of the 1989 Exxon Valdez oil tanker spill, the lead plaintiff’s attorney says*, Reuters (January 28, 2004), available online at <http://www.cnn.com/2004/BUSINESS/01/28/exxon.valdez.reut/> (last visited on July 10, 2004).

90. The universe of potential plaintiffs could range from public interest NGOs and fishermen and other commercial enterprises seeking damages for the harm caused to their trade to landowners seeking redress for harm to their properties.

injured by such mining operations or oil spills<sup>91</sup> could pursue tort claims seeking legal compensation for their injuries. And even if Cuba's environmental laws or the Civil Code are found to provide no redress to private parties for damages suffered through action or inaction by the state or private parties,<sup>92</sup> such actions could be brought, at least in some cases, in U.S. courts.<sup>93</sup>

**Actions by Employees:** In addition to providing the current legal framework for foreign investment in Cuba, Law 77 requires that the Cuban labor used by foreign investors be provided through state employment agencies.<sup>94</sup> Once the joint venture or other investment mechanism has determined its labor needs, the enterprise contacts a designated state employment agency.<sup>95</sup> The state employment agency then hires the necessary Cuban workers and contracts them out to the enterprise involving the foreign investor.<sup>96</sup> The foreign investor pays the state employ-

ment agency directly in U.S. dollars (at rates set by the Cuban Government) for the use of the Cuban labor provided.<sup>97</sup> In turn, the state employment agency pays the Cuban worker a very small fraction of this money in Cuban pesos for his/her labor (again, at rates set by the Cuban Government), resulting in the state pocketing over ninety-five percent (95%) of the value of the work provided by Cuban workers to the foreign investor enterprises.<sup>98</sup>

The structure of the employment relationship among the Cuban worker, the state employment agency intermediary, and the foreign investor has been assailed by multiple sources as exploitative.<sup>99</sup> It has been argued that the structure of the employment relationship violates several International Labor Organization ("ILO") provisions to which Cuba is a party, namely Article 2 of Convention 87<sup>100</sup> and Article 9 of Convention 95.<sup>101</sup>

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91. Although the authors have chosen to highlight potential high-stakes suits against investors in major industries such as mining and oil exploration, potential lawsuits are by no means limited to these two industries. See, e.g., Alejandro González Raga, *Shut-Down of Joint Venture Feared* (July 5, 2002), available online at <http://www.cubanet.org/CNews/y02/jul02/09e2.htm> (last visited on July 10, 2004) (referring to the Diesel-International Economic Association, a joint venture with Canadian capital that runs an engine repair facility that neighbors consider to be a nuisance). Private parties in Cuba could go to court seeking damages or equitable relief from operations by others, including foreign investors, whose activities cause substantial and unreasonable interference with the use and enjoyment of plaintiffs' property.

92. Art. 71(c) of Cuba's Environmental Law gives a right of action for damages to anyone who is adversely impacted by an action or omission that affects the environment, but provides no mechanism for exercising that right and leaves it unclear who would have standing to bring any such suit. Ley del Medio Ambiente, art. 71(c); see also, Key Environmental Legislation at 346. On the other hand, the Civil Code provides general authority for a private party to seek damages from a tortfeasor whose actions have caused him harm. Civil Code, Art. 81-88 and 95-96. Thus, for example, Art. 82 states that he who unlawfully causes damages to another has the obligation to provide remedy for such damage. Art. 83 specifies that such remedy includes (a) restitution of property taken, (b) compensation for property damages, (c) indemnification for losses sustained, and (d) reparations for moral damages.

93. Similar arguments could be raised by U.S.-based plaintiffs to bring action in U.S. courts against current foreign investors for causes of action relating to environmental damage caused to their property in Cuba.

94. Prospects and Perils *at* 926.

95. *Id.*

96. *Id.* at 927.

97. *Id.* at 930.

98. *Id.* at 934.

99. See, e.g., Confederación Obrera Nacional Independiente de Cuba, "Report of the Violations of the International Labor Organization's Standards and Conventions by the Government of Cuba (June 2001).

100. ILO Convention 87, Art. 2, declaring that "[w]orkers and employers, without distinction whatsoever, shall have the right to establish and, subject only to the rules of the organization concerned, to join organizations of their own choosing without previous authorization," available online at <http://www.ilo.org/ilolex/english/convdisp2.htm>.

101. ILO Convention 95, Art. 9, prohibiting any "deduction from wages with a view to insuring a direct or indirect payment for the purpose of obtaining employment, made by a worker to an employer or his representative or to any intermediary," *id.*

One observer has denounced the structure of the employment relationship established by Cuba as constituting the crime of robbery,<sup>102</sup> and has argued that the Cuban workers, and by extension, a successor Cuban government acting in its *parens patriae* capacity, retain a right to seek damages from the foreign investor for its complicity in the crimes perpetrated by the predecessor Cuban government.<sup>103</sup> More specifically, it has been argued that the Cuban worker and successor Cuban government have a right to seek a civil action demanding the payment of back wages plus legal interest, at the rate applied by the international market for the type of work performed, plus any other punitive damages that are deemed appropriate.<sup>104</sup>

While, for the reasons discussed above, such suits by the Cuban Government or individual employees against current foreign investors may fail for legal and factual reasons, the fact that they are being proposed should give some pause to current foreign investors. The mere filing of lawsuits relying on the above theories of liability is likely to result in the imposition of significant legal costs to foreign investors in defending such lawsuits. Furthermore, the lawsuits may be filed (as is likely to be the case) during the early stages of the transition when the Cuban judiciary might still be highly politicized and not yet a truly independent arbiter of the rule of law. Such timing might result in the fate of these lawsuits being determined, not by enduring legal principles, but by the prevailing political winds at that particular moment in the transition.

## **POLICY PRINCIPLES AND LEGAL PROVISIONS THAT WOULD LEND PROTECTION TO FOREIGN INVESTORS AGAINST ADVERSE ACTIONS**

### **Effects of Existing Legislation**

Despite the inherent business risks with which current foreign investors are faced vis-à-vis their investments in Cuba, foreign investors could take some solace in knowing that there are several legal regimes in place with fairly well-defined rules that provide protection to their economic interests against state action.

First and foremost, current foreign investors are protected at the constitutional law level. Cuba's Constitution requires that any state expropriation of the assets of private parties be accompanied by the payment of adequate compensation.<sup>105</sup>

Secondly, current foreign investors are protected at the statutory level. Law 77 provides foreign investors with additional guarantees against uncompensated takings. Attempts to scale back the protections afforded by Law 77 are likely to run into roadblocks, not the least of which is Cuba's historical prohibition against *ex post facto* laws. Furthermore, even if a successor Cuban government were to claim, as a reason for prematurely terminating a contractual relationship with a foreign investor, that the foreign investor is in default of its contract with the Cuban government, Cuba's Civil Code contains an implicit provision for partial compensation in the event of a declared breach of contract.

Finally, current foreign investors are protected at the international agreement level as intended third party beneficiaries of the BITs that Cuba has negotiated with over sixty (60) different countries. Not only do these BITs generally provide foreign investors (whose home countries have entered into BITs with Cuba)

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102. Luzárraga at 251.

103. *Id.* at 252.

104. *Id.*

105. Although there is some debate as to which of Cuba's Constitutions (the 1940 or the 1992) will be considered to be legally in effect during a transition, the outcome of such debate is largely of little consequence on the issues of concern to current foreign investors given that both Constitutions provide protections against uncompensated takings.

with protections against outright expropriation of their productive assets, but they also provide international dispute resolution mechanisms for conflicts between foreign investors and the Cuban government—usually involving a neutral third party as the ultimate arbiter of the dispute.

Therefore, from a strictly legal standpoint, the rights of current foreign investors are reasonably well defined and protected under current Cuban law, and thus a successor Cuban government attempting to undermine these legal protections will be facing an uphill battle.

### Policy Principles

There is no doubt that negative sentiment exists, at least among some members of the Cuban American community and the U.S. Government, against foreign investors who do business in Cuba and thereby provide “badly needed financial benefit, including hard currency, oil and productive investment and expertise to the current Cuban Government.”<sup>106</sup> On the other hand, it is undeniable that foreign investors have made a significant contribution to the Cuban economy and, barring unexpected developments, are likely to do so up to and beyond the country’s transition to a free-market society.<sup>107</sup> Thus there is a substantial policy question whether the prosecution of potential government and private claims against the investors and the taking of other adverse actions is prudent against the possibility that such actions may quickly drive the investors out of the country.

Another policy question is whether taking actions against foreign investors will be consistent with Cuba’s anticipated need during the transition to stimulate foreign investment from the United States and other countries. Policies to create a positive foreign investment climate<sup>108</sup> may be frustrated if a percep-

tion develops that Cuba does not provide reliable protection to investors.

There is also the issue of respect for the rule of law and the extent to which activities which are lawful at the time undertaken can leave the actor open to reprisals later on if there is a change in law or policy. Foreign investors currently in Cuba have come into the country under the auspices of Law 77 and, in most cases, also under the protection of the BITs that Cuba has negotiated with their respective countries. Governmental action against these investors would arguably violate the BITs and might involve *ex post facto* punitive laws—an undesirable precedent for a country seeking to move towards democracy and respect for the rule of law.

### CONCLUSIONS

The ethics of investing in Cuba under current conditions and arguably lending support to the Castro regime are open to debate and such debate is likely to continue after Cuba makes a transition to a free-market society. From the legal and economic viewpoints, however, it appears that no solid bases exist for a transition government to take adverse action against current investors and doing so might be detrimental to the country’s economy and against public policy.

Individuals (former property owners, enterprise employees, and others) may have colorable grounds for taking legal action against current investors. Investors should be aware that they run the risk of multiple private lawsuits during the transition period. The outcome of such lawsuits is uncertain and may be dictated, not only by the laws in effect at the time, but by the political situation at the time the actions are brought. Investors need to take these risks into consideration when formulating strategies for business activities in Cuba under the current regime and after the transition.

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106. Helms-Burton Act, Section 301, Finding 7.

107. Prospects and Perils at 917-18; *see also* Perez 2002.

108. *See* Prospects and Perils at 938-44.