

III. FOREIGN INVESTMENT AND TRADE

(1) Framework for Foreign Direct Investment

1. The Foreign Investment Law, Law No. 861 of 19 July 1978, modified in 1983 by Law 138, governs foreign direct investment (FDI) in the Dominican Republic. Under the law, the Directorate of Foreign Investment (*Directorio de Inversión Extranjera*) evaluates and approves foreign direct investment projects. The Directorate, chaired by the Governor of the Central Bank, is composed of representatives of the Government and the private sector. The law also defines the sectors in which FDI is to be allowed and the extent of such participation. The Directorate may, however, at its discretion declare any sector closed to foreign investment. The law establishes rules on capital registration, reinvestment of profits, and repatriation of capital and profits; in addition, it regulates technology transfer and FDI in certain service sectors.

2. FDI in the free zones, covered by Law 8-90, does not require authorization from the Directorate of Foreign Investment or registration with the Central Bank.

3. FDI policy has been consistent with Dominican industrial policy (Chapter V(4)) in promoting export oriented activities while placing restrictions on development in other sectors of the economy. Priority, by law, is given to projects which promote exports and improve the balance of payments, such as tourism projects. In general, FDI is not allowed in areas of the economy where domestic investment is considered sufficient or in areas that are not considered as contributing to the economic development of the country. It is also restricted in specific sectors of the Dominican economy. FDI is prohibited in the following public sector services: drinking water, sewage, electricity, telecommunications and postal services. FDI is limited to 29 per cent of equity in activities reserved for national enterprises, such as the production of material and equipment related to national defence and security; advertising, broadcasting, newspapers, magazines, publishing and mass media communication; internal land transport, except when directly related to handling tradeables; internal air, maritime transport and cabotage; and forestry. In agriculture, animal husbandry, fishing, banking, insurance, and other financial institutions, in which national and mixed enterprises operate, participation of foreign equity is limited to a percentage not exceeding 49 per cent.¹ Thus, foreign financial institutions based in the Dominican Republic must be at least 50 per cent Dominican-owned. Citibank and the Bank of Nova Scotia are exceptions, since they were established before approval of the Foreign Investment Law.

4. In order to repatriate capital or profits, the initial investment must be registered with the Central Bank and receive approval from the Foreign Investment Directorate. Annual profits generated by foreign capital, duly registered with the Central Bank, may be remitted up to an amount equivalent to 25 per cent of the registered capital. Profits exceeding 25 per cent can be reinvested in tourism, export-oriented industries, and import-substituting industries, provided that they generate at least 30 per cent of domestic value added.² Invested capital can be remitted only up to 2 per cent annually and, cumulatively, up to 20 per cent of the original investment. According to the Government, annual

¹ A national enterprise is one with a minimum of 70 per cent Dominican ownership and management; a mixed enterprise has 51 to 70 per cent Dominican ownership and management.

²Article 20 of Law 861.

profit remittances cannot exceed the equivalent of 25 per cent of the net value of the original and additional investment plus reinvestment, minus repatriation, duly registered with the Central Bank.

5. Further restrictions apply to the acquisition of land, hiring of labour, and access to credit. Foreign companies cannot obtain domestic credit for a period greater than one year without prior approval from the Central Bank. The purchase of land by foreign persons or enterprises is limited to 5,000 m². Land purchases above this limit must be authorized by presidential decree. In relation to labour, at least 80 per cent of the employees hired by a foreign company must be Dominican nationals. Nevertheless, employment of foreigners above the maximum may be authorized if qualified Dominican personnel cannot be found. The company, however, has to train Dominican staff.

6. The restrictive nature of the Dominican Republic's foreign investment laws creates an incentive to circumvent the regulatory system. Much foreign investment, therefore, is not registered with the Central Bank and foreign investors use methods such as transfer pricing to repatriate profits. The Government, however, realizing the flaws of the Law and the importance of foreign capital for further development of the country, have recently drafted a new FDI law.

7. The draft law was approved by the Chamber of Deputies in January 1995 and was sent to the Senate in September 1995. The new law is aimed at attracting foreign capital by liberalizing the investment régime, and granting national treatment to foreign investors. It is expected that the law will eliminate restrictions on capital and profit remittances and permit these to be effected in freely convertible currencies without prior authorization. Registration requirements for foreign capital are to be maintained only for statistical purposes. Specific restrictions on FDI will, however, be maintained. Controls will apply to investment in public services, production of material and equipment related to national defence and security, agriculture, animal husbandry, fishing, banking, insurance, and other financial institutions.³ It is expected that the new law will replace a number of existing special laws, such as the Private Insurance Law, the Civil Aeronautics Law, the Law on the Protection and Development of the Merchant Marine, the Fishing Law, and the Mining Law, that impose restrictions on FDI in these sectors. If the draft FDI law is approved, restrictions to investment in other laws will be eliminated. Furthermore, any remaining restrictions to investment will apply equally to foreigners and nationals.

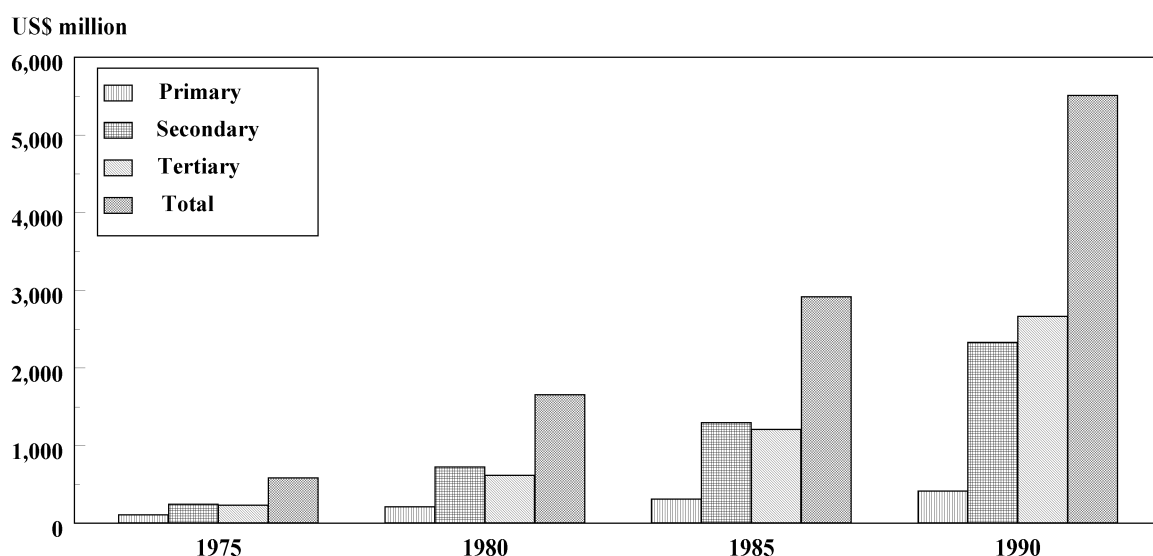
8. The Dominican Republic has signed a bilateral agreement for reciprocal protection of investment (*acuerdos para la protección de las inversiones*) with Spain to cover political and economic risks. Bilateral agreements with the United States, Canada, France, the United Kingdom, and the Republic of Korea are also being negotiated.

9. The Government's policy towards FDI, in fact, reflects the country's overall development strategy. On the one hand, import-substitution industries continue to be protected, while on the other export-oriented activities are promoted. This is accomplished by allowing reinvestment of profits only in import-substituting industries or export-oriented industries. The new FDI law, when approved, should make the Dominican Republic more attractive to foreign investors. The benefits to the Dominican Republic of a yet more liberal FDI law could be considerable, given that unexploited investment opportunities exist and could increase if privatization of State-owned enterprises were to take place.

³Government communication.

(2) Trends and Patterns in Foreign Direct Investment

10. Foreign direct investment in the Dominican Republic increased substantially from 1975 to 1990 (Chart III.1); cumulative inflows increased from US\$582 million to over US\$5.5 billion in the period.⁴ Historically, the sector that has attracted the greatest FDI has been the tertiary sector, followed by the secondary sector; FDI in the tertiary sector grew from 40 per cent in 1975 to 48 per cent in 1990, principally because of the growth in the tourism industry in the Dominican Republic. The share of FDI in the primary sector has become almost insignificant, decreasing from 18.2 per cent in 1975 to 7.5 per cent in 1990.

Chart III.1**Foreign direct investment cumulative inflows by sector, 1970-1990**

Note: Data calculated on the basis of cumulative flows of FDI since 1970. Data on inward investment reflect authorized investments, reinvestment of profits, transfer of technology and other forms of investments reported in the Foreign Investment Directory of the Central Bank of the Dominican Republic.

Source: UNCTAD, World Investment Directory (1994).

11. Developed countries accounted for almost 90 per cent of the cumulative gross inflows of the FDI to the Dominican Republic between 1970 and 1990 (Chart III.1). FDI originated mainly in the United States, Canada, and members of the European Union.⁵ Canada and the United States accounted for 80 per cent of total FDI in 1990. In the same year, ten of the seventeen largest foreign affiliates in the Dominican Republic were U.S. companies, investing mainly in the services sector. One Canadian

⁴U.N. (1994), p.27 World Investment Directory: Latin America and the Caribbean, Vol. IV, New York, NY.

⁵U.N. (1994), p.27 World Investment Directory: Latin America and the Caribbean, Vol. IV, New York, NY.

firm was involved in communications, while the remaining six were European enterprises investing in the manufacture of food, beverages, and chemicals, and in the exploitation of coal and petroleum.⁶

12. The Dominican Republic, with low-cost labour and export promotion schemes, has also attracted some FDI geared towards labour-intensive activities, associated with export-processing zones. For instance, in 1994, 52 per cent of the enterprises operating in the free zones were foreign; 46 per cent of them were U.S. companies.⁷ These data, however, are not reflected in the official Central Bank statistics because, as noted above, FDI in the free zones requires neither authorization nor registration. As these data should normally be taken into account when analysing FDI, only a partial picture of the patterns in foreign investment can be observed.

⁶U.N. (1994), World Investment Directory, Vol. IV.

⁷SEIC (1994). *Secretaría de Estado de Industria y Comercio, "Informe del sector de zonas francas correspondiente al 1994" Santo Domingo, República Dominicana, 1994.*