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AN EVALUATION OF WINDFALL TAX, AND THE IMPACT THAT IT COULD HAVE ON ZAMBIA VIS A VIS FOREIGN DIRECT INVESTMENT

BY

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A dissertation submitted to the University of Zambia in partial fulfillment of the award of Bachelor of Laws Degree

I CHILOMBO KAMBOLE MALAMA COMPUTER NUMBER 26102277 do hereby declare that this directed research is the result of my own investigation and research, no similar piece of work has previously been produced at the University of Zambia or any other institution for the award of Bachelor of Laws Degree. All other works referred to in this essay have been duly acknowledged. I bear absolute responsibility for all errors, defects or any omissions herein. No part of this work may be reproduced or copied in any manner without the consent of the author in writing.

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ABSTRACT

Sovereignty is a key entity of every State. With the status of sovereignty is the ability of a state to create laws that govern the affairs that occur within its territorial domain. A state thus has the right to dictate when and how its resources are to be used by its citizens, and even more so by foreigners wishing to gain some advantage from the use of the said resources. In Zambia one such resource is copper, a mineral heavily depended on by the nation's economy.

This paper examines the rights of Zambia as a sovereign entity to impose laws that will determine how its various industries are to be regulated with particular focus on the mining sector. This is in light of tax policies imposed, specifically windfall tax. The paper addresses the conditions under which the windfall tax was earlier imposed, subsequently removed, and examines the legal implications that may arise from the imposition of windfall tax again, in light of international responsibility and opinion. The paper does this by evaluating various international arbitral tribunal decisions.

The paper proceeds to address the role that foreign direct investment plays in the economy of a nation, the positive aspects as well as any negative ones. An examination of incentives offered to attract investors is reviewed, as well as an examination of the importance if any of attracting and maintaining foreign investment, in light of the fact that Zambia is a developing nation. Thus Zambians current legislative position in this regard is evaluated as well as an assessment of the history of the mining environment, to date.

The paper then concludes by giving a general conclusion of the dissertation, and then offers recommendatory policies that the country may adopt in order to improve its economic growth and prosperity.

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One of the happiest days of my life to date remains the day I got the news that I had been selected into the School of Law at the University of Zambia. Having been told even before I arrived at the University that the journey into the School of Law was the hardest, this joy was not unwarranted. However realisation after my journey through Law School has taught me that entering Law School is not even half the battle. The war begins once in Law school, and just like any war, the battles are long, hard and tiring, but once won the rewards are great.

The Lecturers have demanded nothing but the best from me, and though it has taken me nearly the end of my University journey to realize, this has been to groom me for the legal family, society, and the world at large. To them I say thank you. More so to my supervisor Mr. Sangwani Patrick Ng'ambi for being the most helpful and invaluable mentor a student would be privileged to have. To you I say, keep up the good rapport with your students, for they appreciate it, and you, the more for it.

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This work is in honor of all of you.

DEDICATION

This paper is dedicated to my parents Rhoda and Hans Malama who have always gone more than the extra mile for their daughter.

Glossary of Acronyms

FDI: Foreign Direct Investment

MNC: Multinational Corporation

ZDA: Zambia Development Agency

KCM: Konkola Copper Mine

ZRA: Zambia Revenue Authority

STATUTES

Zambia Development Agency Act No 11 of 2006.

Mines and Minerals Development Act No 7 of 2008.

CASES

SS Wimbledon Case [1923] P.C.I.J (Ser. A) No. 1

AGIP v Congo, Award 30, November [1979], 1 ICSID Reports 321

Texaco Overseas Oil Petroleum Co. /California Asiatic Oil Co. v Libya, 17 I.L.M [1978]

Saudi Arabia v Arabian American Oil Company, 27 I.L.R [1963]

LIAMCO v Liberia, 62 ILR 141

AMINOIL v Kuwait 21 ILM [1978] 1

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CHAPTER 1

FOREIGN DIRECT INVESTMENT AND WINDFALL TAX; A BRIEF ZAMBIAN HISTORY

1.0 INTRODUCTION

Zambia and many other developing countries world over strive to ensure that there is investment in their countries so as to develop their economies. They encourage investment by offering attractive incentives to investors with the motive of benefiting economically and in many other ways. As a result of the potential role that foreign direct investment (FDI) plays in accelerating economic growth, many developing countries and Africa in particular seek such investment in order to boost their development efforts.[1]

One of the key areas in which Zambia benefits from foreign direct investment is in the mining sector, particularly copper mining; an area in which the Zambian economy is heavily dependent. In May 2006, the prices of copper increased affectedly,[2] and the Government in a move to benefit from this increase sought to reconsider the preferential tax regime that foreign mining companies had previously enjoyed. This was ostensibly to ensure that the Zambian public benefited from the high copper prices; which they otherwise would not have.[3]

Thus in 2008 the Government of Zambia introduced a windfall tax on base metals at a minimum rate of 25%. In addition to other tax rates introduced, the windfall tax was designed to bring in additional revenue to the government from the high copper price.[4] This move resulted in a clash between the mining companies and the Government, with the mining companies claiming that Zambia is not the only country looking for Foreign Direct Investment, hence unless we give investors favorable incentives, they will go to other more attractive business destinations and carry their investment with them. The mining companies further argued that windfall taxes would destroy any chances of exploration activities, which are pertinent for growth of the mining

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[1] S. I. Ajayi, FDI and Economic Development in Africa. Paper presented at the ADB/AERC International Conference on Accelerating Africa's Development Five years into the Twenty-First Century, Tunis, Tunisia November 22-24, 2006.
[2] London Metal Exchange http://www.lme.co.uk/copper Accessed on 20th December 2010.
[3] S.P Ng'ambi, Stabilization Clauses and the Zambian Windfall Tax Zambia Social Science Journal (2010) Page 109
[4] C. Mfula, Zambia Needs Stable Mining Laws to Attract Investment Lusaka. Reuters. http://www.postzambia.com/post-read-article Accessed on 20th December 2010.

industry, as well as undermining the effect of the stabilisation clauses which had been included in the concession agreements between the government and the mining companies.[5]

Following these protests from mining companies, the government removed the windfall tax- a move met with different reactions from some stake holders on one hand, and the mining companies on the other, with the former side calling for its reintroduction. As was stated then by the Finance Minister, Situmbeko Musokotwane in a bid to justify the removal of the windfall taxes, saying although the price of copper had risen, the government would not bring back the high mining taxes it scrapped because that would neither be in the interest of the country nor the investors.

> "If we impose tax on revenue on old mines they will end up closing and we don't want to head in that direction. We don't want to create job losses..."

He added that foreign investors need not be skeptical over Zambia's mining prospects because the country realised attracting Foreign Direct Investment (FDI) was key to development.[6] However, the stakeholders' main grievance is that it is unfortunate that the government has continued allowing the mining sector to extract copper for free seemingly ignoring the fact that this is a depleting resource that accounts for about 80 per cent of the country's economic activity.[7]

Regard must be had however to the incentives offered to investors to begin with, in order to attract them to invest in the country as contained within the concession agreements. These include stabilisation clauses ranging for different periods. Stabilisation clauses essentially constitute a promise on the part of the host government not to amend its laws in a way that adversely effects the economic rights contained within that particular concession agreement. This meant therefore that even if the Government amended its national laws, those new laws should not, in theory, apply to the aforementioned concession agreements.[8] Stabilisation clauses essentially act as a lure to foreign investors, enticing them to bring their investment into the country at a lower tax rate, which is granted for a grace period, if you will, that enables the investors to stabilise financially in their particular field of investment.

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[5] C. Mfula, Zambia Needs Stable Mining Laws to Attract Investment
[6] C. Mfula, Zambia Needs Stable Mining Laws to Attract Investment
[7] C. Mfula, Zambia Needs Stable Mining Laws to Attract Investment
[8] S.P Ng'ambi, Stabilisation Clauses and the Zambian Windfall Tax

1.1 STATEMENT OF PROBLEM

Developing countries see FDI as being crucial to their development mainly because it provides required capital for investment, generates employment and acts as an aid to local firms by adopting more resourceful technology. Apart from facilitating capacity building in the host country, it is usually hoped that access to foreign markets will undoubtedly improve the integration of host country into the global economy and result in economic growth.[9]

The common sense result of such happenings should be the economic growth of the host country. This however does not happen. In most developing countries and indeed Zambia, when the multinational enterprises acquire their profits, the capital earned hardly ever remains home as the bulk of it is externalized[10].

Clearly then, a clash, if you will, arises between the interests of government to attract foreign investment, and the policies implemented to actually benefit from that investment because it can be argued that so far, these benefits, for example stabilisation clauses, offered to foreign investors are just colorful glosses enticing the host to open their doors to investment not knowing that the main aim is to make quick profit and leave immediately after their tax havens expire.[11] It is then imperative that policies are introduced that attract foreign direct investment, but maintain the States sovereignty, and ensure that the host nation accrues benefits. There is thus a need to consider new policies and laws which both effectively attract investment and benefit the host country.

1.2 OBJECTIVES

1.2.1 GENERAL OBJECTIVE

This paper intends to show the effect that stabilisation clauses have on the sovereignty of a state; the legal impact that windfall tax has on the said stabilisation clauses; and what effect this has on foreign direct investment. This paper will also propose a legal framework that strikes a balance between the commercial rights of the investor and the sovereign rights of States.

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[9] S. I. Ajayi, FDI and Economic Development in Africa.
[10] S.P. Ng'ambi, Is Zambia fully benefiting from Foreign Direct Investment? Commerce Gazette. May/June 2009. Page 6
[11] K.Wishimanga, The Regulation of Foreign Direct Investment Towards Economic Development Obligatory Essay submitted to the School of Law in partial fulfillment of the award of the Bachelor of Laws Degree 2009/10

1.2.2 SPECIFIC OBJECTIVES

1) To clearly examine the effects of windfall tax on stabilisation clauses, and on the sovereignty of a State, with regards the right to amend its laws without prior consent of the investor.

2) To advocate for clarity and a balance of policies and laws addressing competing interests of foreign investors, and the rights of a sovereign state to benefit from this foreign investment.

1.3 RATIONALE AND JUSTIFICATION

Following the global economic meltdown of 2009 now more than ever before, countries; especially least developed countries are relaxing their already weak laws in order to attract investors so as to counter the effects of the crisis. An example of this maybe said to be the abolition of windfall taxes and a replacement with a formula that is slated to regulate the amount of taxes that mining firms are required to pay in accordance with the profits that they make.[12] As a result of this, the least developed countries like Zambia are being exploited and their sovereignty compromised.

In this regard, it is imperative to note the impact that the reintroduction of windfall tax would have, in order to protect the mining sector of the country which accounts for up to 80% of the nation's economy,[13] but also imperative to refrain from disheartening investors wishing to trade in this area.

1.4 RESEARCH QUESTIONS

In order to address the above issues, the paper will have to ascertain the answers to the following questions;

a) Without windfall tax, is the host country fully benefiting from FDI in the mining sector?
b) What is the legal impact of stabilisation clauses in light of State sovereignty?
c) How can certainty be assured to investors with the existence of the state sovereignty principle?

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[12] K.Wishimanga, The Regulation of Foreign Direct Investment Towards Economic Development
[13] C. Mfula, Zambia Needs Stable Mining Laws to Attract Investment

d) How can a balance of the two interests (foreign investors and the State) be achieved in this sector?

1.5 METHODOLOGY

This research will be a qualitative one which will include desk research and field investigation in the form of interviews with relevant officials from the Zambia Development Agency. Secondary data in form of books, journals, scholarly articles as well as the internet will be consulted with a view to disseminating current information.

1.6 KEY DEFINITIONS

Although the key terms are to be expanded on and evaluated in depth as the essay progresses, some terms that will be frequently encountered and therefore need to be understood in the concept within which they are to be used in the essay are defined as follows:

DEVELOPING COUNTRY

These are present countries of Asia, Africa, Middle East, Latin America, East Europe and former Soviet Union characterized by low level of living, high rates of population growth, low income per capita and generally economic and technological dependence on developed countries.[14]

FOREIGN DIRECT INVESTMENT

The term Foreign Direct Investment has defied a singular definition but many of the definitions share common characteristics. The Zambia Development Agency Act[15] defines foreign investment as investment brought in by an investor from outside Zambia and further defines a foreign investor as a person who makes direct investment in the country and who in the case of a natural person is not a citizen or permanent resident of Zambia and in the case of a company is incorporated outside Zambia.

The World Trade Organisation defines FDI as what occurs when an investor based in one country (the home country) acquires an asset in another country (the host country) with the intent to manage that asset.[16] It will be noticed that in most instances, the investor and the asset being

[14] M. Todaro, S. Smith, Economic Development. 8th Ed. (India: Dorling Kindersley, 2003). p. 826
[15] Zambia Development Agency Act, No. 11 of 2006
[16] http://www.wto.org. Accessed on 28th November 2010

managed abroad are business firms and the investor is typically referred to as the parent firm and the asset as the affiliate or subsidiary.[17]

In summation, FDI is the relation that exists between a parent business enterprise and its foreign affiliate[18] which together comprise a Multinational Corporation. The main or primary purpose of the parent enterprise through its foreign direct investment effort is the exercise of substantial control over the foreign affiliate company.[19] FDI is generally given differential treatment because the foreign investor will move resources from his home state which resources may have been used by that home state and as such, it is justified that such investments are protected.[20]

The essay will therefore incorporate the above characteristics into a definition to be used as follows, FDI is in essence, what arises when an investor acting through a parent business enterprise sets up an associate enterprise in another country, collectively referred to as a Multinational Corporation, with the intent that the parent enterprise controls the activities of the foreign associate enterprise.

ECONOMIC GROWTH/DEVELOPMENT

Economic development is a multifaceted term with no precise definition meaning different things to different people depending on the region.[21] A definition that will be referred to in this paper and one that is accepted as encompassing many factors that are associated with this term is that; economic development is a concerted effort on the part of the responsible governing body in a city or county to influence the direction of private sector investment toward opportunities that can lead to sustained economic growth. Sustained economic growth can provide sufficient incomes for the local labor force, profitable business opportunities for employers and tax revenues for maintaining an infrastructure to support this continued growth.[22]

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[17] http://www.wto.org.
[18] http://www.economywatch.com. Accessed on 14th December 2010.
[19] http://www.economywatch.com
[20] M. Sornarajah, The International Law on Foreign Direct Investment. 2nd Ed. (Cambridge: Cambridge University Press, 2009) Page 8.
[21] http://www.wisegeek.com. Accessed on 14th December 2010.
[22] D. Lal. Development Economics. (Vermont: Edward Elgar Publishing Company, 1992) Page 1192.

STABILISATION CLAUSES

These are clauses inserted into contracts that essentially constitute a promise on the part of the host government not to amend its laws in a way that adversely effects the economic rights contained within a particular concession agreement entered into with a foreign investor. In other words, even if a Government amends its national laws, those new laws should not, in theory, apply to the concession agreements.[23] Stabilisation clauses attempt to ensure that future changes in the legislation of the host state do not vary the terms of the contract on the basis of which entry is made. They essentially do this by "freezing" the law so that future changes in the law will not affect the rights contained in the contract.[24]

WINDFALL TAX

Although to be addressed in greater detail in proceeding chapters, due to its great relevance to the issues at hand, windfall tax will be given an albeit brief but precise definition to better assist in an understanding of the issues at hand. Windfall tax can be defined as the tax levied by governments against certain industries when economic conditions allow those industries to experience above average profits. Windfall taxes are primarily levied on the companies in the targeted industries that have benefited the most from the economic windfall.[25]

SOVEREIGNTY

Like some of the other concepts encountered above, sovereignty is one eluding one definite definition. The essay will at the moment adopt the definition offered by the the representative of Morocco at the UN debates over Cyprus[26] who contended that; the concept of sovereignty must at the very least include the total freedom of a free and independent country to be the sole architect of its constitution and to ensure that its content reflects, in the best possible way, the rights and guarantees of communities and private citizens alike – this of course in the absence of any kind of constraint or interference from abroad.

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[23] S.P Ng'ambi, Stabilisation Clauses and the Zambian Windfall Tax
[24] S.P Ng'ambi, Stabilisation Clauses and the Zambian Windfall Tax
[25] Investment Dictionary. http://www.answers.com/topic/windfall-tax-1 Accessed on 24th December 2010.
[26] U.N. SCOR, 19th Sess., 1097th mtg., at 4, U.N. Doc. S/PV. 1097 (1964) as cited in S.P Ng'ambi. Stabilisation Clauses and the Zambian Windfall Tax. Zambia Social Science Journal (2010) pp107-117

1.7 CONCLUSION

After giving a brief background of the different attitudes towards windfall tax in general, the paper will now proceed to analyze the possible impact that the re-introduction of windfall tax would have on the Zambian economy, with particular emphasis on the importance of foreign direct investment especially in the mining sector. It will examine stabilisation clauses in concession agreements and their legal effect on a host State's sovereign right to amend its laws without the prior consent of the investor. Of particular interest is whether the Zambian government is precluded from unilaterally amending its tax laws contrary to stabilisation clauses contained within the concession agreements[27] and what effect this has on foreign direct investment and in essence the economic development of Zambia, bearing in mind that Zambia is a developing country.

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[27] S.P Ng'ambi, Stabilisation Clauses and the Zambian Windfall Tax

CHAPTER TWO

FOREIGN DIRECT INVESTMENT AND ECONOMIC DEVELOPMENT

2.0 INTRODUCTION

As defined, Foreign Direct Investment (FDI) exists when an investor acting through a parent business enterprise sets up an associate enterprise in another country, collectively referred to as a Multinational Corporation, with the intent that the parent enterprise controls the activities of the foreign associate enterprise.[28] This chapter will consider the aims and benefits of foreign direct investment especially with regard to the host country, as well as the correlation of FDI to economic development. In order to ascertain this, the liability of the Multinational Corporations towards the host country will be ascertained. The duty of the host country to the investors will also be examined in light of existing legislation.

2.1 AIMS AND BENEFITS OF FOREIGN DIRECT INVESTMENT

Due to its nature, FDI is generally given varied treatment because the foreign investor will move resources from his home state which resources may have been used by that home state and as such, it is justified that such investments are protected.[29] The question that may arise from this is why countries need to engage in FDI. What in essence are the aims of FDI and the benefits?

The potential contribution of FDI to host countries development was emphasised at the UN Conference on Financing for Development in Monterrey, Mexico in 2002[30], highlighting the ability of FDI to transfer knowledge and technology, create jobs, boost overall productivity, enhance competitiveness and entrepreneurship, and ultimately eradicate poverty through economic growth and development. Governments across the world have liberalised capital controls, often coupled with financial incentives such as tax holidays and stability clauses in the hope of attracting FDI. However, the relationship between FDI and sustainable development will vary across sectors and institutional conditions of the host country.[31]

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[28] http://www.wto.org.

[29] M. Sornarajah, The International Law on Foreign Direct Investment. Page. 8

[30] United Nations (UN). 2002. Final outcome of the International Conference on Financing for Development. (New York: UN.) http://www.un.org/esa/ffd/0302finalMonterreyConsensus.pdf Accessed on 23rd January 2011.

[31] D. Haglund, Regulating FDI in weak African States : a case study of Chinese copper mining in Zambia. Journal of Modern African Studies (Cambridge: Cambridge University Press, 2008) p.547-575.

FDI could therefore greatly assist the economies of developing nations. In order for a nation to develop, it needs capital and FDI is one way in which this capital may be obtained. Multinational Corporations (MNC's) are the main channel through which investment is brought to Africa. There are a number of reasons for investing by MNCs in developing countries, and these include safety in the host country, creation of profit when the host country is productive, and attraction of market for the said production. Other reasons are cheap labor, adequate resources, large markets, political stability and low risks in order to obtain the said profit. Developed countries therefore consider Africa as conducive for investors to operate their activities due to low production costs and ready markets for the produced goods.[32]

As established, a host country whenever it attracts FDI is sure to amass a number of benefits which may ultimately lead to economic growth and development of that country.[33] The benefits accruing to host countries will now be considered in detail.

2.1.1 Stimulus of the Domestic Economy

FDI acts as a stimulant to the host's economy because national economies are set to benefit from FDI in that it contributes to Gross Domestic product (GDP), Gross Fixed Capital Formation (i.e. total investment in a host economy) and balance of payments. Branches of MNCs which bring the vast portion of FDI are estimated to produce around a third of total global exports.[34] However, it must be noted that the impact of FDI will largely depend on the conditions of the host economy, such as the level of domestic investment or savings, the mode of entry and the sector involved, as well as a country's ability to regulate foreign investment. FDI will also stimulate the economy in relation to foreign participation in the privatisation of government-owned enterprises.[35]

2.1.2 Competition

When MNC'S enter the market in a particular field, the result is that they bring with them an aura of competition for the domestic firms. Further, entry by MNCs into local markets may

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[32] S. Venance, Role of Foreign Direct Investment (FDI) in Development of Low Developing Countries (LDC's): with experience from Tanzania. (Dar es Salaam: Muzumbe University. 2008).
[33] K.Wishimanga, The Regulation of Foreign Direct Investment Towards Economic Development
[34] United Nations Conference on Trade and Development, World Investment Report 1999.
[35] Organisation for Economic Co-Operation and Development, Foreign Direct Investment for Development: Maximising Benefits Minimizing Costs. (Paris: OECD Publication Service, 2002) Page 13.

reduce the concentration of firms in a particular market with the result that there is an increase in competition. The ultimate benefit of this to consumers is lower prices, perhaps a wider choice of goods and reduction in organizational inefficiencies.[36] The local firms will be coerced into producing better goods, and distributing them effectively in order to compete with the bigger firms, eventually this leads to economic advancement for the nation as the market base for local firms will grow.

2.1.3 Technological Spillovers

When MNCs invest in a particular country, the benefits include technological advantages that allow the MNCs to compete successfully with local firms. As a consequence of this, the host country firms have the potential to learn from the foreign affiliates. This is what is referred to as technological spillovers.[37] These spillovers have the ability to foster higher productivity for local firms and hence higher rewards. It is a common practice that parent companies support their foreign affiliates by ensuring adequate human resources and infrastructure are in place. With particular regard to undeveloped investments into new business sectors, there may indeed be a stimulation of new infrastructure development and technologies to host economies.[38]

Furthermore, MNCs have been said to improve labour skills through mechanisms such as on-the-job training, seminars, and formal education.[39] A major contribution by MNCs generally is the provision of technical assistance, training and other information to raise the quality of the suppliers' products. In this way, many local suppliers are assisted in modernising or upgrading production facilities.[40] These developments can also result in social and environmental benefits, but only where they spill over into host communities and businesses.[41] FDI provided in form of technology is best looked at in terms of the money that comes in a country through the

[36] A. Blomstrom et al, Multinational Corporations and Spillovers. Journal of Economic Surveys. (2) (2006) Page. 1-31.
[37] http://www.economywatch.com. Accessed on 14th December 2010.
[38] http://www.economywatch.com.
[39] L. Katerina et.al, Direct Investment and Economic Growth in Transition Economies. South Eastern Europe Journal of Economics (1). (2004) Page 97-110.
[40] Organisation for Economic Co-Operation and Development. Foreign Direct Investment for Development: Maximising Benefits Minimizing Costs. (Paris: OECD Publication Service, 2002) Page 13
[41] C. Dupasquier and P. N. Osakwe, Foreign Direct Investment in Africa: Performance, Challenges and Responsibilities. Geneva: United Nations Economic Commission for Africa. 2005. Page 15

investments which can be made use of by buying or importing technology from other countries. In this way FDI plays an important role in the context of economic development.[42]

2.1.4 Linkages

Related to the aspect of spillovers, is whether foreign firms develop linkages to local firms, which if strong imply that the employment effect of FDI is potentially large.[43] The interaction between local suppliers and the foreign affiliate may be one channel through which learning may take place as in the instance where foreign firms place higher demands on the quality and on timely delivery, forcing local suppliers to become more efficient. This will have the effect of benefiting locally owned downstream firms due to their efficiency.[44]

FDI in developing countries helps to boost the host country exports, which is the case where MNCs assist developing host countries to process and export locally produced raw materials, using their marketing skills, superior technology, and general know-how. Exports of local products are also facilitated through the MNCs distribution networks, and they often account for a significant share of host country exports.[45]

2.1.5 Social development

FDI has the effect, where it generates and expands businesses, of stimulating employment, raising wages and replacing declining market sectors. These investments may be helpful in assisting the host countries to set up mass educational programs which in the long run may help them educate the disadvantaged sections of the society. This form of assistance to these sectors is often provided by non-governmental organizations in the form of grants. It will also be seen that developing countries can actually tackle a number of healthcare issues with the help of FDI[46].

To speak of the benefits that accrue to the host country is real. However, the economic benefits of FDI do not accrue automatically.[47] As defined in the previous chapter, economic development is what occurs when there is a concerted effort on the part of the responsible governing body in a

[42] http://www.economywatch.com.
[43] K.Wishimanga, The Regulation of Foreign Direct Investment Towards Economic Development
[44] L. Katerina et.al. Direct Investment and Economic Growth in Transition Economies. Page. 97-110
[45] L. Katerina et.al. Direct Investment and Economic Growth in Transition Economies. Page. 97-110
[46] http://www.economywatch.com.
[47] K.Wishimanga, The Regulation of Foreign Direct Investment Towards Economic Development

city or county to influence the direction of private sector investment toward opportunities that can lead to sustained economic growth. Sustained economic growth can provide sufficient incomes for the local labor force, profitable business opportunities for employers and tax revenues for maintaining an infrastructure to support this continued growth.[48]

In order that the maximum benefits from FDI are reaped and hence for there to be economic growth, there is a requirement that a healthy enabling environment for business is present, which encourages both domestic and foreign investment, provides incentives for innovation and improvements of skills and contributes to a competitive corporate climate. Some factors holding back the full benefits of FDI in some developing countries include the level of general education and health, the technological level of host-country enterprises, insufficient openness to trade, weak competition and inadequate regulatory frameworks.[49] Other barriers that need to be considered that restrict FDI include the imposition of exchange controls, restrictions on repatriation of capital, and of great relevance to this essay, tax policies that victimize foreign firms.[50]

If the factors considered above are carefully studied by a host country the benefits of having such MNCs present will reap results that would eventually lead to the host country's economic growth. Having highlighted the fruitage of foreign direct investment it would seem imperative to address any hitch to this ostensible economic booster.[51]

2.2 FDI's IMPAIRMENT ON A HOST STATE

After reviewing the benefits of FDI, the general outlook would be that FDI should translate into net foreign exchange influxes that evolve into a host countries economic development; this however is not exactly the case.[52] MNC's engage in ingestion of reserves which eventually drains the resident pool and leaves other domestic entrepreneurs hanging, with no benefit. This situation is further agitated by foreign banks that have a tendency of conniving in the rationalization of financial resources and in most cases cater for the needs of the less risky

[48] D. Lal, Development Economics. (Vermont: Edward Elgar Publishing Company, 1992) Page. 1192
[49] Organisation for Economic Co-Operation and Development. Foreign Direct Investment for Development: Maximising Benefits Minimizing Costs. Page. 21
[50] J. C Baker, Foreign Direct Investment In Less Developed Countries The Role of ICSID and MIGA (Westport, Conneticut. 1999) Page 3-4.
[51] K.Wishimanga, The Regulation of Foreign Direct Investment Towards Economic Development
[52] S. Vaknin, Malignant Self Love - Narcissism Revisited. (Kumanovo: Euro College publications. 2007) Page 356.

segments of the business scene.[53] Looking at their appropriating ability, many international and intercontinental investors borrow money locally at advantageous interest rates in order to finance their ventures. This exercise may be said to generate partial rivalry with local firms with the effect that these local firms will be crowded out of the credit markets, displacing their investments in the process.[54]

Further it has been noticed that most foreign investors, with the first signs of contagion, unrest, and declining fortunes will flee the country to which they initially flocked. Additionally, once the MNCs gain their profits, the capital will hardly ever remain in the country as the bulk of it is usually externalized.[55] The situation is perpetuated by the tax havens or holidays that are offered to the MNCs resulting in loss of revenue, because the only avenue through which the host government could benefit from the capital inflows is left unutilized for half a decade after which many investors would have left the country.[56]

Considering the employment sector, FDI is seen as being the answer for most developing countries. The facts on the ground however demonstrate that this is not always the case; simply because foreign owned projects are capitally concentrated and labor effective. MNCs employ subcontractors and these do their job, frequently hauling entire workforces across continents. This has the result that local inhabitants rarely benefit and when they do actually find employment it is short-term and badly paid.[57] Indeed, even though MNCs do create jobs, in Zambia for instance, labourers are employed for trifling amounts. The facts on the ground actually point to the fact that sometimes even the most basic of jobs are offered to foreign workers regardless of the existence of a plethora of Zambian workers.[58] A further effect to the employment sector is that FDI may cause a shortage of labour in the government sector as many

[53] S. Vaknin. Malignant Self Love - Narcissism Revisited. Page 356.
[54] M. Todaro, S. Smith, Economic Development. 8th Ed. Page.674.
[55] S.P. Ng'ambi, Is Zambia fully benefiting from Foreign Direct Investment? Page 6.
[56] Organisation for Economic Co-Operation and Development, Foreign Direct Investment for Development: Maximising Benefits Minimizing Costs Page. 6
[57] S. Vaknin, Malignant Self Love - Narcissism Revisited Page 356.
[58] S.P. Ng'ambi, Is Zambia fully benefiting from Foreign Direct Investment? Page 6.

workers tend to move to MNCs looking for green pastures, where salaries are high compared to what is paid in the government.[59]

It has become common cause that these MNCs are funded by foreign loans that are hefty and as such may invest in modern machinery which does in fact encourage production of high quality products.[60] Within the local economies exist small scale and rural businesses of host countries that have less capacity to attract foreign investment and bank credit/loans, and because of this unfortunate fact, certain domestic businesses may either be forced out of business or made to use more informal sources of finance or simply, crowded out of business. A major concern raised among smaller developing countries or LDCs, is that a few, large developing country MNCs might become dominant players in their economies with the result that monopolization of that particular sector by the MNC.[61]

The foregoing seems to suggest that it is the downside of FDI that is prevalent in Zambia. One need not look too far in order to assume that there seems to be more pain and hardships caused to the Zambians in terms of FDI than there are benefits.[62] Zambia and many other developing countries remain poor and the economic and legislative environment needs to be examined to determine how these countries can begin to benefit fully from the international investment playing field.

2.3 OBLIGATIONS ON MULTINATIONAL CORPORATIONS[63]

MNCs are obligated by implication to promote economic development or to act in a manner that does not deter that development. There is a further implied obligation on the part of the home state to ensure that its corporate nationals, entering a treaty partners territory do not act in a manner that harms the economic development of the host state which may include avoidance of restrictive business practices and corrupt practices. Most investment instruments have as one of

[59] S.I. Ajayi, FDI and Economic Development in Africa. Accelerating Africa's Development Five years into the Twenty-First Century. 2006.
[60] S. Vaknin, Malignant Self Love - Narcissism Revisited Page 356.
[61] United Nations Conference on Trade and Development.World Investment Report. 2006. FDI from developing and transition economies: implications for development. *Statement by Supachai Panitchpakdi*, Secretary-General of UNCTAD
[62] K.Wishimanga, The Regulation of Foreign Direct Investment Towards Economic Development
[63] K.Wishimanga, The Regulation of Foreign Direct Investment Towards Economic Development

their spillover effects, the assumption that such foreign investment promotes economic development. For instance, bilateral treaties and regional treaties promoting investment contain in their preamble statements that, development comes about due to the investment flows.[64] In essence therefore MNC's have an implied obligation to ensure the expansion of the economic sector of the host country within whom they seek to establish their interest.

2.4 REGULATION OF FDI IN THE MINING SECTOR

2.4.1 CURRENT STATE OF AFFAIRS IN ZAMBIA

Zambia, a developing country has been ranked as the 11th largest producer of copper in the world with an excess of 2 billion tonnes of copper that still needs to be extracted. Copper production in Zambia accounts for 10% of its current gross domestic product (GDP) and 80% of its foreign exchange earnings.[65] Zambia's copper wealth is one of the most discussed and analysed sectors in Africa, especially with regards to international (mostly Chinese) involvement. Zambia has a long history of reliance on copper and has thus gained a strong sense of national identity from the copper sector. The area around the mines is referred to as the Copperbelt and the mining sector has been called both the "mother of Zambia" and its "economic lifeblood" because it has generated three-quarters of the country's foreign exchange earnings.[66]

After independence in 1964, Zambia was the third largest copper producer in the world, exporting more than 700,000 tonnes per annum and ranked among the most prosperous countries on the African continent. More than 35 years later, copper production has decreased to a mere 228,000 tonnes however, as did the overall state of Zambia's economy. Low copper prices in global commodity markets, minimal reinvestment in the mines and inefficiencies in the state-controlled enterprise that ran the copper mines all contributed to this abrupt economic decline.[67]

[64] M. Sornarajah, The International Law on Foreign Direct Investment Page. 8
[65] N. Nkonzo , 'Mining in Zambia: The mining of opportunities,' IMD (Interact Media Defined), 10 June 2010. http://www.interactmedia.co.za/index. Accessed on 24th January 2011.
[66] D. Walters, Examining Zambia's Copper industry www.consultancyafrica.com/index.php. Accessed on 24th January 2011.
[67] D. Walters, Examining Zambia's Copper industry

After the privatisation of the copper mines in April 2000, the downward trend in copper production and exports has reversed as a result of investment in plant rehabilitation, expansion, increased exploration, and high copper prices on the international market.[68] Copper production increased to 535,000 metric tonnes in 2007, but slumping copper prices in late 2008 put significant pressure on the mining companies and Government revenue. In mid-2009, the price of copper increased again and in July 2010, Zambia planned to increase copper production from 700,000 tonnes to 1 million tonnes over the next four years as investment in mining and copper industry, spurred by good policies, continued to flourish. This increase is an attempt to meet growing demand for copper, following increased investment in the industry, most notably from China.[69]

Since the privatisation of the mining sector, Zambia has reaped some rewards with international mining companies' involvement. In December 2009, China's investment in Zambia has exceeded US$ 1 billion and created approximately 15,000 local job opportunities. During 2009, the Zambian Development Agency asserted that Zambia's mining industry gained the most benefit from Chinese investment. Zambia's Development Agency also reported that the recent signing (March 2010) of an Investment Promotion and Protection Agreement (IPPA) with a Chinese private mining company - Zhougui Mining Group - will attract US$ 5 billion towards copper mining and other minerals in the North Western and Copperbelt provinces and employ more than 1,000 Zambians.[70]

However, while the privatised (and mostly internationally-owned) mines have recorded large profits, the Government of Zambia has acknowledged that revenue from copper as a proportion of Government income has been very low.[71] For the period 2002 to 2006, the Government received nearly US$ 752 million in various taxes from foreign investors holding large-scale mining licences. The Government earned about US$ 70 million from total copper sales of US$ 3 billion. The Institute for Security Studies (ISS) reports that the low revenues from copper sales

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[68] 'Zambia,' US Department of State website, 2010 http://www.state.gov/r/pa/ei/bgn/2359.htm. . Accessed on 24th January 2011.
[69] D. Walters, Examining Zambia's Copper industry
[70] T. Fourie, China-Zambia relations strengthen IHS Global Insight Southern Africa, 19 March 2010, http://www.ihsglobalinsight.co.za/News/news. Accessed on 24th January 2011.
[71] N. Simutanyi, Copper mining in Zambia: The Developmental Legacy of Privatisation ISS (Institute for Security Studies), July 2008, http://www.iss.co.za/uploads Accessed on 24th January 2011.

are partly a result of development agreements, which prescribe tax concessions for mining companies for periods ranging from 10 to 15 years, and a reduction in mineral royalty taxes from the statutory 3 percent to 0.6 percent, which is the lowest in the world.[72]

It is the aforementioned events that have seen the Zambian government reestablishing its legislation to attempt to cater for both Zambian priorities, and investor priorities in the foreign investment field. We proceed to examine the statutory position with regards foreign investors, the requirements they ought to satisfy, and the position with regards concession agreements.

2.4.2 CURRENT LEGISLATIVE FRAMEWORK AND INVESTMENT ENVIRONMENT

2.4.2.1 THE MINES AND MINERALS DEVELOPMENT ACT No. 7 of 2008

This is an Act to revise the law relating to the prospecting for, mining and processing of minerals; to repeal and replace the Mines and Mineral Act, 1995. Under Section 6 (1) of this Act[73], the following rights may be granted: (a) a prospecting licence; (b) a large-scale mining licence; (c) a large-scale gemstone licence; (d) a prospecting permit; (e) a small-scale mining licence; (f) a small-scale gemstone licence; and (g) an artisan's mining right.

Section 7(3)[74] qualifies this position to state that; a prospecting permit, small-scale mining licence, small-scale gemstone licence and an artisan's mining right shall not be granted to a person who is not a citizen of Zambia or a company which is not a citizen-owned company. It stands therefore that foreign companies wishing to obtain mining rights in Zambia, can only obtain; a large scale mining right, large scale gemstone right, or a prospecting licence.

The reason for this may be inferred from Section 25(3)[75] which provides that; an application for a large-scale mining licence shall include- (g) the applicant's proposal with respect to the employment and training of citizens of Zambia; (h) the applicant's proposals for the promotion of local business development outlining how the applicant intends to promote- (i) the participation of Zambian entrepreneurs in procurement and supply business opportunities with

[72] N. Simutanyi, Copper mining in Zambia: The Developmental Legacy of Privatisation
[73] The Mines and Minerals Development Act No.7 of 2008, Section 6(1)
[74] The Mines and Minerals Development Act No.7 of 2008, Section 7(3)
[75] The Mines and Minerals Development Act No.7 of 2008, Section 25(3)

the applicant; (ii) the setting up by Zambian entrepreneurs of import substitution, and repair and maintenance businesses locally; (iii) partnership between the Zambian entrepreneurs and foreign suppliers and contractors; and (iv) skills development to enable the Zambian entrepreneurs attain quality standards in contract works and supply.

Bearing in mind the advantages of FDI that had earlier been looked at in specification, technological spillovers, linkages, stimulation of the domestic economy, to mention but a few, it would appear that the drafters of the Act where trying to capture the essence of the advantages of FDI. By limiting the mining rights of foreigners to a large scale, the drafters ensured that more capital was brought into the country, and with it better job opportunities. As is noted in Section 26 (1)[76] The Director shall, in considering an application under Section 25, take the following into account (g) the size and nature of the proposed mining operations, and that the applicant's proposals for the employment and training of citizens of Zambia are adequate. The stimulation of the local economy would also benefit in that partnerships with foreign investors would see an exposure to exports as well as assistance in the improvement of the local enterprise as is shown in Section 25.

Likewise, under Section 13(1)[77] a holder of a mining right or a mineral processing licence issued under this Act, shall, in the conduct of operations under the mining right or mineral processing licence, and in the purchase, construction and installation of facilities, give preference, to the maximum extent possible to- (a) materials and products made in Zambia; and (b) service agencies located in Zambia and owned by Zambia citizens or citizen owned companies. (2) A holder of a mining right or mineral processing licence shall, in all phases of the operations, give preference in employment to citizens of Zambia to the maximum extent possible. (3) A holder of a mining right or mineral processing licence shall, in the mining operations, conduct training programmes, in consultation with the Minister, for the benefit of employees to enable the employees qualify for advancement.

The legislature recognized that FDI is a two way street, with investors coming into the country to make their profit, and thus likewise, the host country getting full benefits for use of their

[76] The Mines and Minerals Development Act No.7 of 2008, Section 26 (1)
[77] The Mines and Minerals Development Act No.7 of 2008, Section 13 (1)

resources. In Section 13, it is made mandatory by use of the words, shall, to the maximum extent possible, give preference to locally produced materials and products. In this way the local economy is stimulated because foreign investors are obligated to purchase and make use of locally produced goods when they are needed.

Having seen the hullabaloo that the earlier concession agreements and the imposition of windfall tax subsequently caused, Section 160[78] provides; A development agreement which is in existence before the commencement of this Act shall, notwithstanding any provision to the contrary contained in any law or in the development agreement, cease to be binding on the Republic from the commencement of this Act.

This section clearly then brings the legislative position today to be that all mining agreements, specifically the concession agreements entered into with foreign investors that included stabilisation clauses of up to 10-15 years as of 2008, when the Act was passed became non-binding upon the Republic of Zambia. Thus any future agreements are to be entered into based on the requirements of this Act, and as we now proceed to examine, the Zambia Development Agency Act.

2.4.2.2 THE ZAMBIA DEVELOPMENT AGENCY ACT No. 11 of 2006

Zambia offers a very liberal investment environment. Currently, FDI is governed by the Zambia Development Agency Act of 2006. This Act establishes the Zambia Development Agency. The Government actively seeks foreign investment through ZDA which was established in January 2007, by consolidating a number of trade and investment promotion entities into a one-stop resource for international investors interested in investing in Zambia. The ZDA board screens all investments for which incentives are requested and usually makes its decision within 30 days. The reviews appear routine and non-discriminatory, and applicants have the right to appeal investment board decisions. There is no distinction in Zambian law between foreign and domestic investors. Investors are free to invest in any sector of the economy and are entitled to incentives per the ZDA Act of 2006. In the privatisation process, foreign investors are eligible to

[78] The Mines and Minerals Development Act No.7 of 2008, Section 160

bid on state-owned companies. Non-Zambians may also invest in the Lusaka Stock Exchange without restriction and on terms comparable to those Zambians receive.[79]

The ZDA Act provides in Section 5(1)[80] as one of its functions to further the economic development of Zambia by promoting efficiency, investment and competitiveness in business and promoting exports from Zambia; and (g) formulate investment promotion strategies; (h) promote and coordinate Government policies on, and facilitate, investment in Zambia.

ZDA has a Board of Agency and under Section 17[81] it is mandated to promote private investment by- (a) taking measures and actions which help to create and maintain a predictable and secure investment climate; (b) encourage foreign investment, including the formation of strategic alliances with Zambian business enterprises; (d) encourage sector investment so as to promote foreign investment; (g) disseminate information on investment opportunities and business operational conditions in Zambia; (i) give development services to investors so as to assist in creating a responsive investment environment and information base to guide and encourage the flow of capital; and (j) endeavor to conclude investment promotion and protection agreements with prospective investors.

These sections clearly demonstrate that the role of ZDA in Zambia is centered around economic development of the country, which is then recognized to require foreign direct investment. The Board is mandated to provide a predictable and secure investment environment, further recognizing that a country that amends its laws at a whim that may detract from a prior investment agreement does not present itself as an attractive destination for foreign investment. However, it has also been said that although foreign investors are encouraged to commit to local participation, the Act does not stipulate any requirements for local content, technology transfer, equity, employment or use of subcontractors. The Act allows investors to repatriate any capital investments freely, repatriate profit, dividends, interest, fees. It also allows foreign nationals to transfer out wages earned in the country.[82]

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[79] 2010 Investment Climate Statement. Bureau of Economic, Energy and Business Affairs. March 2010
[80] Zambia Development Agency Act, No. 11 of 2006, Section. 5 (1)
[81] Zambia Development Agency Act, No. 11 of 2006, Section.17
[82] L. Muyoyeta, Foreign Direct Investment and the Fulfillment of Key Rights Social Watch Poverty Eradication and Gender Rights http://www.socwatch.org/node/12120 Accessed on 24th January 2011.

Having examined the current legislative framework governing foreign direct investment in the mining sector more specifically, it would appear that the legislature embraces the importance of Foreign Direct Investment, and seeks to find ways to increase its input in the Zambian economy. It would then follow that this maybe because FDI has played a key role in improving the Zambian economy. Whether this is the case remains a matter of key debate.

The Zambian community generally feels that the country has not really reaped too many benefits from international involvement in the country's copper sector. Instead, most of the potential benefits that existed turned into somewhat negative impacts, namely the reduced Government income from copper mining taxes and royalty taxes; the casualisation of labour as many local Zambians are only employed on a short-term basis; not to mention the flooding of Chinese labourers at Chinese-owned mines and mine safety problems that killed 49 miners in an explosion in 2005. Thus, the Zambian Government might need to re-evaluate its mining policies and legislation in order to garner the maximum benefits from the copper industry and create an enabling environment for those rewards to trickle down to the local population.[83]

Government on the other hand stands on the footing that FDI has long term benefits which Zambia in order to develop, needs. Their position remains that foreign investors need not be skeptical over Zambia's mining prospects because the country realizes that attracting Foreign Direct Investment (FDI) is key to development.[84]

2.5 CONCLUSION

The focus of this chapter has been the aims of FDI and the benefits to the host country. The benefits have been greatly highlighted as have the aims. The chapter has shown that there is potential by the host country to benefit from FDI because of spillovers in terms of technological transfer and linkages with regards improved labour and efficiency. It has been shown that FDI to prosper requires a certain favorable environment, which as the Zambian legislation pertaining to it has shown, has recognized and sought to implement.

[83] Zambia,' US Department of State website, 2010 http://www.state.gov/r/pa/ei/bgn/2359.htm Accessed on 24th January 2011.
[84] C. Mfula, Zambia Needs Stable Mining Laws to Attract Investment

Unfortunately, in spite of these benefits that accrue to the host country most countries still remain poor, Zambia notwithstanding, as FDI brings together with its benefits, certain negative connotations that the country greatly feels. The mining sector being a key player in the field of Zambia's economic success has been shown to require a great deal of FDI in order to function. Unfortunately, it is in this same sector that Zambia has had to revisit its tax requirements time and time again in an effort to capture a haven that benefits both investors and the local community. It is imperative therefore that a balance ought to be struck, between Zambia's wish to obtain FDI and its ability to benefit from the same at a maximum level, bearing in mind the sovereignty of the nation, and on the other hand, its obligations to the international community.

CHAPTER THREE
SOVEREIGNTY AND STABILISATION CLAUSES

3.0 INTRODUCTION

Scholars have doubted whether a stable essential notion of state sovereignty exists. Several definitions have been offered which will now be considered under this chapter, and the characteristics, assembled and analyzed to come up with a comprehensive understanding of the concept of state sovereignty. The view of the international community with regards stabilisation clauses and their effect on a sovereign host states right to amend its laws minus the prior consent of the investor will then be apprised. This view will then be related to the Zambian context in light of the windfall tax that was earlier imposed and subsequently removed, following protests from the mining community. A conclusion will then be drawn as to whether Zambia as a sovereign nation is better off developing economically with the imposition of windfall tax regardless of any prior investment agreements with foreign investors.

3.1 SOVEREIGNTY DEFINED

We may embark on the concept of state sovereignty by linking the concept of the state, with that of sovereignty. Sociologist, Max Weber famously defined the 'state' as:

> "a human community which within a defined territory successfully claims for itself the monopoly of legitimate physical force; and 'territory' it should be noted is a characteristic of the state."[85]

Another definition rendered is that the state is the political institution in which sovereignty is embodied.[86] The three attributes of the modern state including structure, legitimacy and spatiality can be discerned from these general definitions. A state must possess the structure by which to wield a monopoly of force (government), the legitimacy to use that force (sovereignty) and the spatial field on which to use force (territory).[87]

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[85] M. Weber, The Essential Weber: A reader, (London: Routledge. 2004) Page.131.

[86] Stanford Encyclopedia of Philosophy http://plato.stanford.edu/entries/sovereignty Accessed on 2nd February 2011.

[87] J. W. Donaldson, Marking Territory: demarcation of the DRC-Zambia boundary from 1894 to the present day, Thesis for the degree of Doctor of Philosophy (PhD) Department of Geography, Durham University June 2010.

As earlier stated in the first chapter, the representative of Morocco at the UN debates over Cyprus[88] contended that; the concept of sovereignty must at the very least include the total freedom of a free and independent country to be the sole architect of its constitution and to ensure that its content reflects, in the best possible way, the rights and guarantees of communities and private citizens alike – this of course in the absence of any kind of constraint or interference from abroad. In line with this, independence is defined as, the state of condition of being free from dependence, subjection, or control. Political independence is the attribute of a nation or state which is entirely autonomous, and not subject to the government, control, or dictation of any exterior power.[89]

With the above definitions ventured of an independent state in mind, Black's Law Dictionary 6th Edition,[90] defines the concept of sovereignty as; the supreme, absolute, and uncontrollable power by which any independent state is governed; supreme political authority; the supreme will; paramount control of the constitution and frame of government and its administration; the self-sufficient source of political power, from which all specific political powers are derived; the international independence of a state, combined with the right and power of regulating its internal affairs without foreign dictation. [...] The power to do everything in a state without accountability, to make laws, to execute and to apply them, to impose and collect taxes and levy contributions, to make war or peace, to form treaties of alliance or of commerce with foreign nations, and the like.

If sovereignty is a matter of authority, it is not a matter of mere authority, but of supreme authority. Supremacy is what makes the constitution of the United States superior to the government of Pennsylvania or any holder of sovereignty different from a police chief or corporate executive. The holder of sovereignty is superior to all authorities under its purview.[91]

Given the above analysis of a sovereign state, it would be safe to conclude that the notion of state sovereignty endows upon a state the power, the authority, the absolute intractable right to govern itself, within its territory, according to its own rules and legislation, to the exclusion of all others

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[88] U.N. SCOR, 19th Sess., 1097th mtg., at 4, U.N. Doc. S/PV. 1097 (1964) as cited in S.P Ng'ambi, Stabilization Clauses and the Zambian Windfall Tax, Zambia Social Science Journal (2010) pp107-117

[89] Black's Law Dictionary 5th Ed. http://www.hawaii-nation.org/sovereignty.html Accessed on 2nd February 2011.

[90] Black's Law Dictionary 6th Ed. http://www.hawaii-nation.org/sovereignty.html Accessed on 2nd February 2011.

[91] Stanford Encyclopedia of Philosophy

within the bounds of its own constitution, freely established. However, bearing in mind that a state exists as a member of an international community made up equally of other sovereign states, that in order to survive need communication links in matters of trade of goods, technology and services with one another, it would seem imperative then that each nation, as sovereign as it may be, takes into account its international relationship with its sovereign colleagues; which is then to be reflected in its national laws and policies.

3.2 STATE SOVEREIGNTY AND STABILISATION CLAUSES

The common means for conducting business in a host country is through investment contracts, which are commonly known as economic development agreements. Such agreements establish a delicate balance between the interests of the contracting state, which needs the technical know-how of foreign experts, and the interests of the foreign investor who is reluctant to take great risks without adequate measures.[92]

As a state is a sovereign entity, any activities occurring within its territory are governed by its domestic law; this includes any contracts that may be entered into between the government of that state, and any foreign investors. As such, when foreign investors enter into agreements with governments, there is no real guarantee that the host state will uphold the contractual obligations contained therein. This is because governments may change the law as and when they please to override the rights contained in investment contracts.[93] However, because of the very fact that the state enjoys sovereignty, the private contracting party has a legitimate interest in seeking legal guarantees. Thus, foreign investors in order to obtain sufficient protection against the risk of having their rights nullified and their contractual equilibrium disturbed as a result of the state's intervention, seek an effective system comprising a mechanism which provides sufficient protection against this risk.[94]

One technique to shield a foreign investor from the consequences of change in the host state's law is the insertion of a stabilisation clause into the investment contract. Under such a clause, the

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[92]M. Al-Saeed, Legal Protection of Economic Development Agreements_ *Arab Law Quarterly* Vol. 17, No. 2 (2002), Page 150.

[93] S.P Ng'ambi, Stabilization Clauses and the Zambian Windfall Tax

[94] M. Al-Saeed, Legal Protection of Economic Development Agreements, Page. 150

host state undertakes to have the investor unaffected by any subsequent changes of the local law.[95] In the case of LETCO v Liberia[96] the tribunal observed;

> "This clause, commonly referred to as a "stabilisation clause" is commonly found in long term development contracts and is the case with notification procedures of the Concession Agreement, is meant to avoid the arbitrary actions of the contracting government. This clause must be respected, especially in this type of agreement. Otherwise the contracting State may easily avoid its contractual obligations by legislation."

In essence therefore, stabilisation clauses are a promise on the part of the host government not to amend its laws in a way that adversely effects the economic rights contained within a particular concession agreement (development agreement) entered into with a foreign investor.[97] Governments that undertake to insert stabilisation clauses in their concession agreement consequently take on the obligation to adhere to those clauses.

The effect of this therefore is that even if a Government amends its national laws, those new laws should not, in theory, apply to the concession agreements. Stabilisation clauses where there are included in a development agreement endeavour to ensure that an investors rights are protected within the domestic sphere of a host state, by ensuring that future changes in the municipal law of the host state do not diverge from the terms of the contract on the basis of which entry is made, to the detriment of the investor.

Put differently, the parties' choice of law is specified also in terms of the chosen laws evolution over time. The rules of law agreed to by the parties are only those enacted up to the date of the contract. In order to immunize stabilisation clauses, against their abrogation by subsequent national law of the host state, it is sometimes said that they are governed by international law, even if otherwise the chosen law is domestic law. The over whelming weight of opinion is that those clauses are binding and must be upheld by arbitral tribunals.[98]

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[95] C. Schreuer, The ICSID Convention: a commentary on the Convention for Settlement of Investment Disputes http://books.google.co.zm/books Page. 593 Accessed on 24th February 2011.
[96] Award 31, March 1986, 2 ICSID Reports 346.
[97] M. Al-Saeed, Legal Protection of Economic Development Agreements Page. 150
[98] C. Schreuer, The ICSID Convention: a commentary on the Convention for Settlement of Investment Disputes Page. 593.

3.3 INTERNATIONAL APPROACH TO STABILISATION CLAUSES

The concept of state sovereignty as important as it maybe, and as much as it may grant a state absolute power within its own territory, seems nevertheless to be curtailed by international responsibilities. In the SS Wimbledon Case[99] the Permanent Court of International Justice held that the right of entering into international engagements is an attribute of State sovereignty. Therefore any limitations a State accepts when it enters into a treaty cannot later then be renounced as an encroachment of their sovereignty.[100]

Numerous arbitral awards have stood on the footing that stabilisation clauses by their very nature prohibit a host nation from amending its laws unilaterally in a way that may have an antagonistic effect on the rights of the investor as contained within an investment contract. To begin with, in AGIP v Congo[101]the chosen law was Congolese law supplemented by international law. The agreement between the parties contained clauses protecting the investor against certain subsequent changes of Congolese law. The tribunal in this case held;

> "These stabilisation clauses which where freely entered into by the Government do not affect the principle of its legislative and regulatory sovereignty since it retains both with respect to those, whether nationals or foreigners with whom the Government has not entered into such undertakings, and that, in the present case they are limited to rendering the modifications to the legislative and regulatory provisions provided for in the Agreement unopposable to the other contracting party. In consequence, the application of international law in the present case does not require an examination of the other possible violations of its rules with which AGIP reproaches the government. [...] It suffices to concentrate the examination of the compatibility of the nationalisation[102] with international law on the stabilisation clauses. It is indeed in connection with these clauses that the principles of international law suffices to complete the rules of Congolese law." [103]

This decision shows not only a general deference to the stabilisation clauses but also a willingness to regard them as part of international law, thereby shielding them against unilateral abrogation through host state legislation. This is not a prohibition to change the law, but merely a promise not to apply any changes vis-a-vis the investor or a promise to compensate the investor

[99] [1923] P.C.I.J. (Ser. A), No. 1
[100] S.P Ng'ambi, Stabilization Clauses and the Zambian Windfall Tax
[101] Award 30, November 1979, 1 ICSID Reports 321/2
[102] As was the issue in this case.
[103] M. Al-Saeed, Legal Protection of Economic Development Agreements Page. 150

for any adverse consequences of such a change.[104] Further, the very fact that a State freely enters into the agreement that contains the stabilisation clause means it is well aware of the implications of that agreement and should therefore not be allowed to derail from its commitments.

This position was recapped in the case of Texaco Overseas Oil Petroleum Co. /California Asiatic Oil Co.v Libya[105] where the arbitrator there stated that the arbitral clause did not in principle impair the sovereignty of the State (Libya) because all its sovereign powers still remained intact and could still be exercised on persons other than those to whom it owed contractual obligations. Thus in respect of the international law of contracts a nationalisation cannot prevail over an internationalised contract that contains stabilisation clauses entered into between a State and a foreign private company. The situation could be different only if one were to conclude that the exercise by a State of its right to nationaliee, place that State on a level outside of, and superior to the contract and also to which is beyond the scope of any judicial redress or criticism.

This position would clearly not suffice. Recalling the essence of sovereignty to be that of a States freedom to do as it pleases within the confines of its territory, according to this case however, this does not mean a country may not be bound by contractual obligations or repercussions for breach of those obligations. In essence this does not override the States sovereignty, rather, it recognises the State as being a sovereign entity by acknowledging its right to exercise its sovereignty over all others persons to whom it does not owe a duty it itself acquiesced to by entering into the agreement to begin with.

The decision by the arbitrator in the Texaco Overseas Oil Petroleum Co. /California Asiatic Oil Co.v Libya case has been construed as having the effect that the stabilisation clause internationalizes the contract, and this in turn has the effect of putting both parties to the contract, as equals, with the host state bound by the guarantees offered to the investor.[106] Where parties are equal therefore none can claim to have the authority over the other. Consequently, none can then alter the terms of an agreement between the parties minus the consent of the other, without opening themselves up to certain repercussions like actions for breach of contract. Where this is

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[104] C. Schreuer, The ICSID Convention: a commentary on the Convention for Settlement of Investment Disputes Page. 593.
[105] 17 I.L.M [1978] 1
[106] B.T.M Coale, Stabilization Clauses in International Petroleum Transactions Denver Journal of International Law and Policy as cited in S.P Ng'ambi, Stabilization Clauses and the Zambian Windfall Tax Zambia Social Science Journal.2010. Page. 111.

on an international level, it follows therefore that the severity is even fiercer than an action between two domestic parties, as this impact is felt at a nationwide scale.

In Saudi Arabia v Arabian American Oil Company[107] the arbitral tribunal stood on the premise that;

> "By reason of its very sovereignty within its territorial domain, the State possesses the legal power to grant rights by which it forbids itself to withdraw before the end of the concession."

The question posed in regard to this by Weil[108] was, what would be the point of having a state renounce the exercise of certain of its prerogatives of sovereignty if, at the first difficulty, that state could free itself from this promise by invoking precisely these same prerogatives? He added that, in subscribing to a protection clause, the host government creates to the benefit of the other party a legitimate expectation which the government may not subsequently frustrate without infringing the principle of good faith.

Principally, what the arbitral tribunal in the Saudi Arabia v Arabian American Oil Company Case and Weil were saying is that an entity by the very fact that it is a sovereign, acquires the ability to contract at an international level with persons from other (equally) sovereign entities. Where a State invokes its sovereignty to enter into this contract, it then accepts to give up certain attributes of its sovereignty, (like the ability to change its laws as it pleases to the detriment of the investor) in order to fulfill its contractual obligations. Would it then be practicable for the State to again use its very sovereignty to desist from carrying out its duties as contained in the contract? It would seem that if the answer was in the positive it would defeat the whole purpose of having used its sovereignty to enter into the contract in the first place, as well as having agreed to give up certain attributes of the sovereignty to begin with.

Thus where an investor contracts with a State, the investor essentially has an authentic expectation that the rights and duties bestowed upon both parties by the terms of the contract will be adhered to. Accordingly where a State willingly detracts from its obligations, as Weil states, then the State is in breach of the principle of good faith. It is on such a premise that arbitral

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[107] 27 I.L.R 117 [1963]

[108] P. Weil, "Les clauses de stabilization ou d'intangibilite inserees dans les accords de development economique" in Melangues offerts a Charles Rousseau. (Paris: A Pedone. 1974) as cited in S.P Ng'ambi, Stabilisation Clauses and the Zambian Windfall Tax Zambia Social Science Journal.2010. Page. 109.

tribunals do not respond too considerately to the argument of state sovereignty as a means of qualifying a breach of a protection clause.

Although by no means exhausted, the above cases have shown that the majority of arbitral tribunal decisions stand on the footing that stabilisation clauses protect the rights of the investor and should be left unaltered by any acts of a host state that may prove detrimental to the rights of the investor.[109]

Ii is necessary however to also reflect upon the decision of the in the case of AMINOIL v Kuwait[110] where the tribunal took a somewhat different, but neutral view towards the rights of an investor and those of a State as contained in an agreement bearing a stability clause. In this case a concession agreement granted to an American oil company for a 60 year period contained a stabilisation clause precluding Kuwait from altering the agreement unless by joint agreement with the company. Before the lapse of the 60 year period, the Kuwait Government negotiated changes to the agreement with AMINOIL who gradually agreed to an imposition of higher taxes. However, when oil prices quadrupled, despite the increase of taxes, the Government issued a decree terminating the concession agreement and nationalising AMINOIL's property.

In its defence, Kuwait alleged that nationalisation had not specifically been mentioned in the stabilisation clause i.e. the stabilisation clause did not specifically state that the Kuwait government could not nationalise the assets of AMINOIL, and admitted to the fact that they had to compensate the company. The arbitral tribunal opined that; although there was a stabilisation clause between the Kuwait government and AMINOIL, these stabilisation clauses in themselves did not amount to an express agreement not to nationalise.

The tribunal opined that what stabilisation clauses are there to do is to protect against confiscatory termination and takeover.[111] If the takeover is not confiscatory, it would not amount to breach of the stabilisation clauses. However, the tribunal did recognise that legislation abrogating a stabilisation clause did create a legitimate expectation on the part of AMINOIL with

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[109] For a different approach to stabilisation clauses by an arbitral tribunal, reference can be made to the case of LIAMCO v Libya [62 ILR 141], where the tribunal held that stabilization clauses do not affect the State's sovereign right to expropriate a contract, as to hold otherwise, would amount to intolerable interference with a State's sovereignty.

[110] 21 ILM [1978] 1

[111] This is nationalisation without compensation to the investor.

regard how long they could do business in Kuwait, and this legitimate expectation ought to be considered in the awarding of damages.

Thus far it has been established that as a general rule the sovereignty argument is not looked upon by the arbitral tribunals kindly. This is essentially because governments freely enter into these contracts, an action which in itself is an attribute of sovereignty. Thus the general position is that Governments cannot suddenly turn around and invoke the principle of sovereignty in order to abdicate responsibility for their actions.[112]

The above cases have shown this to be the case for the reasons that; firstly stabilisation clauses are regarded as part of international law, thereby shielding them against unilateral abrogation through host state legislation. This is not a prohibition to change the law, but merely a promise not to apply any changes vis-a-vis the investor or a promise to compensate the investor for any adverse consequences of such a change.[113]

Secondly, the stabilisation clause internationalizes the contract, and this in turn has the effect of putting both parties to the contract, equals, with the host state bound by the guarantees offered to the investor.[114] Thirdly, by reason of its very sovereignty within its territorial domain, the State possesses the legal power to grant rights by which it forbids itself to withdraw before the end of the concession.[115]

Finally, as an investor enters into a contract with the state, he has a legitimate expectation that the contractual obligations are to be respected, and of how long he could do business in that State, and this legitimate expectation ought to be considered in the awarding of damages should the law be abrogated in any way that detriments him.[116]

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[112] S.P Ng'ambi, Stabilization Clauses and the Zambian Windfall Tax

[113] AGIP v Congo, Award 30, November 1979, 1 ICSID Reports 321/2

[114] B.T.M Coale, Stabilization Clauses in International Petroleum Transactions Denver Journal of International Law and Policy as cited in S.P Ng'ambi Stabilization Clauses and the Zambian Windfall Tax Zambia Social Science Journal.2010. at p. 111.

[115] Saudi Arabia v Arabian American Oil Company 27 I.L.R 117 [1963]

[116] AMINOIL v Kuwait 21 ILM [1978]

3.4 WINDFALL TAX IN LIGHT OF STATE SOVEREIGNTY

3.4.1 WINDFALL TAX

Although many definitions are ventured forth, the essay will adopt the definition of Windfall tax to be the tax levied by governments against certain industries when economic conditions allow those industries to experience above average profits. Windfall taxes are primarily levied on the companies in the targeted industries that have benefited the most from the economic windfall.[117] In the case of Zambia, as earlier established, in May 2006, the prices of copper increased, and the Government in a move to benefit from this increase sought to reconsider the preferential tax regime that foreign mining companies had previously enjoyed. This was ostensibly to ensure that the Zambian public benefited from the high copper prices; which they otherwise would not have. Thus in 2008 the Government of Zambia introduced a windfall tax on base metals at a minimum rate of 25%. In addition to other tax rates introduced, the windfall tax was designed to bring in additional revenue to the government from the high copper price.[118]

3.4.2 WINDFALL TAX AND STABILISATION CLAUSES

The history of Zambia and the foreign investment in the mining sector began around 2000, when most of the state owned mining companies were privatized, and most of the development agreements between the government and the foreign mine owners were concluded. Most of the development agreements between the government of Zambia, and the foreign investors contained stabilisation clauses and in addition to this, the agreements contained specific "Taxation Stability" clauses.[119]

An example of these Taxation Stability clauses would be Clause 14.1 of the agreement between Kansanshi mines and the government of Zambia precluding the government from imposing or increasing the corporate or any new tax to an extent that would cause a materially adverse effect on the Company's profits. Whereas Clause 13 of Part D of the development agreement between the government and Konkola mines contains in addition to a "Taxation Stability" clause, a general stabilisation clause, whereby the State party undertakes not to enact any legislation that

[117] Investment Dictionary. http://www.answers.com/topic/windfall-tax-1
[118] C. Mfula Zambia Needs Stable Mining Laws to Attract Investment
[119] S.P Ng'ambi Stabilisation Clauses and the Zambian Windfall Tax

basically undermines the rights of the investing party, and essentially hinder the performance of the agreement.

However, bearing in mind The Mines and Minerals Development Act No.7 of 2008 provides in Section 160; A development agreement which is in existence before the commencement of this Act shall, notwithstanding any provision to the contrary contained in any law or in the development agreement, cease to be binding on the Republic from the commencement of this Act, and thus brings the legislative position today to be that mining agreements, specifically the concession agreements entered into with foreign investors that included stabilisation clauses of up to 10-15 years as of 2008, when the Act was passed as non-binding upon the Republic of Zambia.

However, as Zambia continues to receive large amounts of FDI in the mining sector, and continues to offer tax havens to the investors, as can be noted in Section 55 of the Zambia Development Agency Act[120] which specifically provides that; an incentive offered shall be valid for a period of five years from the grant of the licence, permit or certificate or for such period as the Minister responsible for finance may prescribe, it is imperative to note that Zambia continues to offer incentives to foreigners by way of tax havens, and thus it is important to establish whether or not Zambia as a sovereign state is allowed to unilaterally amend its laws, and in this regard reintroduce windfall tax regardless of standing agreements made after 2008.

The fact cannot be escaped that every sovereign state, Zambia included, belongs to an international community that bestows upon it, in addition to its sovereignty, certain responsibilities in relation to the other states. Having earlier established that stabilisation clauses ultimately have the status of an international principle, putting the two parties on an equal footing, it stands therefore that Zambia as a member of this international community ought to honor that international principle. Windfall tax essentially has the effect of affecting adversely the rights of an investor contrary to prior agreement, a move which undermines the very spirit of stabilisation clauses.

In comparison to the AMINOIL case considered above, where the government of Kuwait attempted to negotiate with the investor before it amended its laws, in Zambia what transpired is

[120] Zambia Development Agency Act, No. 11 of 2006, Section. 55.

the Government unilaterally amended its tax laws without consulting the mining companies.[121] Further as the concession agreements in the AMINOIL case ran for period of 60 years, it was understandable that the arbitral tribunal would consider the length of the agreement, and held it to be too long. In Zambia as earlier pointed out, the development agreements ranged from 10-15 years on an average. Thus this defence of an unreasonable length of tax havens in Zambia could hardly stand before an arbitral tribunal. Additionally, Section 55 of the Zambia Development Agency Act[122] now specifically provides that an incentive offered shall be valid for a period of five years, making the length of a stabilisation clause even shorter.

Furthermore, although the Government of Kuwait acceded to compensating for the nationalization of the assets, there is no evidence to suggest that Zambia was willing to compensate the mining companies for any losses incurred due to the imposition of the windfall tax.[123] Finally, the concession agreement was signed between Kuwait and AMINOIL prior to independence, however Zambia as an independent and sovereign State freely entered into the development agreements with the mining companies.[124] It is on this basis that the decision by the arbitral tribunal in the case of Saudi Arabia v Arabian American Oil Company[125] stands to state that;

> "By reason of its very sovereignty within its territorial domain, the State possesses the legal power to grant rights by which it forbids itself to withdraw before the end of the concession."

The effect of this is therefore that Zambia as an independent and sovereign entity, having freely entered into the concession agreements, should not be allowed to detract from these very agreements that they were able to enter into by virtue of its sovereignty.

It could thus be concluded that stabilisation clauses will be binding on the Zambian government, and they may be liable to pay the mining companies some amount of compensation should the latter choose to initiate arbitral proceedings.[126]

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[121] S.P Ng'ambi Stabilisation Clauses and the Zambian Windfall Tax
[122] Zambia Development Agency Act, No. 11 of 2006, Section. 55.
[123] S.P Ng'ambi Stabilisation Clauses and the Zambian Windfall Tax
[124] S.P Ng'ambi Stabilisation Clauses and the Zambian Windfall Tax
[125] 27 I.L.R 117 [1963]
[126] S.P Ng'ambi Stabilisation Clauses and the Zambian Windfall Tax

3.4.3 WINDFALL TAX AND STABILISATION CLAUSES; THE INTERPLAY WITH FOREIGN DIRECT INVESTMENT

A host country whenever it attracts FDI is sure to amass a number of benefits which may ultimately lead to economic growth and development of that country.[127] The potential contribution of FDI to host countries development was emphasised earlier highlighting the ability of FDI to transfer knowledge and technology, create jobs, boost overall productivity, enhance competitiveness and entrepreneurship, and ultimately eradicate poverty through economic growth and development. Governments across the world have liberalised capital controls, often coupled with financial incentives such as tax holidays and stability clauses in the hope of attracting FDI.[128]

Developing countries see FDI as being crucial to their development mainly because it provides required capital for investment, generates employment and acts as an aid to local firms by adopting more resourceful technology. Apart from facilitating capacity building in the host country, it is usually hoped that access to foreign markets will undoubtedly improve the integration of host country into the global economy and result in economic growth.[129]

In order that the maximum benefits from FDI are reaped and hence for there to be economic development, there is a requirement that a healthy enabling environment for business is present, which encourages both domestic and foreign investment, provides incentives for innovation and improvements of skills and contributes to a competitive corporate climate. Some factors holding back the full benefits of FDI in some developing countries include inadequate regulatory frameworks,[130] and tax policies that victimize foreign firms.[131]

As has been held by various arbitral tribunals, sovereignty is not an excuse for a government's failure to fulfill its contractual obligations and in essence an excuse to victimize foreign firms. Not only does the international community frown upon such acts, but such acts have the result of greatly deterring foreign investment. For a developing country like Zambia, FDI is a great asset

[127] K.Wishimanga, The Regulation of Foreign Direct Investment Towards Economic Development
[128] D. Haglund, Regulating FDI in weak African States : a case study of Chinese copper mining in Zambia Journal of Modern African Studies (Cambridge: Cambridge University Press, 2008) Page 547-575.
[129] S.I Ajayi, FDI and Economic Development in Africa. 2006
[130] C. Schreuer, The ICSID Convention: a commentary on the Convention for Settlement of Investment Disputes Page. 593.
[131] J. C Baker, Foreign Direct Investment In Less Developed Countries The Role of ICSID and MIGA (Westport, Connecticut. London 1999) Page 4.

that should be coveted. The facts show that FDI in the mining sector has helped open up areas that were previously idle because Zambia lacked the ability to run mining operations in those areas.

For instance once the Government of Zambia started with the privatization process in the late 1990s, the now China Non-Ferrous Metals Mining Company (CNMC) acquired ownership of the defunct and bankrupt Chambishi mine in north-central Zambia for US$ 20 million in 1998 and began to turn production around. China also committed additional investment into the copper sector when they announced in November 2006 that US$ 200 million would be invested in a copper smelter to be located in the newly established Multi-Facility Economic Zone in the Copperbelt region.[132]

Other international minerals and mining companies are also active in Zambia's copper sector. For example, Vedanta Resources, a London-listed firm based principally in India, announced in August 2004 the completion of a formal agreement to purchase a controlling stake in KCM. In November 2004, the company completed the acquisition of a 51% controlling stake in the Konkola copper mine for a total cash consideration of US$ 48.2 million.[133]

It is clear from the above statistics that Zambia needs FDI in order to boost its mining sector. As copper amounts for about 80 percent of the Zambian economy[134] and for there to be economic development in the country, it is imperative that the government does all it can to attract investment in this sector, and maintain it. Respect for contractual obligations is a key to attracting investment, and thus stabilisation clauses ought to be honored, in light of windfall tax.

3.5 CONCLUSION

This Chapter firstly established that a state is a sovereign entity, and by this it means it can establish rules and regulations with no external interference. In connection with this sovereignty comes the ability to enter into contractual relations with foreign investors. This interaction with foreign investors thus qualifies the sovereignty to the extent that a respect for contractual

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[132] P. Hare 'China and Zambia: The all-weather friendship hits stormy weather,' Association for Asian Research, 26 April 2007, http://www.asianresearch.org/articles/3009.html. Accessed on 1st February 2011.
[133] Mbendi Information Services Copper mining in Zambia – Overview, http://www.mbendi.com/indy/ming/cppr/af/za/p0005.htm. Accessed on 1st February 2011.
[134] C. Mfula, Zambia Needs Stable Mining Laws to Attract Investment

obligations is established. Failure to do so is a great deterrence to foreign direct investment which Zambia as a developing country greatly needs as it depends on the copper sector for most of its economic prosperity, and as has been shown Zambia requires international investment to maintain this sector. Stabilisation clauses essentially ought to be respected, as failure to do so attracts international responsibility as has been shown to be the position in various arbitral tribunal decisions. Consequentially, windfall tax if imposed is in effect a breach of contractual obligations, unless expressly provided for at the time an investment contract is being concluded.

CHAPTER FOUR

RECOMMENDATIONS AND CONCLUSION

4.0 INTRODUCTION

The aim of this chapter, is to draw some conclusions from the findings of the study and based on those conclusions come up with some relevant recommendations on the topic at hand with the aim of improving the situation prevailing currently. This chapter therefore draws conclusions from the discussion on foreign direct investment and how it can lead to the economic development of a country with special regard to the mining industry being a large contributor to revenue for Zambia. Finally recommendations will be submitted as to what can be done to improve the current investment framework as it stands.

4.1 GENERAL CONCLUSIONS

Zambia as a developing country strives to ensure that there is foreign investment in order to develop the economy, because of the correlation between FDI and economic development. In order to encourage investment, Zambia offers attractive incentives to investors with the motive of benefiting economically and in many other ways. Thus as a result of the potential role that FDI plays in accelerating economic growth, many developing countries and Africa in particular seek such investment in order to boost their development efforts.

The benefits may vary, and as has been shown include, the capital that these MNCs bring that help boost the economies development as these entities have the capacity of increasing government revenue tremendously which may be used for improvement of infrastructure and empower local corporations.

One of the key areas in which Zambia benefits from foreign direct investment is in the mining sector, particularly copper mining; an area in which the Zambian economy is heavily dependent on. As statistics and facts have shown, Zambia's mining areas lay dormant as Zambia lacked the resources and in effect the know-how to capitalize on the mining sector minus the assistance of the international investment community. Up until the involvement of certain foreign investors, some mining areas lay abandoned, or if not touched at all. This inevitably means that as Zambia

is so heavily dependent on the mining sector, it needs even more FDI in this area, if it is to reap benefits from it.

Despite the aid that Zambia has been receiving in the mining sector, it sadly remains an under-developed country. Reasons ventured for this with regards the mining industry is that the foreign owned projects are capitally concentrated and labor effective. Local inhabitants rarely benefit and when they do actually find employment, it is short-term and badly paid that is to say labourers are employed for trifling amounts. The facts on the ground also point to the fact that sometimes even the most basic of jobs are offered to foreign workers regardless of the existence of an excess of Zambian workers.

Further, large developing country MNCs have become dominant players in the economies of developing countries with the result that monopolization of that particular sector (in this case the mining sector). It follows then that the Government has a greater calling, to play a hand in rectifying the situation where the attraction for investment which is so greatly needed is satisfied, but not at the expense of the economy that it is in effect being called on to assist. The government has to be cautious however to remember that in its attempts to bring about the best for the country in terms of economic development, it should observe its international obligations. This is in light of international opinion as expressed in various arbitral decisions that answered the question posed at the beginning of the paper as to what is the legal impact of stabilization clauses in light of state sovereignty; the answer being sovereignty cannot be used to detract from promises made under contract.

In answer to the other question posed earlier in the thesis, i.e. whether or not the country is benefiting from FDI in the mining sector without windfall tax, the answer would be although windfall tax may seem attractive at a time when a particular economy experiences a boom, if its imposition goes contrary to existing contractual obligations, then its imposition may attract international liability. In the long run, this may not contribute to the long term economic growth of a nation. It may deter foreign investors, in that a country may acquire a reputation of using stability clauses to lure investors, and yet imposing laws that defeat the purpose of the investment, and thus other countries may be reluctant to take the risk of engaging in investment in that particular country. As statistics have shown Zambia's economy greatly depends on the mining sector, consequently, the mining sector is heavily dependent on foreign investment to

function. The practical end result would therefore be that although the government has removed the windfall tax, the long term benefits in light of foreign investment and economic growth override the short term benefits of gaining a share of the unexpected profit that is not certain to last forever.

The paper now addresses certain recommendations that will help achieve a balance of the two interests; those of the State, and those of the investors.

4.2 RECOMMENDATIONS

4.2.1 PRIVATE-PUBLIC SECTOR INTERACTION

To begin with, this paper recommends that the Zambian Government improves its public sector-private sector interaction. That is to say, the Government as a representative of the public sector needs to improve its enlightenment of the said sector, with regards transparency in the imposition of its policies dealing with the private sector, which inevitably impact on the public sector. With good governance and transparency the exploitation of mineral resources can generate large revenues that can cultivate and help in sustaining growth and poverty reduction. Over the past 40 years we have seen the country being robbed off of millions of dollars through tax avoidance. The above-mentioned situation exists due to the weak transparency and governance in the extractive industries and also inadequate democratic scrutiny as several key aspects of mining in Zambia remain shrouded in secrecy.[135]

It follows then that the Government ought to adopt the implementation of policies that are transparent and readily accessible to the public and both the private sectors of the community. Zambia as a democracy needs to have a government that is by the people, for the people, thus there is no room in a democratic society for any form of secrecy especially in a sector that greatly impacts on the economic well-being of the society as a whole.

[135] E. Kangamungazi, Tax Avoidance and Inequitable Mine Contracts, Case Study: Zambia Programme Officer, Economic Justice Programme, Caritas Zambia, 6 October 2009, Side event, United Nations Geneva, United Nations consultation on business & human rights.

4.2.2 TAX POLICIES

The biggest outcry from the Zambian community to date remains the taxation policies employed with regards the mining companies. To be specific, the outcry over the removal of the windfall tax policy was one uttered by many sectors of the community. However, in addition to the fact that Zambia has an international obligation to respect its contractual obligations with foreign investors, light must be shed on the fact that the windfall tax policy was improperly constituted to begin with. Finance and National Planning Minister Situmbeko Musokotwane in answer to a question posed to him in Parliament as to why the Government had abolished the windfall tax responded to say, the system was defective and not consistent with international practice as it was based on revenue as opposed to profit. He then added that the windfall tax did not take into account the cost of production.[136]

Based on the response given by the Minister of Finance the Zambian community may not have launched such an outcry to begin with if they were made aware of the reasons why the windfall tax was being imposed; under what conditions it could be imposed; and why in this instance it had to be removed. This thus ties in with the above recommendation as to transparency in the imposition of government policies.

However the government generally also needs to improve its imposition of taxes. Certainty in the legislative framework is a key attraction for FDI. In this regard the Government ought to adopt a stable framework within which the mining community operates. This means laws imposed should offer a uniform and permanent standard by which the entire investment mining community is governed by. Zambia Revenue Authority, the tax governing body in Zambia, should not be given the prerogative to sway from the standard framework by offering "sweeter" investment deals to some investors at the expense of others, including the local ones.

Compliance provisions should be clearly stated and provided as guidelines for the use of taxpayers. The ZRA should continue its efforts to publicize relevant policies but consider other effective methods of dissemination. Increasing efforts to obtain information and feedback from the public and the business community will contribute to improved policy and relations. Legislation which confers wide discretionary powers on ZRA officials should be repealed. In

[136] Times of Zambia, Friday November 26th 2010, Page 2.

addition, measures and procedures are required to ensure that taxpayers can report corrupt practices or other misconduct of ZRA officers without suffering retaliation.[137]

4.2.3 FOREIGN INVESTMENT TAXATION INCENTIVES

The lesson learnt from the imposition of the windfall tax and the response from the mining communities, is that taxes should be levied at all times not just when the profits have become hefty, and an ethical argument can be used to qualify an impulsive introduction of taxes. The law should from the onset reflect permanent mining conditions, which if they include stabilisation clauses should also include the fact that in case of unexpected profit, the Government reserves the right to impose a reasonable tax on the said profit, so as not to defeat the essence of the investment to begin with.

Further, the investors that are granted these tax holidays have no reason to remain operational in the jurisdiction when these holidays' expire and past experience has shown that these investors withdraw from the economy as soon as the tax holidays nears an end. In this way the generosity of the state and government in granting these tax holidays is compromised, because the corporations maximize their profits and run away just before they have to atone for it. If tax holidays are to be granted then they should be accompanied by a minimum investment period that the foreign investor has to comply with, which runs beyond the stabilised period.

4.2.4 WORKMANS CONDITIONS

It is understood and appreciated that FDI is important for the development of the mining economy in Zambia. However, FDI should not be attracted at the expense of the Zambians well-being. It is recommended that the legal framework regulating the conditions of employment for citizens should be strengthened to ensure that the benefits of outsourcing of labour by multinational corporations are fully realised by the host nations. Workers in developing countries, Zambia inclusive, lack the rights, legal protection and union protection enjoyed by their counterparts in developed countries thus the benefits of FDI are harder for the workers to enjoy.

[137] Africa Private Sector Group An Assessment of the Investment Climate in Zambia

The labour laws should ensure that the minimum wages available from this form of investment should be able to cater for the basic needs of the least paid person. In this way the integration and the transfer of the means of production into the hands of individuals and corporations will still ensure that citizens are taken care of. Zambians ought to be educated on their labour rights as well, so that incase of any attempt to detract from them, the power to make the appropriate authorities aware of the situation lies in their hands.

CONCLUSION

Zambia is a sovereign entity, the implication of which is that she should be able to make use of, and benefit greatly from the resources that she has been gifted with. The body entrusted with the authority to govern these resources, that is, the Government is obligated to ensure that the benefits from these resources is experienced equally by all the inhabitants of the state. In the case of FDI, the benefits can only be achieved if there is regulation which ensures that such benefits filter down to each citizen.

In this regard, incentives should not be offered aimlessly to the detriment of the host. MNC's should also be closely monitored to ensure that they are maintaining their implied obligation to ensure the expansion of the economic sector of the host country within whom they seek to establish their interest. There is also a need to encourage collaboration of foreign owned firms and local ones as is the case in countries like Botswana, and better working conditions for miners as is the case in Chile.

In order that Zambia fully benefits from the inflows of FDI, it is essential that the government implement the policy and legal recommendations suggested because as things stand, Zambia is clearly not taking full advantage of its mining potential to the detriment of its own economic development. In the Zambia Development Agency Act are to be found key provisions which if successfully implemented will be able to assist in the economic development for Zambia. However, it is also necessary that more regulation and less incentive be offered in the various pieces of legislation providing for taxation of investments, and that the Zambia Revenue Authority is kept on a tighter and transparent leash as it engages in relations with the foreign sector.

It is the conclusion of this paper that Zambia still has a long way to go in reaping all the benefits of FDI and this can only be done through the apparatus of the law. Zambia must begin to realize that it has great resources which it can and should exploit to the fullest as with such resources it can have a better hold on its economic development and growth.

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