Inside Counsel

American Investment in Cuba: Not So Fast!

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Introduction

On December 17, 2014, President Obama announced that the United States and Cuba would restore diplomatic ties for the first time in more than 50 years. American businesses have long viewed Cuba as an untapped market, ripe for investment in real estate and tourism, as well as agriculture, infrastructure, sugar and nickel mining. President Obama's announcement prompted many to consider ways in which they might be able to get a head start in the Cuban market. However, multiple obstacles remain for foreign investment. Americans should view the recent announcement as a positive sign for future potential but not a green light for investment today.

The New Regulations

Following the President's announcement, the U.S. Department of the Treasury published revised Cuban Assets Control Regulations ("CACR"; 31 C.F.R. § 515), and the U.S. Department of Commerce published revised Export Administration Regulations ("EAR"; 15 C.F.R. § 730-744). The regulations, which are amendments to existing sanctions, were effective as of January 16, 2015. The new regulations include the following notable provisions:

- Americans may use U.S. credit and debit cards in Cuba;
- U.S. financial institutions may open accounts at Cuban banks to facilitate authorized transactions;
- U.S. companies may export mobile phones, televisions, memory devices, recording devices, computers and software into Cuba;
- U.S. companies may ship building materials and equipment to private Cuban companies to renovate private buildings;
- Americans who are authorized to visit Cuba no longer need to apply for special licenses (though general tourist travel is still prohibited);
- There is no longer a limit on how much money Americans can spend in Cuba each day or restrictions on what they spend it on;
- Remittance payments to family members in Cuba will be allowed up to $8,000 per year (up from $2,000 per year);

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- U.S. investment in some small businesses and agricultural operations are permitted; and
- Remittance payments to support humanitarian projects are permitted.

Of specific interest for U.S. investors are the last two measures, which are discussed in detail below.

U.S. Investment in Small Businesses and Agricultural Operations. The new regulations authorize the following projects:

- medical and health-related projects;
- construction projects intended to benefit certain civil society groups;
- environmental projects;
- projects involving educational training on the topics of entrepreneurship and business, civil education, journalism, advocacy and organizing, adult literacy, or vocational skills;
- community-based grassroots projects;
- projects suitable to the development of small-scale private enterprise;
- projects related to agricultural and rural development that promote independent activity;
- certain microfinancing projects; and
- projects to meet basic human needs.

An investment must meet one of the above limited categories to be permitted under U.S. law.

Remittance Payments to Support Humanitarian Projects. The new regulations permit "remittances by persons subject to U.S. jurisdiction to individuals and independent non-governmental entities in Cuba, including pro-democracy groups and civil society groups, and to members of such groups or organizations" for limited purposes, including:

- To support humanitarian projects that are designed to directly benefit the Cuban people;
- To support the Cuban people through activities of recognized human rights organizations, independent organizations designed to promote a rapid, peaceful transition to democracy, and activities of individuals and non-governmental organizations that promote independent activity intended to strength civil society in Cuba; and
- To support the development of private businesses, including small farms.

Remittances for other purposes would be prohibited under U.S. law.

Obstacles to Investment

There remain many obstacles to U.S. investment in Cuba:

The U.S. Embargo. While the new U.S. regulations relax certain travel and business restrictions, the U.S. still maintains a comprehensive embargo on trade and relations with Cuba. The embargo includes some of the most significant limits on travel, tourism and trade between the U.S. and Cuba. Only Congress can repeal the embargo, a step which seems unlikely to occur anytime soon. Whether Congress will act is a highly charged political issue, and it could be years before the embargo is lifted, if ever.

Cuban Appetite for Foreign Investment. Cuba has sent mixed messages about its appetite for foreign investment. In March of 2014, Cuba passed a law intended to attract foreign investors. However, in September of that same year, a Cuban court sentenced a Canadian executive to fifteen years in prison for economic charges in a case which Western diplomats called a "chilling development" for foreign investors.

Cuban Government Restrictions. Cuban laws can make investment difficult. Under Cuban Law 77 ("Ley de la Inversion Extranjera" or the Foreign Investment Act), passed in 1995 by the Cuban National Assembly, only three kinds of foreign investment are permitted: (i) international association contracts, (ii) joint ventures (which can be entirely foreign-owned) and (iii) totally foreign-owned companies. Under the Act, all foreign investments must be approved by the Cuban Council of Ministers and, in many cases, the Executive Committee thereof. Companies that wish to enter the Cuban market are often required to establish joint ventures with the government or state-owned firms, similar to China's approach when it opened its economy in the 1980's and 1990's. In China's case, many U.S. and other foreign companies found the joint venture structure prohibitively restrictive and costly. In Cuba, the state-owned firms are notoriously inefficient, slow and short on cash.

Possible Litigation. Many Cuban-Americans and U.S. companies had property confiscated in the 1959 Castro revolution. Experts have pointed to the potential for these parties to sue companies entering into business with the Cuban government in order to recover lost funds. While the success of any suit may be remote, the cost and negative publicity associated with addressing a claim remains a chilling factor to foreign investment.

Cuban Infrastructure & Economy. Cuba lacks an effective legal infrastructure for contract and judicial enforcement of property rights, and there are still a number of limitations and restrictions on ownership of Cuban real property by foreigners. "Cuba needs to make internal reforms of its real estate system, including its title system, and financing laws so there can be more foreign investment," according to Jose Gabilondo, a professor at Florida International University College of Law and an expert on Cuban finance. In addition to a lacking legal infrastructure, Cuba also lacks a physical infrastructure which makes investment challenging. Cuba is, in many ways, an island frozen in time: buildings and amenities desperately need to be modernized, roads need to be repaved, and the island needs even the most basic internet and telecommunications capabilities. Cuba's economy ranks 69th in the world (about the size of Hawaii's), and according to the United Nations the annual per capita income is just $6,200 – a disturbingly low figure.

U.S. Political Considerations. U.S. lawmakers from both parties have stated that they plan to complicate President Obama's efforts to restore U.S./Cuban relations by refusing to confirm diplomatic nominees or fund certain of Obama's proposals. Congress may erect legislative barriers to investments or relations with Cuba, making any investment illegal or problematic under U.S. law despite the regulations. It is too early to know whether any action will be taken politically to stand in the way of repaired relations or future investment.

Cuban Presidential Leadership. Raul Castro replaced Fidel Castro as president of Cuba and has demonstrated a less confrontational style of leadership than his older brother. The younger Castro has allowed more economic reforms to take place in Cuba, and initially seemed supportive of the new U.S. regulations. However, in late January 2015 he demanded that the U.S. return the base at Guantanamo Bay, lift the embargo and compensate his country for hundreds of millions of dollars in damages caused by the embargo before the two nations re-establish normal relations. It appears unlikely that the U.S. will meet these demands, at least in the near future.

Conclusion

The new U.S. Treasury and Commerce regulations regarding Cuba represent a major improvement in U.S./Cuban relations. However, there is still a long way to go. There will be plenty of opportunities to make money in Cuba if the decades-long embargo is effectively lifted and the other obstacles noted above are able to be successfully mitigated – however, American investors need to be patient to see how things play out before rushing to invest in Cuba.