



CENTRE FOR CO-OPERATION WITH NON-MEMBERS
DIRECTORATE FOR FINANCIAL, FISCAL AND ENTERPRISE AFFAIRS

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Private sector presentation for the Netherlands Antilles

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As an outcome of the previous workshops on this topic, several areas for further study to draw up investment policies were identified. They are listed in the annotated agenda, which we all received and the ones I'll talk about are:

- Promotion of forward and backward linkages to indigenous industries
- Improving institutional framework
- Creating efficient capital markets and improving access to capital
- Tax treatment of foreign investment

Not all countries seeking foreign direct investment ("FDI") will have to pay attention to all items on the list to the same extent. The Netherlands Antilles ("NA") has modelled its regulatory framework in all areas on that of the Netherlands and has benefited from that country's experience. The Netherlands, over the last ten years, has been among the top five countries both on the inflow and outflow sides of the OECD's most recent FDI statistics. Moreover, traditionally FDI in the NA, in large part has come from the Netherlands.

Tax incentives to prospective investors, both local and foreign, early on became the primary tool for the Netherlands Antilles to induce investment. My talk will concentrate on the development of these incentives and their part in foreign direct investment in the NA through mergers and acquisitions ("M&A") and will touch briefly on the status of the other areas of study on the list.

To move down the agenda, I believe that the items: "improving the institutional framework, improving foreign direct investment statistics, assessment of competitive advantages, and improving the indicators to assess the performance of Investment Promotion Agencies", are related, in that they do not impact the profitability of foreign direct investment, but are instrumental in procuring it.

There is no lack of offices, organizations and reports that can supply information on, document, assist and regulate prospective foreign direct investment in the NA. The institutional infrastructure is very developed and, as said, modelled on the Dutch system and the competitive advantages of the NA are extolled in all the literature put forth.

Lately it seems as if the administrative agencies consider their activities to be the ultimate goal and thus have lost sight of their purpose, which is to assist real life individuals and businesses to accomplish their goals. This is in part due to demands from international organisations and therefore a worldwide situation. The regulatory agencies tend to forget that the statistics and the permits and advice they provide, are subservient to direct investment, which is what both the host country and the investor are really interested in. By making the compliance requirements ever more complex, decisions to invest become more difficult and wrapped up in red tape. Improving the institutional framework, and related issues, in my opinion and at least in the NA should mean removing the regulatory roadblocks on the road leading to actual investment. It is useless for one government agency to convince an investor to come to the NA to invest, if the other agencies do not provide the landing and work permits or the import duty exemptions or whatever else was promised the investor within an acceptable, which means "short", period. Examples of frustrated investors taking their money elsewhere abound.

Creating efficient capital markets and improving access to capital. The Netherlands Antilles has an open capital market and several international banks are operating here. Most recently, the Royal Bank of Trinidad and Tobago has decided to invest in the islands of the NA. They started by acquiring the Mc Laughlin Bank in Curaçao and recently completed their acquisition of the Chase Manhattan Bank's branch in Sint Maarten. They are now in the due diligence stage for the planned purchase of ABN-AMRO's Curaçao onshore business.

Through large local and international banks such as MCB, RBTT, NIB (Netherlands Investment Bank) financing from the whole world is available to prospective investors. In certain instances of great significance to the economy, financing obtained from third parties will be guaranteed by the NA Government.

If any aspect of the availability of capital for the financing of new projects is to be criticized, it is the high rates of interest charged locally, although some incentives are available for small businesses. However, since interest payments abroad are allowed by the Central Bank, loans at better interest rates may be contracted outside of the NA.

M&A is the form of foreign direct investment preferred by investors from OECD countries, according to the recent OECD article I read on Recent Trends in Foreign Direct Investment. I wish to thank Maiko Miyake, present today, and Magdolna Sass of the OECD and Richard Bolwijn, partner at KPMG Consulting in London, for having written it and allowing me to use its findings. In the NA, for a number of reasons, the use of M&A is limited. Most of them are related to the size of the territory and the consequent need of any investor to be able to sell his product through export. Competitiveness is crucial to be able to export and because of tariffs, taxes and/or labor laws, the price level in the NA for most products is too high.

Although the NA offers many of the advantages, generally considered to be driving the M&A wave, such as good regional political relations, good facilitating legislation (of which more later), a well developed technological environment, and an open capital market as discussed before, the factors negatively influencing M&A investment still outweigh the advantages.

Specifically,

- the limited offer of midsize privately owned businesses;
 - the downward spiral of the local economy;
 - domestic impediments, such as protectionist measures and public monopolies;
 - the plethora of regulatory agencies (“too much red tape”),
- continue to hinder investor driven M&A growth in the NA.

While larger economies with indigenous raw materials and/or cottage industries, at a certain point in their development become attractive targets for foreign acquisition, and consequently are the main vehicle for foreign direct investment, the Netherlands Antilles has very few manufacturing industries that can attract foreign direct investment. Tourism related businesses until now have offered the best possibilities for both acquisitions and new direct investment. Outside of the hospitality industry, only very limited M&A activity is found, except, for instance, the one by RBTT mentioned before. In the technology industry, the other area which has seen a lot of M&A activity worldwide, legislation passed this year may open the way for e-business investment in the NA.

In the 80's, the NA decided that it was necessary to broaden the base of its economy and offered incentives, in the form of protective tariffs to newly established industries.

Due to the lack of raw materials, with the exception of salt in Bonaire, or any manufacturing tradition, the new industries were primarily (re)packaging industries of product imported in bulk. Their aim was either to supply the domestic market or to profit from the export incentives offered by the E.U. to the associated territories of its member states.

The industries focusing on the local market so far have been unattractive M&A targets for foreign investors, mainly because of the high price of their products preventing extension of the market through export. A change of policy in the E.U. has made those directed toward export to the E.U. uninteresting.

Currently, the main industries of the NA are, its oldest industry, the oil refinery “Isla” and related transportation activity, the ship repair industry, international finance and services, trade, tourism, the semi-private utility companies and some mining activities in Bonaire.

The large foreign transactions have been limited to Bonaire's salt mining and salt export industry owned by Cargill of the USA and the oil refinery “Isla” in Curaçao, sold by Shell Curaçao for ANG 1,- to the island government, and subsequently leased to the Venezuelan State Oil Company, PdVSA. The other large businesses in the NA, if not yet M&A targets, have all sought foreign direct investment: recently there have been negotiations for the sale of the ship repair company to a Dutch entrepreneur, and the utilities' company, Aqualetra, concluded a foreign investment agreement with Delta Nutsbedrijven from the Netherlands for the installation of electricity generating windmills involving an investment of some USD 17 million.

When the Government seeks foreign investment for fully public or semi-private industries, it is usually prompted by imminent national calamities, such as the threat of loss of jobs. These foreign investments are not entrepreneurial in the sense that the risk aspect of the investment disappears because of Government guarantees and/or far reaching incentives, removing the tariff and other regulatory barriers, otherwise hindering FDI activity.

This type of investment subsequently induces infusions of capital for the upgrading of the facilities acquired. A current local example is the upgrading projects of Isla, carried out by a consortium of foreign companies, with financing from numerous foreign and local banks, guaranteed by the Government of the NA and the island of Curaçao and partially paid for by PdVSA. These projects aim to improve the power and water supply of the island, thereby reducing the price of electricity and water, and will correct the oil refining procedure so as to drastically reduce its polluting effects. The USD 500 million to be spent, moreover, should give a boost to the ailing economy. Even with such significant results at stake, (labor) regulation is causing the project to stagnate.

Investor initiated M&A activity can be found in the tourism sector and as said before with regard to capital markets, in the financial sector. As a matter of fact, most hotels, restaurants and entertainment projects are now in the hands of foreign entrepreneurs. There is the investment by the Dutch Van der Valk group in the Plaza Hotel in Curaçao and in Bonaire; the Sheraton and Princess Beach hotels in Curaçao, purchased by Argentinean entrepreneurs; Porto Paseo and the ex-Kadushi Cliffs time share resort, both owned by the Dutch entrepreneur who also owns the Kura Hulanda museum and conference center and has plans for further investment (if he finally gets his permits), Jacob Gelt Dekker.

Curaçao's Blue Bay Golf course was built by another Dutch entrepreneur Joep van de Nieuwenhuyzen, who may also become the owner of Curaçao's ship repair company. Curaçao has also benefited from several smaller investments by primarily Dutch entrepreneurs, in the restaurants and cafés that can be found downtown and here and there on the island. Even the extensive investment in the Otrabanda part of Willemstad by the Kimatrai group of Curaçao, is partially funded with capital from other Caribbean investors.

Tourism, and to a certain extent trade, are export industries and as such depend on foreign markets. They are highly dependent on a good transportation system, both to get goods and people in and out of the islands. The national airline company is not able to satisfy the demand and regulation prevents other solutions.

Tax treatment of foreign investment, the last item on the agenda.

A whole sector of the NA economy is based on its tax legislation. Over the last fifty years, the so-called offshore companies have profited from the favorable rates of tax offered. The taxes paid by these foreign owned companies and by the local trust and financial services companies handling the business and the thousands of people employed by the industry have alleviated the shortages in Government revenue which, especially in recent years, have become astronomical. The offshore business also permitted the growth of what is now a tradition of professionalism in the financial, legal and administrative areas. In fact, it can be said that the financial services sector over the past 50 years has matured into Curaçao's largest local industry. This capability will allow the industry to switch from a jurisdiction with multiple types of tax for its different taxpayers to one system for all taxpayers, which the NA has committed to through its level one commitment of November 30, 2000 to the OECD and which should free it from the tax haven taint in all OECD member countries.

In addition to having a separate set of tax rules for offshore companies, which will be abolished this year with the introduction of the tax overhaul, called "New Fiscal Framework" and in general referred to as "NFR", the NA has been giving tax incentives to attract direct investment since the 50's.

The earliest incentives (1953) are the tax holidays for investment in the construction and/or renovation of hotels, and in industries aiming to improve the economy and job market. The first hotels were all built with complete freedom from import duties on all materials imported for their construction and were run exempt from NA income tax both at the hotel level, and at the level of the investors receiving dividends. As with all things, there's bad with the good. The downside to the tax holiday law was that after expiration of the tax holiday, investors were no longer interested in the business and sold it to a buyer, who could then apply for a new tax holiday of his own.

In 1954 the offshore industry was born. Two new articles were added to the tax code, the articles 14 and 14A, which provided for favorable taxation of income derived outside of the NA for the benefit of non-residents of the NA. As said before, this change was significant not only for the NA Treasury, but it made it possible for a large part of the population to acquire skills and learning and improve their lives, while, at the same time building a high degree of professionalism. In that sense, the much maligned offshore business was a necessary stage in the financial industry's development that will enable the NA to adapt to the new fiscal standards set by the E.U. and OECD.

In 1964 the tax code was amended to include incentives to stimulate the development of unproductive land and in 1975 the Free Zone legislation was passed.

The rate of tax for Free Zone businesses who, by law should derive the bulk of their income from exports, is 2%. The reason for this low rate lies in the low profit margin that the Free Zone companies can make because of the constraints of competitiveness for exports and the consequently higher proportion of income being spent to cover the operating costs. Free Zone companies are easy to set up and hardly any established Free Zone businesses are interesting M&A targets. There has been, however, a lot of new foreign direct investment in that sector of the economy. In spite of the fact that the market of the Free Zone companies is foreign, and not dependent on the sluggish local economy, revenue from the Free Zone has declined in recent years, in part also because of the problems experienced by the national airline and its unreliable service.

The latest development in the incentives area is the E-Zone legislation, which is much broader based than the Free Zone legislation, in that it extends the incentives from companies trading physical goods from a Free Zone location, to those providing services through e-business from several possible locations.

While the earlier incentives provided for a complete tax holiday for a period of ten to eleven years, the Free Zone and now E-zone legislation, provide for tax of net income at a 2% rate. This differentiation in rates, with respect to the rates applicable for all other companies, is justified by the fact that, in essence the taxable income is not derived in the NA and there could be a question as to whether it should be taxable in the NA at all.

In combination with the acquisition of sufficient capacity for telecommunications, and the OECD determination that the location of a server can give rise to a taxable permanent establishment, the E-zone legislation is the latest in a chain of tax incentives that we in the NA have high hopes for as a source of foreign investment.

In conclusion, I believe that it is justified to say that the NA has a very good framework in place, able to attract and assist foreign direct investment. At the same time it must be said that overregulation, and/or regulation at two levels, those of the NA government and the island governments, in the best case is inefficient and in the worst, can even turn away investors.

Over the past fifty years the NA Government has shown great flexibility in accommodating the requirements of foreign investors, either through new legislation or by giving exemptions on a case by case basis and there is no reason to believe that it will not continue to do so. On the other hand, inflow of increased foreign investment, will only be possible if targets become more attractive, by removal of tariff and other restraining barriers, and improving transportation to and from the islands.

Lastly, the highly competent local financial services and tax advisory sector is there to provide assistance to investors from the moment foreign investment is first contemplated through all stages of implementation and subsequent business. KPMG, with its consulting, accounting, tax and legal services is among the leaders of the sector.

This is what I had to say. Thank you for your attention.

Thank you