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SOVEREIGN WEALTH FUNDS LAW CENTRE

BI-ANNUAL LEGAL REPORT 2013

03 / APRIL 2013



SWF LAW CENTRE

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LEGAL REPORT**

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The main issue of this 2013/1 Report focuses on national taxation regimes and namely tax exemption granted to sovereign investors by national laws or practices, or by bilateral agreements on a reciprocity basis. Practice quite surprisingly shows that there is not always a direct relationship between state immunity and tax exemption, and that their respective theoretical structure are not often corresponding. The SWF Law Centre taxation database (with data updated on a monthly basis) registers national tax treatments and exemptions applicable to SOEs or SWFs.

The country analysis focuses on Russia. Russia's legal order and economic environment are currently experiencing massive and critical changes deeply affecting national institutions. The accession to the WTO is fast-moving Russian economy toward a free economy, and Russian companies to an unexperienced competitive arena. On the other hand the Eurasian Customs Union, a regional integration initiative, fast-changing toward a single market Union, is imposing Russian institutions to deal with a supra-national organization, having its own institutions (a Commission, a Court of Justice) and rules, some of which directly applicable in the member states' legal orders. Scholars and observers believe that the path is now irreversible; we try to list the potential effects of such radical changes in the Russian market and trade.

Our SWF focus is on the Fundo Soberano de Angola, a recently established fund, which independence, governance, transparency, investment targets we investigate, also trying to forecast its positive effects

in the Angolan and, more generally, in the African pattern as a development fund.

The book reviewed is Sovereign Investment – concerns and policy reactions, edited by Karl P. Sauvant, Lisa E. Sachs and Wouter P. F. Schmit Jongbloed.

The big picture shows a sharp contradiction between the slowness of the current economic upturn on the one side, and the fast changes that are moving the investment pattern, especially when states are investors, on the other side. Such a fracture deserves further investigation.

PROF. FABIO BASSAN

SWF Law Centre Founding Director

Main Theme

- 01 SWFs and the Foreign Tax Exemption p. 7
Fabio Bassan

Country focus: Russia

- 02 FDI in Russia, after Russian Eurasian Customs p. 24
Union Membership and WTO Accession
Giuseppe Liotine

SWF focus: Angola

- 03 The upcoming African Sovereign p. 40
Wealth Funds: the Fundo Soberano
de Angola - FSDEA
Celeste Cecilia Moles Lo Turco

FDI: New Bilateral Investment Treaties 2011-2012 p. 65

Book review

- Sovereign investments – p. 69
Concerns and policy reactions
(edited by Karl P. Sauvant, Lisa E. Sachs,
and Wouter P. F. Schmit Jongbloed)
Silvia Venturini

**MAIN
THEME**

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FABIO BASSAN

SWFS AND FOREIGN TAX EXEMPTION

I. INTRODUCTION

Unlike operators, scholars have hardly paid attention to the ‘SWFs’ tax exemption factor’. Sovereign investments, depending on the country they invest in, the kind of investment and the type of state investor, are sometimes exempt from taxation. Such exemption produces direct effects on both the host state’s domestic competitive environment (it distorts competition) and on investor states’ decision about which state to choose as investment target. The tax exemption factor becomes actually crucial when a sovereign investor decides where to invest. Hence, the issue whether SWFs should be paying taxes on the income earned from the investments they make remains critical at both national (host/home state) and international level¹.

**UNLIKE OPERATORS,
SCHOLARS HAVE
HARDLY PAID
ATTENTION TO
THE ‘SWFS’ TAX
EXEMPTION FACTOR’**

¹ Barbieri M., *Sovereign Wealth Funds and the principle of state immunity from taxation. Which implications for economic development?*, UNCTAD-Virtual Institute digital library; January 2010.

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Nevertheless, as for now, a debate on the tax exemption of sovereign investments has been raised by scholars in the United States only, while in the rest of the world this topic seems not to be adequately discussed. Hence, there is room for investigating if, where, why, and on which conditions a tax exemption is granted by states through national laws, bilateral treaties and case law, and for researching a theoretical tax exemption structure. Finally, the existence of a direct or indirect relationship between tax exemption and state immunity on one side, and bilateral investment agreements on the other side, should be verified as well.

With no ambition of exhaustiveness, and hoping that new studies will focus on this topic, we can pool the practices adopted by the states into three main groups. The first group comprises those national laws that grant tax exemption to sovereign investments based on the assumption that, by so doing, the states concerned are merely implementing a general principle of international law according to which *par in parem iudicium non habet*. In this first group, tax exemption is sometimes absolute, but more often it depends on the nature of the business.

The second group comprises those states where limited or absolute tax exemption is granted not under the law, but under a bilateral investment treaty, usually on a reciprocity basis. The theoretical structure of such exemption is actually, in all these cases, a practical one.

The third group comprises those states that do not grant any tax exemption to foreign investments, neither relative nor absolute, under no condition.

THE EXISTENCE OF A DIRECT OR INDIRECT RELATIONSHIP BETWEEN TAX EXEMPTION AND STATE IMMUNITY ON ONE SIDE, AND BILATERAL INVESTMENT AGREEMENTS ON THE OTHER SIDE, SHOULD BE VERIFIED

The general classification above raises some questions, the first one being a possible relationship between granting tax exemption to state investments and allowing immunity from jurisdiction to states. When it comes to state immunity, tax exemption should be granted to states accordingly. The practice shows instead that there is not always a direct relationship between state immunity and tax exemption, and that their respective theoretical structures often do not match. As a matter of fact, partial or total tax exemption does not always correspond to relative or absolute immunity (respectively) being granted. A few significant examples of this practice are listed in paragraph 2.1.

A second question may be raised on the relationship between tax exemption and subjective and objective features. Namely, the question is whether a tax exemption applies both to SWFs and State-Owned Entities (SOEs). Theoretically, a tax exemption should be granted more to SWFs than to SOEs, as the former are state investors, and the latter are companies operating abroad and subject to company law, regardless of their owner. On the contrary, the practice is quite surprising.

A partial answer to these questions can be searched in the integration between domestic laws and bilateral investment treaties, which both consent state immunity, the former unilaterally (absolute or relative immunity is provided for by the law), and the latter bilaterally (on a reciprocity basis, as established by a treaty). Now, let us look at how this is implemented in the practice.

THE PRACTICE SHOWS INSTEAD THAT THERE IS NOT ALWAYS A DIRECT RELATIONSHIP BETWEEN STATE IMMUNITY AND TAX EXEMPTION

THE QUESTION IS WHETHER A TAX EXEMPTION APPLIES BOTH TO SWFS AND STATE-OWNED ENTITIES (SOES)

2. TAXATION OF FOREIGN INVESTMENTS

When investing abroad, SWFs are (or should be) nothing but foreign investors. A general tax treatment is usually granted to foreign investors regardless of their owners (individuals, private companies/funds, state-owned companies/funds).

The SWF Law Centre has developed a database recording national general tax treatments and exemptions applicable to SOEs or SWFs.

According to the SWF Law Centre's taxation database, the tax treatment of the income earned by a foreign investor in host countries may be divided into three main groups.

THE SWF LAW CENTRE HAS DEVELOPED A DATABASE RECORDING NATIONAL GENERAL TAX TREATMENTS AND EXEMPTIONS APPLICABLE TO SOES OR SWFS

2.1. First group: tax treatment for passive income coming from commercial activities undertaken in the host state by a foreign investor

The tax treatment granted to the disposable income coming from the commercial activities carried out by a foreign investor in the host country falls within the first group. According to the OECD Model Tax Convention on Income and Capital, in order to receive such treatment a foreign investor should have a permanent establishment² in the host country: this allows the host country to tax the income attributable to the foreign entity that is gathered in that country.

² OECD Model Convention on Income and on Capital, Article 5 (OECD Model) and commentary thereon.

A foreign investor has a permanent establishment when it has a fixed place of business in that country³. The permanent establishment criterion allows those who do business in a foreign country to have their income taxed as if they were domestic enterprises. Hence, foreign investors falling in this category are treated as residents of the host country, even if there are not⁴.

**THE PERMANENT
ESTABLISHMENT
CRITERION
ALLOWS THOSE
WHO DO BUSINESS
IN A FOREIGN
COUNTRY TO HAVE
THEIR INCOME
TAXED AS IF THEY
WERE DOMESTIC
ENTERPRISES**

2.2. Second group: outbound remittances

Outbound payments of recurrent income (i.e. interest, royalties and dividends) fall within the second group. This type of income is generally subject to withholding taxes. The withholding tax on gross income usually applies when either the foreign investor has no permanent establishment

³ The commentary indicates that a fixed place of business has three components:

- i. Fixed refers to a link between the place of business and a specific geographic point, as well as a degree of permanence with respect to the taxpayer. An "office hotel" may constitute a fixed place of business for an enterprise that regularly uses different offices within the space. By contrast, where there is no commercial coherence, the fact that activities may be conducted within a limited geographic area should not result in that area being considered a fixed place of business.
- ii. A place of business. This refers to some facilities used by an enterprise to carry out its business. The premises must be at the disposal of the enterprise. The mere presence of the enterprise at that place does not necessarily mean that it is a place of business of the enterprise. The facilities need not be the exclusive location, and they need not be used exclusively by that enterprise or for that business. However, the facilities must be those of the taxpayer, not of another unrelated person. Thus, the regular use of a customer's premises does not generally constitute a place of business.
- iii. The business of the enterprise must be carried out wholly or partly at the fixed place.

⁴ Irish Ch., *Income taxation of Sovereign Wealth Funds*, Working Paper, University of Wisconsin, July 2008.

in the host country or the outbound payment is not attributable to the permanent establishment⁵.

2.3. Third group: other types of income

The third group comprises all the income that does not fall in the previous categories. This type of income is generally exempt from host country income taxes. The most common tax exemptions at host state level are usually granted to: gains from the sale of stocks, bonds, and other securities; gains from the sale of business inventory not attributable to a permanent establishment and interests paid to foreign investors on debt obligations and bank deposits⁶.

**THE THIRD GROUP
COMPRISES ALL
THE INCOME THAT
DOES NOT FALL
IN THE PREVIOUS
CATEGORIES**

3. TAXATION OF SWF INVESTMENTS

3.1. SWF investments

SWFs are sovereign investors that aim at investing, domestically and/or abroad, the wealth owned by a state, often in order to prevent risks of waste of assets, inefficient allocation of resources, or uncontrolled market effects such as a rise of inflation.

Hence, SWFs are important promoters of a sustainable development, especially in

⁵ According to the OECD Model Tax Convention, if the foreign investor has a permanent establishment in the host country and the outbound payment (i.e. interests, royalties, dividends) is attributable to that permanent establishment, the income is taxed on a net basis in the same fashion as the other income of the permanent establishment (because of the fact that the *beneficial owner* of the recurrent income is the permanent establishment).

⁶ Irish Ch., *Income taxation of Sovereign Wealth Funds*, Working Paper, University of Wisconsin, July 2008.

countries still lacking a stable and predictable internal market (i.e. economies in transition and developing countries). Therefore, we can state that the taxes imposed by host states on the investment activities of foreign SWFs have a huge impact on the development of the home state's domestic market, since a higher or lower tax burden can affect the returns and thus the final disposable amount available to the government owning the fund.

Having a look at the investment targets of SWFs in general, most of the addressees of SWFs investments are in developed countries. Investments are often located in North America and Europe⁷. The reason behind these investment flows is that US and European capital markets meet three fundamental requirements: a wide selection of investment opportunities, safe currencies and high level of liquidity.

Due to these investments trends (from developing countries to developed and mature markets), most of the information about the tax treatments granted to SWFs usually regards developed countries. However, the SWF Law Centre is constantly updating and gathering the forms of tax treatment of SWF investments at length.

**THE SWF LAW
CENTRE IS
CONSTANTLY
UPDATING AND
GATHERING THE
FORMS OF TAX
TREATMENT OF SWF
INVESTMENTS AT
LENGTH**

⁷ According to public data, from 1995 to mid-2008, 37% of the total transaction volume of SWF investments was related to North American enterprises, and 32% to Europe-based firms.

3.2. Taxation of the income generated by foreign SWF

An overview of the tax treatment granted to SWF investments in host countries starts from grouping the case practice into three main groups listed according to the 'exemption factor':

- (i) unilateral exemption granted by the host state pursuant to domestic laws;
- (ii) reciprocal exemption granted by home state and host state domestic laws or as a result of bilateral tax treaties between the two;
- (iii) no tax exemption granted.

3.2.1. Unilateral exemption granted by host state domestic laws

The first group comprises countries providing unilateral exemptions for SWFs on their investment income. The exemption is granted as an extension of the doctrine of sovereign immunity. Due to the widespread adoption of the restrictive theory of sovereign immunity, with immunity no longer applying to commercial activities of foreign government enterprises, unilateral tax exemption should apply to passive investment income and not to income coming from commercial activities. Nevertheless, the practice is quite surprising. The United States, the United Kingdom, Australia and the Philippines belong to this group.

The United States

The United States grant unilateral exemption to foreign governments according to Section 892 of the Internal Revenue Code. As a matter of fact, by implementing the sovereign immunity doctrine, the US tax system grants a tax exemption to

**THE FIRST GROUP
COMPRISES
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SWFS ON THEIR
INVESTMENT
INCOME AS AN
EXTENSION OF
THE DOCTRINE
OF SOVEREIGN
IMMUNITY**

SWFs as foreign investors owned by a foreign government⁸.

The United Kingdom

The UK grants individual tax exemptions to SWFs on a case by case basis, through a statement of the HM Treasury. The UK practice shows that when a SWF is an integral part of a foreign government it will benefit from tax exemption. Since the UK follows the principle of absolute sovereign immunity, according to which one state does not attempt to tax the activities of another state, the UK Government usually treats all passive income and gains beneficially owned by a foreign government (and a SWF) as being immune and thus exempted from direct taxes⁹.

**THE UK GRANTS
INDIVIDUAL TAX
EXEMPTIONS TO
SWFS ON A CASE BY
CASE BASIS**

8 Pursuant to Section 892 of the Internal Revenue Code, the income earned by foreign governments on investments in the United States in stocks, bonds, or other domestic securities, financial instruments held in enforcement of governmental financial or monetary policies, or interest on bank deposits in the United States, is exempt from taxation. The exemption does not apply to commercial activities. According to the doctrine of sovereign immunity, the exemption should be limited to activities that are related to the sovereign functions of the government. The definition of commercial activity under Sec. 892 is as follows: “any entity engaged in commercial activities (whether within or outside the United States) if the government (i) holds (directly or indirectly) any interest in such entity which (by value or voting interest) is 50% or more of the total of such interests in such entity, or (ii) holds (directly or indirectly) any other interest in such entity which provides the foreign government with effective control of such entity”. See also, among others: J. Bird-Pollan, *The unjustified subsidy: Sovereign Wealth Funds and the foreign tax exemption*, in *Fordham Journal of Corporate & Financial Law*, Vol. XVII, 2012 pp. 987-1021; M. Knoll, *Taxation and the competitiveness of Sovereign Wealth Funds: do taxes encourage Sovereign Wealth Funds to invest in the United States?*, in *Southern California Law Review*, Vol. 82, 2009, pp. 703-767; V. Fleischer, *A theory of taxing Sovereign Wealth*, Illinois Law and Economics Research Paper Series, 2008.

9 HM Revenue and Customs, INTM155010 – *Sovereign and Crown Immunity*, <http://www.hmrc.gov.uk/manuals/intmanual/INTM155010.htm> (Directorate of Legal Research for International, Comparative, and Foreign Law – Law Library of the US Congress, *Taxation of the passive income of foreign governments and Sovereign Wealth Funds in selected foreign countries*, May 2008).

Australia

As a practice of the Australian Taxation Office (ATO), Australia exempts SWFs from income tax on investments in Australia when all the following requirements are met:

- the investor is a foreign government or an agency of a foreign government performing government functions. This requires that the foreign investor be either a government or an instrument of the government;
- the monies being invested are and will remain government property, and the foreign government entity is, and will remain, the beneficial owner of the assets and income derived from those assets;
- the income derives from a non-commercial activity¹⁰.

In order for the SWFs to be granted the exemption, they must obtain a private binding ruling from the ATO. Nevertheless, the process of codification of such practice into Australian domestic law is still going on. The Australian

**AUSTRALIA EXEMPTS
SWFS FROM
INCOME TAX ON
INVESTMENTS IN
AUSTRALIA WHEN
ALL THE FOLLOWING
REQUIREMENTS ARE
MET**

¹⁰ A commercial activity is an activity concerned with the trading in goods and services. Owning an equity interest is considered non-commercial if it meets certain requirements. Although it remains unclear what that threshold is, a 10% or less equity investment is generally considered as non-commercial (PwC, *Sovereign Wealth Funds: Investment trends and global tax risks – Asia*, May 2010).

Treasury started a consultation procedure that has led to a draft legislation, still pending¹¹.

The Philippines

The income derived from investments in the Philippines by foreign governments, financial institutions owned or controlled by foreign governments, and international or regional financial institutions established by foreign governments, is exempt from income tax¹². Therefore, the income derived from SWF investments in loans, stocks, bonds or other domestic securities, or from interest on bank deposits in the Philippines that are set up and controlled by a foreign government, is exempt from income tax. The income derived by any other foreign entity that does not fall under these exemptions is generally subject to income tax.

The practice in US, UK, Australia and the Philippines shows that there is no direct relationship between absolute or relative state

THE PRACTICE SHOWS THAT THERE IS NO DIRECT RELATIONSHIP BETWEEN ABSOLUTE OR RELATIVE STATE IMMUNITY ON ONE SIDE, AND PARTIAL OR TOTAL TAX EXEMPTION ON THE OTHER SIDE

¹¹ In keeping with its goal of encouraging foreign investments in Australia, the Federal Government will change the existing laws to ensure that foreign pension funds and SWFs can access the Managed Investment Trust (MIT) withholding tax regime. This regime allows a MIT to make payments to non-residents at concessional withholding tax rates, offering an attractive Australian investment option for foreign funds should they and their members be ultimately based overseas. Whether a foreign trust (such as a foreign pension fund or a SWF) meets the relevant requirements under the tax laws applicable to MITs, it can qualify for the concessional tax treatment.

However, since its inception in 2008, the major hurdle for funds interested in investing in Australia has been the law itself, that has prevented foreign funds from obtaining the concessional rate due to difficulties in its implementation.

¹² SEC 32 (B) (7) (a) of the National Internal Revenue Code (NIRC) states that the income earned from investments in the Philippines in loans, stocks, bonds or other domestic securities, or from interest on bank deposits in the Philippines by (i) foreign governments, (ii) financing institutions owned, controlled, or enjoying refinancing from foreign governments, and (iii) international or regional financial institutions established by foreign governments shall not be included in the gross income and shall be exempt from taxation.

immunity on one side, and partial or total tax exemption on the other side, even when both state immunity and tax exemption are granted by domestic laws, and apply automatically or on a case by case basis.

3.2.2. Reciprocal exemptions granted by home state and host state domestic laws or by bilateral tax treaties

A second group consists of governments that exempt foreign governments and their SWFs only on a reciprocal basis. This exemption may come from domestic laws or bilateral double taxation treaties.

Canada

Canada does not have a detailed legislation dealing with the taxation of income generated by foreign authorities or governments. The Canada Revenue Agency has issued on the matter an Information Circular¹³ describing the Agency's position, according to which a foreign government, a central bank or a "foreign government agency"¹⁴ may be granted an exemption from tax on certain forms of Canadian-source investment income according to the doctrine of sovereign immunity.

In order to qualify for the exemption, (i) the foreign country has to grant a reciprocal treatment to Canada, and (ii) the investment income must derive from the exercise of a function of governmental nature; it cannot come from an industrial or commercial activity carried out by the foreign entity.

**A SECOND GROUP
CONSISTS OF
GOVERNMENTS THAT
EXEMPT FOREIGN
GOVERNMENTS AND
THEIR SWFS ONLY ON
A RECIPROCAL BASIS**

**A FOREIGN
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BE GRANTED AN
EXEMPTION FROM
TAX ACCORDING
TO THE DOCTRINE
OF SOVEREIGN
IMMUNITY**

¹³ Information Circular Number: 77-16R4 Date: May 11, 1992. Available at <http://www.cra-arc.gc.ca/E/pub/tp/ic77-16r4/ic77-16r4-e.txt>.

¹⁴ The definition of "foreign government agency" has not been clarified by the CRA.

The exemption applies to withholding tax on arm's length interest, portfolio dividends on listed company shares and — according to both the practice and the case law — to capital gains¹⁵. In order to benefit from the exemption, SWFs must apply to the Canadian Revenue Agency for a written authorization, granted because the income is considered as property of a foreign government or central bank.

Singapore and Malaysia tax treaty

Singapore and Malaysia have signed a bilateral tax treaty effective from January 1st, 2007 granting to both countries reciprocal exemption for the income generated by their governmental entities abroad (the tax treaty provides for a withholding tax on the interest paid to non-residents not exceeding 10%¹⁶).

Other bilateral tax treaties (i.e. between Singapore and Japan, or Norway and Russia), contain reciprocal exemptions for the interest paid to foreign governments, local authorities and their agencies¹⁷.

Japan

Japan does not provide for a tax exemption applicable to foreign government entities. SWFs are considered as foreign corporations and are normally subject to the Japanese tax law applicable to foreign corporations. However,

15 Canadian Tax Highlights, Volume 19, Number 6.

16 Article 11 of the Singapore-Malaysia Tax Treaty. Available at http://www.iras.gov.sg/irasHome/uploadedFiles/Quick_Links/newsingaporemalaysiadta13feb2006.pdf.

17 See http://www.iras.gov.sg/irasHome/uploadedFiles/Quick_Links/singaporejapandta.pdf and <http://www.regjeringen.no/en/dep/fin/Selected-topics/Taxes-and-Duties/skatteavtaler/Skatteatale-Norge-Russland-vedlegg2.html?id=107028>.

bilateral income tax treaties signed by Japan may grant a different treatment to SWFs.

New Zealand

No tax exemption to SWFs is provided for by the tax system in New Zealand. Foreign SWFs are taxed like any other non-resident taxpayer, unless specific conditions have been granted according to a bilateral income tax treaty.

Norway

The tax system in Norway seems not to grant any exemption to SWFs. However, bilateral income tax treaties may grant a specific tax treatment to certain SWFs.

Pakistan

No exemption to foreign SWFs is granted under Pakistani domestic tax law. Hence, foreign SWFs are generally taxed like any other non-resident taxpayer. Nevertheless, SWFs may be eligible for exemption pursuant to a bilateral treaty, like any other non-resident taxpayer.

South Korea

The tax system in South Korea treats foreign SWFs as non-resident taxpayers. However, bilateral income tax treaties may provide for a tax exemption being granted to SWFs.

Thailand

In Thailand, foreign SWFs are taxed like any other non-resident taxpayer. However, SWFs may benefit from tax exemptions applicable to governments if they qualify under the definition of 'Government' in a relevant income tax treaty.

3.2.3. No tax exemption granted

In the third group we find countries with no special provisions for SWFs and other

**BILATERAL INCOME
TAX TREATIES
SIGNED BY JAPAN
MAY GRANT
A DIFFERENT
TREATMENT TO SWFS**

**IN THE THIRD GROUP
WE FIND COUNTRIES
WITH NO SPECIAL
PROVISIONS FOR
SWFS AND OTHER
GOVERNMENT-
OWNED AND
GOVERNMENT-
CONTROLLED
ENTITIES**

government-owned and government-controlled entities, such as China, Germany, Hong Kong, India, Indonesia, Malaysia, Poland, Singapore, Sri Lanka, Switzerland and Vietnam (among others).

China

The tax system in China does not grant tax exemption to foreign SWFs on China-sourced income. Foreign SWFs are taxed as non-resident taxpayers pursuant to China's Corporate Income Tax law. Foreign SWFs may qualify for special tax treatment according to bilateral income tax treaties signed by China, subject to an approval procedure for passive income (i.e. dividends, interest, capital gains) or a record-filing procedure for active income (i.e. business income of a permanent establishment).

**FOREIGN SWFS
ARE TAXED AS
NON-RESIDENT
TAXPAYERS
PURSUANT TO
CHINA'S CORPORATE
INCOME TAX LAW**

Germany

Germany has no special tax provisions for foreign governments, including SWFs. Hence, foreign governments and their SWFs are considered as foreign corporations investing in Germany and taxed accordingly. Foreign investors' interest income and capital gains from shares are generally exempt from tax¹⁸.

Hong Kong

No exemption to foreign SWFs is granted by domestic tax law in Hong Kong. SWFs are taxed like any other non-resident taxpayer.

India

The tax system in India does not provide for any specific exemption from taxation to SWFs, that are taxed like any other non-resident taxpayer.

¹⁸ Directorate of Legal Research for International, Comparative, and Foreign Law – Law Library of the US Congress, *Taxation of the passive income of foreign governments and Sovereign Wealth Funds in selected foreign countries*, May 2008.

Indonesia

No exemption for foreign SWFs is granted by domestic tax law in Indonesia. SWFs are taxed like any other non-resident taxpayer.

Malaysia

No exemption to foreign SWFs is granted pursuant to Malaysia domestic tax law.

Poland

The tax system in Poland does not provide any special regime regarding SWFs; hence, no tax exemption applies to SWFs.

Singapore

There is no specific provision in Singapore's domestic tax regime providing for income tax exemption on the passive income of foreign SWFs.

Sri Lanka

The tax system in Sri Lanka treats foreign SWFs in the same way as non-resident taxpayers.

Switzerland

The tax system in Switzerland does not provide for any domestic rule exempting foreign SWFs from the taxation of their passive income in Switzerland.

Vietnam

The tax system in Vietnam does not provide for any domestic rule exempting foreign SWFs from taxation on their passive income in Vietnam. Foreign SWFs are taxed the same way as other non-resident persons but may qualify for a different treatment under income tax treaties to which Vietnam is a party.

**COUNTRY
FOCUS:
RUSSIA**

02

GIUSEPPE LIOTINE

FDI IN RUSSIA, AFTER RUSSIAN CUSTOMS UNION MEMBERSHIP AND WTO ACCESSION

I. INTRODUCTION

During the last World Economic Forum held in Davos, the Russian Prime Minister, Dmitry Medvedev, made a strong call for foreign investments in Russia, and during his first special address speech, he restated that the Federation was ready to become a partner.

Medvedev openly stated that the country hopes to achieve at least a 10% annual growth in investments. The Government of the Russian Federation seeks to transform the country into an open market, and Russia's recently acquired WTO membership might strongly promote its attractiveness to foreign investors.

The statement of the Russian Prime Minister should be read in the light of the country's development in the past decade, grown by an annual average rate of 4.9%¹⁹, while real disposable income has doubled. Russian growth

**THE COUNTRY
HOPES TO ACHIEVE
AT LEAST A 10%
ANNUAL GROWTH IN
INVESTMENTS**

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¹⁹ World Bank, *GDP Growth Database*, <http://data.worldbank.org>.

is obviously based on commodities: revenues are mainly coming from oil and gas, that in 2011 accounted for about half the federal revenue and almost two thirds of the exports²⁰.

In spite of its strategic role in natural resources, Russia has not grown at the same pace as other large emerging economies. Indeed, the growth of China, over the past 20 years, registered a 10% average annual GDP increase²¹. According to the ‘Doing Business in Russia 2012 Report’, the global financial crisis of 2008-2009 has drawn attention in Russia to the fragility of growth based on natural resources. Weak competition, poor investments and lack of innovation constrain growth²²; despite that, in 2009-2010 Russian per capita GDP (USD 11,110) was the highest among BRIC countries.

According to the World Bank’s Enterprise Surveys, in 2009 Russian managers spent 20% of their time dealing with government regulations — more than twice as much compared to their peers in the 10 EU emerging countries²³. Indeed, the main obstacles to growth in Russia seem to be its weak institutional framework, its low degree of success in implementing laws and regulations, and the uncertainty of its legal system.

**WEAK
COMPETITION,
POOR INVESTMENTS
AND LACK OF
INNOVATION
CONSTRAIN
GROWTH**

**THE MAIN
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IMPLEMENTING
LAWS AND
REGULATIONS, AND
THE UNCERTAINTY
OF ITS LEGAL SYSTEM**

²⁰ World Bank - Russian Federation Partnership, *Country Program Snapshot*, April 2012, World Bank.

²¹ World Bank, *GDP Growth Database*, <http://data.worldbank.org>.

²² *Doing business in Russia 2012 Report* (IBRD, IFC, World Bank).

²³ These 10 EU countries include the 8 Central European countries that joined the European Union in 2004: Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Slovak Republic and Slovenia; plus Bulgaria and Romania, that joined the EU in 2007, “EU 10 Regular Economic Report,” World Bank, 2011.

2. RUSSIA'S ATTRACTIVENESS FOR FDIS

Recent researches²⁴ show that Russia is, together with Poland, the rising star in Eastern Europe. With 7% of first-choice votes from investors, it ranks as the fourth most attractive country in Europe, just one percentage point behind the UK.

While Russia is becoming an interesting target for many investors, it still pays the price of a lack of confidence. Such a contradiction is due to the fact that Russia's growing economy is mainly based on high export prices for oil and gas, but started only recently to develop a strong domestic market. The Russian consumer market counts over 140 million people and can rely on vast natural resources, a highly educated workforce, technologically advanced research and production capabilities. In particular, the Russian workforce is becoming more and more well educated, highly productive and affordable, and provides the hands and minds for expanding manufacturing and services²⁵. Of course, political tensions and requests for democracy still do matter.

Two relevant and recent facts should be taken into account when assessing Russia's foreign investment attractiveness. The first one is the approval, in December 2011, of the 'accession package' to the World Trade Organization (WTO). A perceived lack of transparency in the Russian

RUSSIA'S GROWING ECONOMY STARTED ONLY RECENTLY TO DEVELOP A STRONG DOMESTIC MARKET

TWO RELEVANT AND RECENT FACTS SHOULD BE TAKEN INTO ACCOUNT WHEN ASSESSING RUSSIA'S FOREIGN INVESTMENT ATTRACTIVENESS

²⁴ Russia attractiveness survey 2011, Ernst & Young, October 2011.

²⁵ Russia attractiveness survey 2011, Ernst & Young, October 2011.

political, legislative and administrative environment has caused almost twenty years of negotiations and unease for inward investors, but the recent WTO membership is supposed to provide some partial reassurance and support an opening of Russian business sectors to foreign investors. The second relevant recent event is the establishment, in January 2012, of a common economic space among the Eurasian Economic Communities, based on a Customs Union between Belarus, Kazakhstan and Russia, and aimed at economic integration.

3. RUSSIA'S ACCESSION TO THE WTO

After 18 years of negotiation, on August 22nd, 2012, the WTO welcomed the Russian Federation as its 156th member. The terms of accession were adopted by the WTO at the Ministerial Conference in Geneva, in December 2011. The Russian Parliament ratified the agreement in July 2012, thus completing a long accession process that started back in 1993.

In order to comply with the terms of accession, Russia agreed to a number of commitments including:

- gradually reducing subsidies and lowering import duties in agriculture and manufacturing sectors (by around 2-3 percentage points on average);

AFTER 18 YEARS OF NEGOTIATION, ON AUGUST 22ND, 2012, THE WTO WELCOMED THE RUSSIAN FEDERATION AS ITS 156TH MEMBER

- relaxing restrictions on foreign entry in services sectors such as insurance and telecommunications²⁶;
- reducing non-tariff barriers and reforming the general trade-related legislative framework;
- introducing a legislation ensuring the compliance of technical standards with WTO disciplines;
- limiting future agricultural subsidies;
- introducing non-discriminatory tariffs for the trans-shipment of goods through the country;
- reducing customs administration inefficiencies and enforcing intellectual property rights.

Many provisions include transitional periods of up to nine years, depending on the sector. After the accession, Russia initiated the procedure for entering the Organization for Economic Co-operation and Development (OECD)²⁷.

WTO membership sends a strong signal to foreign investors, stating that the country complies with international rules, standards, principles and generally accepted practices. An increase in the transparency and consistency of policymaking will also be a critical factor in attracting foreign investors in the near future²⁸.

3.1 Accession effects: relevant data

The World Bank has forecast that in the medium term Russia's accession to the WTO will cause an increase in the economic growth of the Russian

**MANY PROVISIONS
INCLUDE
TRANSITIONAL
PERIODS OF UP
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DEPENDING ON THE
SECTOR**

**RUSSIA'S ACCESSION
TO THE WTO WILL
CAUSE AN INCREASE
IN THE ECONOMIC
GROWTH OF THE
RUSSIAN ECONOMY
BY BETWEEN 1%
AND 3%**

²⁶ See Jensen J., Rutherford T., Tarr D., *Telecommunications reform within Russia's accession to the World Trade Organization*, World Bank Policy Research Working Paper, 3501, 2005.

²⁷ IBRD, *Transition Report 2012*, Integration Across Borders.

²⁸ Russian Analytical Digest No. 119, 21 October 2012.

economy by between 1% and 3%, whereas in the long-run the increase might reach 11%²⁹.

The European Commission estimates that the Russian membership will produce relevant effects in terms of saving about 2.5 billion Euro on custom import duties, and will also lead to an increase of exports from EU towards Russia by about 3.9 billion Euro³⁰.

According to World Bank estimates, the increase of FDI in services sectors might turn out to be the most relevant outcome of Russia's WTO accession. This is primarily due to Moscow's commitments to open public procurement and services sectors (banking, insurance, telecommunications and transportation³¹) to foreign investment.

It has been estimated that the reduction in the barriers to FDI may generate an improvement in Russian welfare – on average across regions – by 3.7% of GDP. Together with WTO membership, barrier reduction should contribute to an improvement in Russian welfare by 0.3% and 0.7% respectively. Thus, accounting for about

29 ECIPE Bulletin No. 04/2012, *Russia in the WTO: Unriddling the Mystery of Russia's Trade Policy*.

30 Relevant consequences coming from Russia's accession to the WTO are also related to bilateral treaties and economic relations between EU and Russia. See, for example, Dragneva R., Wolczuk K., *Russia, the Eurasian Customs Union and the EU: cooperation, stagnation or rivalry?* Chatham House briefing paper, 2012; Jouralev A., *The effect of the European Union's unbundling provisions on the EU-Russian natural gas relationship and Russia's accession to the World Trade Organization*, working paper, 2011, available at: <http://ssrn.com/abstract=1969502>.

31 Tarr D., *Russian WTO Accession: what has been accomplished, what can be expected*, The World Bank, Policy Research Paper, 2007. See also: Rutherford T., Tarr D., *Regional impacts of Russia's accession to the World Trade Organization*, World Bank Policy Research Working Paper 4015, 2006; Lissovolick B., Lissovolick Y., *Russia and the WTO: the 'gravity' of outsider status*, IMF Working Paper, 2004.

85% of the gains from WTO accession, the most important effect derives by far from the reduction in the obstacles to FDI in the services business³².

3.2 Benefits of Membership

The countries that joined the WTO with at least the same level of uncertainty that surrounded the Russian accession have all benefited from a step-up in economic growth and inward investment. In all of these precedents, the crucial element was not the mere act of joining the WTO, but the pace of the internal reforms required to comply with the increased foreign competition that followed WTO membership. World Bank studies show that all the 15 transition economies that joined the WTO implemented a broader and deeper set of reforms than before their joining. Of course, some scholars pointed out that, as Russia has already adopted many of the measures associated with WTO membership, and the cost base has risen so much over the past 10 years, the benefit of membership will probably be very limited in the near future³³.

WTO MEMBERSHIP PROVIDES AN IMPROVED REGULATORY FRAMEWORK FOR FOREIGN INVESTORS AND SETS A LONG-TERM INCENTIVE FOR THE RUSSIAN INDUSTRY TO BECOME MORE EFFICIENT

32 Shepoylo O., Tarr D., *Impact of WTO accession and the Customs union on the bound and applied tariff rates of the Russian Federation*, The World Bank Policy Research Working Paper, 2012; Tarr D., *Russian WTO accession: Achievements, impacts, challenges* OECD, 2008. See also Tarr D., *Political economy of Russian Trade policy: early transition, Customs Unions, WTO accession and protection for industrial diversification*, working paper, available at <http://ssrn.com/abstract=1396813>; J. Jensen, Rutherford T., Tarr D., *The impact of liberalizing barriers to foreign direct investment in services: the case of Russian accession to the World Trade Organization*, working paper.

33 Troika Dialog, *Russia: The Director's Cut – Somewhere over the rainbow: winners and losers of WTO Entry*, August 2012. See also Tarr D., *Political economy of Russian Trade policy: early transition, Customs Unions, WTO accession and protection for industrial diversification*, working paper, available at <http://ssrn.com/abstract=1396813>, where the A. considered the WTO accession as an instrument of economic development and domestic modernization.

On the other hand, WTO membership provides an improved regulatory framework for foreign investors and sets a long-term incentive for the Russian industry to become more efficient in facing the increase in foreign competition. In this perspective, WTO membership is a significant step that adds to the hopes that the next government will foster improvements towards a free economy and, starting to address the perception of a high country risk, will seek a greater involvement of foreign manufacturing and service companies in the economy. The advantages of WTO membership include:

- access to foreign markets and provision of non-discriminatory treatment for Russian exporters;
- access to the international dispute settlement mechanism;
- a more favorable climate for foreign investments in Russia;
- conditions for a growth in domestic production quality and competitiveness.

It is a common understanding³⁴ that WTO membership will therefore mark the time for the government's agenda to create greater efficiency and diversification in the economy. The terms and conditions of such a revolution are still to be assessed. This is something investors will only find out over the next few years. Nevertheless, the strong political support to WTO membership makes observers think and hope that the time for opening the market to (even foreign) investments is now.

**THE TERMS AND
CONDITIONS OF
SUCH A REVOLUTION
ARE STILL TO BE
ASSESSED**

³⁴ Troika Dialog, *Russia: The Director's Cut*.

This changing regulatory environment has still to cope with the common obstacles to growth: corruption, political interests opposed to the change, intrusive bureaucracy, unreliable rule of law and uncertainty in the judicial review of administrative decisions are all well-known barriers to investment and growth in Russia. Hence, the effective implementation of reforms on public administration and justice is strategic in order to let WTO membership opportunities have a chance to operate.

THIS CHANGING REGULATORY ENVIRONMENT HAS STILL TO COPE WITH THE COMMON OBSTACLES TO GROWTH

4. THE EURASIAN CUSTOMS UNION

Started in 1995, the Eurasian Customs Union (ECU) was finally established on January 1st, 2010 among Russia, Kazakhstan and Belarus, pursuing the free movement of goods among those three countries through the creation of a single customs area. Controls at the borders were removed on July 1st, 2011 and since January 1st, 2012 the three countries have started operating as a single economic area³⁵, and plan to start a Eurasian Economic Union in 2015.

THE EURASIAN CUSTOMS UNION (ECU) WAS FINALLY ESTABLISHED ON JANUARY 1ST, 2010 AMONG RUSSIA, KAZAKHSTAN AND BELARUS

The ECU is a vehicle for reintegrating the post-Soviet area (Russia is still seeking to include

³⁵ A first treaty among Russia, Belarus and Kazakhstan was signed in 1995. Kyrgyzstan joined in 1996 and Tajikistan in 1997, but the Union did not become effective. In 2000 the same member states created the Eurasian Economic Community (EEC), that failed too because of the lack of a legal framework and of common institutions. Then, a master treaty on a Customs Union was signed by Russia, Belarus and Kazakhstan in 2007, and in 2012 the Eurasian Customs Union was formalized.

Ukraine in a regional integration initiative), and is based on a few general principles:

- a common custom tariff (CET, Common External Tariff);
- the removal of duties and obligations on internal trade;
- a single commercial trade policy towards other third countries;
- a shared system of technical regulations;
- common institutions (like the CU Commission, enjoying legal status and enacting directly applicable laws);
- direct effectiveness of Treaty provisions;
- *acquis communautaire* (each step toward a single integrated market is irreversible, and new member states must agree to abide by the existing rules);
- general principles of international law are a source of ECU law;
- principle of legality;
- an effective dispute resolution mechanism: in 2011 the EEC Court entered into force; its rulings are binding on the parties, and the Court can judge on actions brought by states, ECU institutions, but also by private parties (both companies and individuals);
- the ECU functional character towards a single integrated market.

Among the main achievements of the ECU are:

1. a common import customs tariff;
2. the removal of internal borders;
3. a Common Customs Code (CCC), mainly based on Russian customs tariffs (the most expensive

ones among the three countries, so that Belarus and Kazakhstan had to increase their tariffs).

The manifest ultimate goal of the ECU is the free movement of goods, labor capital, workers and enterprises, as well as the harmonization of macroeconomic and structural policies. The Eurasian Economic Commission, a newly established supranational body of the Union (replacing the CU Commission), composed of nine members (three from each country) and aimed at strengthening the ECU institutional framework, is expected to gradually take responsibilities over the national authorities in such areas as competition policies, technical regulations and environmental standards. At the end of 2012, member countries agreed to harmonize their existing agreements and treaties by 2015, before stepping forward a stricter integration.

4.1 The benefits of the Customs Union

The European Bank for Reconstruction and Development Transition Report 2012 (Integration Across Borders³⁶), highlights the following benefits of the Customs Union:

- lower tariff and non-tariff trade barriers are expected to increase trade and enhance consumer choice;
- producers within a regional integration grouping may benefit from the greater market size;
- exporting within a regional area may be a first step towards the expansion of exports worldwide, first by building up export capability taking

**THE MANIFEST
ULTIMATE GOAL
OF THE ECU IS THE
FREE MOVEMENT
OF GOODS, LABOR
CAPITAL, WORKERS
AND ENTERPRISES,
AS WELL AS THE
HARMONIZATION OF
MACROECONOMIC
AND STRUCTURAL
POLICIES**

**AT THE END OF
2012, MEMBER
COUNTRIES AGREED
TO HARMONIZE
THEIR EXISTING
AGREEMENTS
AND TREATIES
BY 2015, BEFORE
STEPPING FORWARD
A STRICTER
INTEGRATION**

36 IBRD, *Transition Report 2012*, Integration Across Borders.

advantage of low tariff and non-tariff barriers within a Union, and then by leveraging on this capability to achieve a competitive advantage in exporting to other countries;

- countries within a regional integration area may build cross-border production chains, improving each other's comparative advantages and subsequently exporting the finished products outside that common area;
- political and economic institutions would benefit and draw strength from a deeper regional economic integration;
- integration may foster the liberalization of services markets, which tend to be subject to greater regulation and protection than commodity markets (even within the European Union they remain fragmented to some extent). Nevertheless, in the context of Eurasian integration there is a huge potential for efficiency gains in these markets, which could be obtained by lowering entry barriers for foreign firms and investors.

Many observers estimate that the ECU's efforts toward a stricter single market could benefit greatly from the Russian accession to the WTO, as the ECU will adjust its rules to standards in order to comply with Russia's WTO accession commitments³⁷.

**THE ECU WILL
ADJUST ITS RULES
TO STANDARDS IN
ORDER TO COMPLY
WITH RUSSIA'S
WTO ACCESSION
COMMITMENTS**

³⁷ See Tarr, D., *The Eurasian Custom Union among Russia, Belarus and Kazakhstan: can it succeed where its predecessor failed?* Working paper, available at: <http://ssrn.com/abstract=2185517>.

4.2 Relationship between Russia's accession to the WTO and the Eurasian Customs Union

Russia's accession to the WTO has had relevant consequences within the Customs Union. The main concern regarded the relations between the Customs Union and WTO regimes, from a perspective of preventing conflicts between the two legal systems, ensuring that Russia will honor its commitments towards the WTO.

Possible conflicts between WTO and Customs Union legal systems are addressed by a specific tool, the Treaty on the Functioning of the Customs Union in the Multilateral System (TFCUMS)³⁸, which entered into force in November 2011. The Treaty ensures that the provisions of WTO agreements, as set out in the Accession Protocol of a Customs Union state (i.e. Russia), become an integral part of the legal system of the Customs Union as of the date of accession of a member state (Russia). Member states are also required to ensure that current and future Customs Union international agreements and internal regulations comply with WTO rules. Hence, one can say without doubt that, pursuant to the TFCUMS, WTO treaties would prevail over Customs Union in case of conflicting provisions.

As a possible consequence of TFCUMS rules, the WTO regime might be extended to all the member states of the Customs Union, with significant positive effects such as transparency

POSSIBLE CONFLICTS BETWEEN WTO AND CUSTOMS UNION LEGAL SYSTEMS ARE ADDRESSED BY A SPECIFIC TOOL, THE TREATY ON THE FUNCTIONING OF THE CUSTOMS UNION IN THE MULTILATERAL SYSTEM (TFCUMS)

AS A POSSIBLE CONSEQUENCE OF TFCUMS RULES, THE WTO REGIME MIGHT BE EXTENDED TO ALL THE MEMBER STATES OF THE CUSTOMS UNION

³⁸ Treaty On the Functioning of the Customs Union in the framework of the Multilateral Trading System, available at: http://ec.europa.eu/food/international/trade/docs/decision_87_eurasec_en.pdf.

and predictability of policy-making in all member states³⁹. Furthermore, in the process of accession to the WTO, Russia has been modernizing its trade regime and embedding it in the ECU⁴⁰. At present, much uncertainty remains as to whether there will be a beneficial and comprehensive impact in the ECU; nevertheless, scholars point out that the provisions of the WTO and the international customs regime (i.e. the Kyoto Convention) are becoming standard reference when it comes to drafting ECU international agreements.

5. FINAL REMARKS

Russia's legal system and economic environment are currently experiencing massive and critical changes that are deeply affecting its national institutions. The accession to the WTO is pushing Russian economy toward a free economy, and Russian companies into an unprecedented competitive arena. On the other hand, the Eurasian Customs Union, a regional integration initiative that is changing quickly into a single market Union, is forcing Russian institutions to deal with a supra-national organization with its own institutions (a Commission, a Court of

**RUSSIA'S LEGAL
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AFFECTING
ITS NATIONAL
INSTITUTIONS**

39 Final Report of the Second EU–Russia International Conference ‘Prospects for a Strategic Partnership’, Brussels, November 2011.

40 Dragneva R., Wolczuk K., *Russia, The Eurasian Customs Union and the EU: Cooperation, Stagnation or Rivalry?*, Chatham House Briefing Paper, August 2012.

Justice) and rules, some of which are directly enforceable in the member states' legal systems.

It is actually impossible to forecast the outcomes and consequences of such a radical change in Russia's economic and legal systems. Nevertheless, scholars and independent observers believe and show that the path is now irreversible, and have started focusing on how the new supra-national institutional framework can be attractive to other ex-CSI countries, and on what effects can a prospective enlargement of the EC Union have on the political and economic relations among the states and, now, between the supra-national organizations (EU and ECU Union).

**SCHOLARS AND
INDEPENDENT
OBSERVERS BELIEVE
AND SHOW THAT
THE PATH IS NOW
IRREVERSIBLE**

**SWF
FOCUS:
ANGOLA**

03

CELESTE CECILIA MOLES LO TURCO

THE UPCOMING AFRICAN SOVEREIGN WEALTH FUNDS: THE FUNDO SOBERANO DE ANGOLA – FSDEA

INTRODUCTION

Sovereign Wealth Funds (SWFs) have emerged as potential solutions to actively manage foreign reserves accumulated from commodity sales or strong exports and they correspond to government-owned investment vehicles managed by a state-controlled entity or external managers, on behalf of the nation, to serve primarily medium to long term economic and financial objectives⁴¹.

They can have different and multiple objectives such as: (i) the stabilization of the economy from the volatility of the prices of the natural

CELESTE CECILIA
MOLES LO TURCO

SWF Strategic
Committee, Italian
Ministry of Foreign
Affairs. The ideas
contained in this
document are those
of the Author alone
and does not necessarily
reflect the views of the
Ministry of Foreign
Affairs.

41 Triki T. and Faye I., *Africa's Quest for Development: Can Sovereign Wealth Funds help?*, AfDB Working Paper Series n. 142, 2011, Tunis.

resources they depend on, protecting from commodity shocks, (ii) the function of reserve fund for the time of economic and financial crisis, (iii) the diversification and internationalization of the domestic economy, (iv) the support of national development, (v) the transfer of wealth across generations and many other goals and missions.

SWFs can pursue some of the above objectives separately or concurrently and this can be done with one main fund or with subdivided funds with specific objectives.

According to Adam D. Dixon and Ashby H. B. Monk⁴², resource-rich developing countries can benefit from setting up, subsequently, three separate SWFs such as: (i) a stabilization fund (ii) a development fund and lastly (iii) a saving fund. Once achieved the main goal of the stabilization of the economy, in fact, the SWF could focus more on fostering national development and on the transfer of wealth to future generations.

Furthermore, as many of the new upcoming SWFs are sponsored by Emerging Countries, as in the case of Angola, Brazil⁴³, Mongolia and others, many of these brand new SWFs are called to perform an important role in the promotion of the development of the sponsor countries.

Development consists not only in increasing the assets of the SWF and in the financial and economic growth of the sponsor country, but it

**MANY OF THESE
BRAND NEW SWFS
ARE CALLED TO
PERFORM AN
IMPORTANT ROLE IN
THE PROMOTION OF
THE DEVELOPMENT
OF THE SPONSOR
COUNTRIES**

42 Dixon A. D., Monk A. H. B., *What role for SWF in Africa's Development?*, Oil to cash initiative background paper, Center for Global Development, October 2011.

43 <http://swfinstitute.com/fund/brazil.php>.

refers to a much wider definition that takes into account the overall wealth of the country and the standard of life of the entire population that is, or should be, the real ultimate beneficiary of the Fund's activities.

In this sense, development includes both social and economic goals, measurable through, the reduction of the country's poverty level, the increase of the standard of life of citizens and the construction of the necessary infrastructures for a sound and prompt development of the country, such as roads, hospitals, schools, etc.

SWF's definition according to the Santiago Principles⁴⁴:

“SWFs are special-purpose investment funds or arrangements that are owned by the general government and created for macroeconomic purposes. SWFs hold, manage, or administer assets to achieve financial objectives, and employ a set of investment strategies that include investing in foreign financial assets. SWFs are commonly established out of balance of payments surpluses, official foreign currency operations, the proceeds of privatizations, fiscal surpluses, and/or receipts resulting from commodity exports. SWFs have diverse legal, institutional, and governance structures. They are a heterogeneous group, comprising fiscal stabilization funds, savings funds, reserve investment corporations, development funds, and pension reserve funds without explicit pension liabilities”.

**DEVELOPMENT
INCLUDES BOTH
SOCIAL AND
ECONOMIC GOALS**

44 Santiago Principles are a set of 24 principles and practices, promoted by the International Forum of Sovereign Wealth Fund (IFSWF) in order to improve SWFs standards of governance, transparency and accountability.

I. UPCOMING SWFS IN AFRICA

The lack of a generally agreed definition of SWFs and of their status, among academics analysts and professionals, leads to different interpretations on the overall number of SWFs, with specific reference to those of the African continent. Some sources, as expressed more in details in the following paragraph, take into consideration only those SWFs that are already active, while others consider also the planned ones and the established but still not active ones. As a result, the number of SWFs could be different, according to different sources, as presented hereafter.

However, combining data from different sources, it is possible to say that Africa counts 11 already active SWFs⁴⁵, 3 established but still not yet completely active SWFs⁴⁶ and 10 only planned SWFs⁴⁷.

**AFRICA COUNTS 11
ALREADY ACTIVE
SWFS, 3 ESTABLISHED
BUT STILL NOT YET
COMPLETELY ACTIVE
SWFS AND 10 ONLY
PLANNED SWFS**

45 Mauritania, Algeria, Libya, Sudan, Nigeria, Gabon, Namibia, Botswana, Equatorial Guinea (2), Sao Tome and Principe.

46 Angola, Ghana, Rwanda.

47 South Africa, Zimbabwe, Zambia, Mozambique, Tanzania, Kenya, Uganda, D. R. Congo, Liberia, Tunisia.

TABLE 1
SWFS IN AFRICA



Source: Elaboration of different sources by the authors (In particular Ashby Monk's blog).

According to the SWF Institute⁴⁸, as for the following table, the total number of African SWFs is 10 and includes those of Algeria, Angola, Botswana, Equatorial Guinea, Gabon, Ghana⁴⁹, Libya, Mauritania, Mauritius⁵⁰ and Nigeria for a total amount of around \$ 139 billion.

48 <http://www.swfinstitute.org/fund-rankings/>.

49 SWF still under development.

50 SWF still under development.

TABLE 2
SWF INSTITUTE LIST OF AFRICAN SWF

FUND	COUNTRY	USD
LIBYAN INVESTMENT AUTHORITY	LIBYA	65 BILLION
REVENUE GENERATION FUND	ALGERIA	56.7 BILLION
PULA FUND	BOTSAWANA	7 BILLION
FUNDO SOBERANO DE ANGOLA	ANGOLA	5 BILLION
NIGERIAN SOVEREIGN INVESTMENT AUTHORITY	NIGERIA	1 BILLION
GABON SOVEREIGN WEALTH FUND	GABON	400 MILLION
NATIONAL FUND FOR HYDROCARBON RESERVES	MAURITANIA	300 MILLION
FUND FOR FUTURE GENERATIONS	EQUATORIAL GUINEA	80 MILLION
GHANA PETROLEUM FUNDS	GHANA	69 MILLION
MAURITIUS SOVEREIGN WEALTH FUNDS*	MAURITIUS	3 BILLION

*Note: proposed.

Source: Sovereign Wealth Fund Institute.

According to Thouraya Triki and Issa Faye⁵¹, the total number of African SWFs is of 15 for a total amount of around \$143 billion and includes Algeria, Angola, Botswana, Chad, Congo, Equatorial Guinea (Future Generations Fund), Equatorial Guinea (Stabilization Fund), Gabon, Ghana, Libya, Mauritania, Namibia, Nigeria, Sao Tome' and Principe, Sudan, as for the following table.

51 Triki T., Faye I., *Africa's Quest for Development: Can Sovereign Wealth Funds help?*, AfDB Working Paper Series n. 142, 2011, Tunis.

TABLE 3
THOURAYA TRIKI AND ISSA FAYE'S LIST OF AFRICAN SWFS

FUND	COUNTRY	DATE OF ESTABLISHMENT	FUNDING SOURCE	FUND TYPE	MOST RECENT ESTIMATE OF AUM (US\$BN)	YEAR
FONDS DE RÉGULATION DES RECETTES	ALGERIA	2000	OIL	STABILIZATION FUND	59.34	2009
FONDS DE STABILISATION DES RECETTES BUDGÉTAIRES	CHAD	2006	OIL	STABILIZATION FUND	0.003	2010
RESERVE FUND FOR OIL	ANGOLA	2004	OIL	STABILIZATION FUND	0.2	2008
PULA FUND	BOTSWANA	1994	DIAMONDS	DEVELOPMENT FUND	6.9	2010
FONDS DE STABILISATION DES RECETTES BUDGÉTAIRES	CONGO	UNKNOWN	OIL	STABILIZATION FUND	1.64	2010
FONDS DE STABILISATION DES RECETTES BUDGÉTAIRES	EQUATORIAL GUINEA	UNKNOWN	OIL	STABILIZATION FUND	1.39	2010
FONDS DE RÉSERVES POUR GÉNÉRATIONS FUTURES	EQUATORIAL GUINEA	UNKNOWN	OIL	DEVELOPMENT FUND	0.080	2010
FONDS SOUVERAIN DE LA RÉPUBLIQUE GABONAISE	GABON	1998	OIL	DEVELOPMENT FUND	0.380	2010
MINERALS DEVELOPMENT FUND	GHANA	1994	GOLD AND OTHER MINERALS	DEVELOPMENT FUND		
LIBYAN INVESTMENT AUTHORITY	LIBYA	2006	OIL	DEVELOPMENT FUND	70	2010
FONDS NATIONAL DES REVENUS DES HYDROCARBURES	MAURITANIA	2006	OIL	STABILIZATION FUND	0.03425	2009
MINERALS DEVELOPMENT FUND	NAMIBIA	1995	MINERALS	DEVELOPMENT FUND	NA	
EXCESS CRUDE FUND (ACCOUNT)	NIGERIA	2004	OIL AND GAS	STABILIZATION FUND	3	2010
NATIONAL OIL ACCOUNT	SÃO TOMÉ AND PRINCIPE	2004	OIL	DEVELOPMENT FUND	0.010	2009
OIL REVENUE STABILIZATION FUND	SUDAN	2002	OIL	STABILIZATION FUND	0.15	2009

Source: Triki T., Faye I., *Africa's Quest for Development: Can Sovereign Wealth Funds help?*, AfDB Working Paper Series n. 142, 2011, Tunis.

According to the AfDB Chief Economist and Vice President, Professor Mthuli Ncube, there are

14 SWFs in Africa representing 3%⁵² of the total of SWFs assets under management.

Other sources include in the list of the African SWFs also the upcoming ones of Kenya⁵³, Liberia, Mozambique, South Africa, Tanzania, Uganda and Zambia whose creation is encouraged by the latest oil discoveries.

Among all the African SWFs, the oldest one is the Pula Fund of Botswana, created in 1994, while the largest one is the Libyan Investment Authority with \$65 billion of assets under management, followed by Algeria's Revenue Regulation Fund with \$56.7 billion of assets under management.

Currently only three of the African SWFs, the Botswana Pula Fund, the Fund for Future Generation of Equatorial Guinea and the Libyan Investment Authority, are members of the IFSWF⁵⁴ and have officially voluntarily ratified the Santiago Principles⁵⁵.

One of the most committed to the sustainable development of the sponsor country and the wealth of its citizens is the Fundo Soberano de Angola (FSDEA).

**CURRENTLY ONLY
THREE OF THE
AFRICAN SWFS ARE
MEMBERS OF THE
IFSWF**

2. ANGOLA AS A GROWING ECONOMY

Since the global economic slowdown experienced in 2008/2009, Angola has been progressively recovering and, the

⁵² <http://www.afdb.org/fr/blogs/afdb-championing-inclusive-growth-across-africa/post/the-boom-in-african-sovereign-wealth-funds-10198/>.

⁵³ <http://www.institutionalinvestor.com/blogarticle/3036532/Blog/Welcome-Kenya-To-The-SWF-Club.html>.

⁵⁴ <http://www.ifswf.org/>.

⁵⁵ <http://www.iwg-swf.org/pubs/eng/santiagoprinciples.pdf>.

country now presents solid economic growth prospects due to higher oil prices and increased spending. According to the AfDB African Economic Outlook 2012⁵⁶, Angola's growth of GDP recorded 8.2% in 2012 and is expected to record 7.1% in 2013. The country is currently rated BB- by Fitch (May 2011), Ba3 by Moody's (June 2011) and BB- by Standard and Poor's (July 2011).

Oil is the backbone of the Angola's economy. After twenty-seven years of a civil war that ravaged the country, Angola has emerged as the second largest oil producer in Africa⁵⁷ with over 1.9 million barrels per day (bpd). In 2011, crude oil, refined oil products and gas exports accounted for more than 95% of the total exports and 47% of the GDP was related to the oil sector. Diamonds were the second main exports driver. According to OPEC estimates, Angola's proven oil reserves reach 10.5 billion barrels (0.9% of the OPEC share⁵⁸).

Angola's dependency on oil is evident. Oil revenue accounts for around 75% of budgetary revenue and oil is the main driver of reserves accumulation. This dependency is the reason why, following the acute oil price drop in

ANGOLA'S GROWTH OF GDP RECORDED 8.2% IN 2012 AND IS EXPECTED TO RECORD 7.1% IN 2013

ANGOLA HAS EMERGED AS THE SECOND LARGEST OIL PRODUCER IN AFRICA

56 <http://www.africaneconomicoutlook.org/fileadmin/uploads/aeo/PDF/Angola%20Full%20PDF%20Country%20Note.pdf>.

57 According to the IMF Country Report No. 12/194, Nigeria produced 2.4 million bpd in 2011.

58 More than 80% of the world's proven oil reserves are located in OPEC Member Countries, with the bulk of OPEC oil reserves in the Middle East, amounting to 66% of the OPEC total. However, the biggest proven reserves are those of Venezuela: 24.8% of the OPEC total.

2008-2009, Angola faced macroeconomic instability and public authorities sought support from the IMF, signing, in November 2009, the IMF Stand-By Arrangement program, which comprises, in particular, fiscal and monetary tightening.

Included in the IMF recommendations was also the establishment of a brand new SWF⁵⁹ as part of the country's commitment in building up a medium-term macroeconomic framework to protect, in particular, against oil price volatility and to create a more resilient and diversified economy.

The diversification of the national economy represents one of the main goals of this new economic deal, able to, on the long term, (i) avoid the effects of the Dutch disease, (ii) foster the overall social and economic improvement of the country (iii) assure the equal distributions of wealth across generations.

Furthermore, many characteristics of the Angola's economy such as being a fast-growing country, with important oil reserves, make the establishment of a SWF recommendable.

Moreover, despite recovering gradually, the country still has to cope with the reduction of poverty particularly in rural areas, the promotion of job-intensive activities and inclusive growth. Income inequalities remain high, unemployment rate is estimated at around 26% (the oil sector is capital-intensive and does not dramatically foster employment, counting less than 1% of the total labor force⁶⁰) and the country is currently

**THE
DIVERSIFICATION
OF THE NATIONAL
ECONOMY
REPRESENTS ONE
OF THE MAIN
GOALS OF THIS NEW
ECONOMIC DEAL**

59 <http://www.imf.org/external/np/loi/2010/ago/082710.pdf>.

60 <http://www.africaneconomicoutlook.org/en/countries/southern-africa/angola/>.

ranked 148 out of 187 countries in the UNDP⁶¹ Human Development Index (HDI)⁶² ranking and is categorized as a “low human development” country.

The Fundo Soberano de Angola could be beneficial for all the above mentioned areas.

3. THE FUNDO SOBERANO DE ANGOLA: A SOVEREIGN WEALTH FUND SET UP TO FOSTER ANGOLA’S ECONOMIC AND SOCIAL DEVELOPMENT

3.1 FSDEA main features

The Fundo Soberano de Angola has been announced in 2008, legally notified in 2011 and officially established on the 17th of October 2012.

FSDEA counts \$5 billion of assets under management and a specific mandate to support the social and economic development of the country through (i) the stabilization of the economy (ii) jobs creation and (iii) wealth transfer across generations.

The FSDEA is funded by oil revenues and it has to experience a yearly increase in assets of \$3.5 billion in order to reach a size of around \$30 billion by 2020. It could then become one of the largest 30 SWFs in the world.

**FSDEA COUNTS
\$5 BILLION OF
ASSETS UNDER
MANAGEMENT
AND A SPECIFIC
MANDATE TO
SUPPORT THE SOCIAL
AND ECONOMIC
DEVELOPMENT OF
THE COUNTRY**

61 United Nations Development Program.

62 The HDI is a way of measuring development by combining indicators of life expectancy, educational attainment and income. A ranking is published every year by the UNPD.

TABLE 4
LIST OF THE 10 BIGGEST SWFS THAT BELONG TO THE IFSWF, BY 2013
(\$US BN)

COUNTRY	FUND	ASSET UNDER MANAGEMENT (\$US BN)	DATE OF ESTABLISHMENT	FUNDING SOURCE
NORWAY	GOVERNMENT PENSION FUND (GPF)	715.9	1990	OIL
THE UNITED ARAB EMIRATES	ABU DHABI INVESTMENT AUTHORITY (ADIA)	627	1976	OIL
CHINA	CHINA INVESTMENT CORPORATION (CIC)	482	2007	FX RESERVES
KUWAIT	KUWAIT INVESTMENT AUTHORITY (KIA)	296	1953	OIL
SINGAPORE	GOVERNMENT OF SINGAPORE OF INVESTMENT CORPORATION (GIC)	247.5	1981	FISCAL SURPLUSES, FX RESERVES
RUSSIA	NATIONAL WEALTH FUND (NWF)	175.5	2008	OIL
SINGAPORE	TEMASEK HOLDINGS	157.5	1974	FISCAL SURPLUSES
QATAR	QATAR INVESTMENT AUTHORITY (QIA)	115	2005	OIL
AUSTRALIA	THE FUTURE FUND	83	2006	FISCAL SURPLUSES
LIBYA	LIBYA INVESTMENT AUTHORITY (LIA)	65	2006	OIL

Sources: <http://www.swfinstitute.org/fund-rankings/>

At the domestic level the FSDEA acts accordingly to the national macroeconomic plan, established and developed by the Government.

Currently, the FSDEA does not have any direct link to Sonangol. However, according to some sources⁶³, the FSDEA could take up the role previously endorsed by the National Oil Company Sonangol that used to buy stakes in companies. As a result, its stakes might be transferred to the Fund.

63 http://taighde.com/w/Fundo_Soberano_Angolano.

The Fund is supposed to be independent from the Government and managed by an independent Board of Directors.

The structure of the Fund comprises: a Board of Directors, an Advisory Council, a Fiscal Council and the executives, as described, more into details, hereafter.

	ROLE	COMPOSED BY
BOARD OF DIRECTORS	Defines the Fund's investment strategy and oversees the Fund's activities and assets.	Chairman: - Armando Manuel ⁶⁴ Member of the Board of director: - José Filomeno de Sousa dos Santos - Hugo Migule Evora Goncalves ⁶⁵
ADVISORY COUNCIL	Reviews investment proposals and the strategy recommendations made by the Board of Directors and offers recommendations to the President of the Republic of Angola who ultimately approves the Fund's investment policies.	- Carlos Alberto Lopes, Minister of Finance - Abraão Pio dos Santos Gourgel, Minister of Economy - Job Graça, Minister of Planning and Territorial Development - José de Lima Massano, Governor of the National Bank of Angola
EXECUTIVE	Executive roles include: - Fiscal Council - Risk Management Committee - Chief Risk Officer - Chief Compliance Officer - External Asset Managers	
FISCAL COUNCIL	Ensures compliance with the laws and regulations applicable to the Fund. The Fund will be subject to regular annual audits conducted by independent auditors.	

Even though the Fund's strategy has not been still officially disclosed, the FSDEA is expected to focus on its domestic market, in fields such as: real estate, infrastructures, hospitality (mainly luxury hotel), agriculture, water, power generation,

⁶⁴ Government's economic affairs secretary.

⁶⁵ Former manager at Standard Bank of Angola and Pension and Development Fund of Angola.

transport, etc. The Fund aims to gradually diversify its investment portfolio across a number of industries and asset classes. It would probably include global private and public stocks, bonds, foreign currencies, financial derivatives, commodities, treasury bills, and real estate and infrastructure funds, being an active partner in these ventures.

The fund main investment objective is pure economic return with a mostly conservative investment strategy that targets a low risk and long-term investments able to provide the Fund with stable returns both in economic and social terms.

**THE FUND MAIN
INVESTMENT
OBJECTIVE IS PURE
ECONOMIC RETURN
WITH A MOSTLY
CONSERVATIVE
INVESTMENT
STRATEGY**

“We are committed to promoting social and economic development investing in projects that create opportunities that will positively impact the lives of all Angolans today and to generate wealth for future generations”, says José Filomeno de Sousa dos Santo a member of the Board of Directors⁶⁶.

In terms of geographical allocation of the investments, it is presumed by different sources that priority will be given to emerging countries, with a focus on Sub-Saharan Africa and Asia, but Europe could also represent a possible target.

The Angolan fund wants to inspire itself from the Government Pension Fund of Norway (GPF), especially on ethical guidelines and social accountability⁶⁷. This has led some observers to expect the FSDEA to replicate the investment strategy of the GPF by purchasing small stakes of common stock in international companies. As in the case of newly launched SWFs and as

⁶⁶ <http://www.angola-today.com/tag/investment/>.

⁶⁷ <http://www.norad.no/en/countries/africa/angola>.

some sources report, the FSDEA will use external management⁶⁸.

With the establishment of a dedicated Social Charter, the FSDEA will consider investments not only on the basis of their profitability, but also on the basis of their capacity to address national social challenges such as access to clean water and healthcare services, and to support government social programs and general economic growth.

The FSDEA will also look to promote the generation of income through small and medium sized enterprises (SMEs), by sponsoring programs aimed at the most economically deprived segments of the society in Angola.

The FSDEA will be guided by a set of values that act as its guiding principles in all its activities.

As a matter of fact, the Fund is committed to operating transparently, responsibly and in full compliance with the laws and regulations of the countries it invests in. In this respect, it is supposed to be committed to the highest level of transparency across all areas of its business. It is fully accountable for all of its actions and always acts in the best interest of the people of Angola and all other stakeholders⁶⁹.

It has also stated it wants to follow the Santiago Principles.

The FSDEA's commitment to transparency has been confirmed by the recent disclosure of the key future milestones to be met by 2013 and 2014⁷⁰ (presented hereafter).

**THE FSDEA
WILL CONSIDER
INVESTMENTS ALSO
ON THE BASIS OF
THEIR CAPACITY TO
ADDRESS NATIONAL
SOCIAL CHALLENGES**

**IT HAS ALSO
STATED IT WANTS
TO FOLLOW
THE SANTIAGO
PRINCIPLES**

⁶⁸ <http://www.businessweek.com/news/2012-12-21/angola-wealth-fund-to-announce-policies-appoint-auditors>.

⁶⁹ www.fundosoberano.ao.

⁷⁰ <http://www.swfinstitute.org/swf-article/transparency-still-remains-elusive-for-most-sovereign-wealth-funds/>.

	2013	2014
FIRST QUARTER	<ul style="list-style-type: none"> - Publication of the FSDEA Social Charter (the Charter will address a number of key social challenges faced by Angolans). - Publication of the Government approved FSDEA Investment Policy. 	<ul style="list-style-type: none"> - The FSDEA annual report. - First Linaburg-Maduell Transparency Index FSDEA rating.
SECOND QUARTER	<ul style="list-style-type: none"> - The appointment of internationally recognized independent auditors. 	-
THIRD QUARTER	<ul style="list-style-type: none"> - The FSDEA mid-year update to include executive commentary on investment activities. 	<ul style="list-style-type: none"> - The FSDEA mid-year update to include executive commentary on investment activities.
FOURTH QUARTER	-	-

In addition to this, the Fund will provide regular updates on its investments and its governance to the public.

The Fund will also promote initiatives in education and healthcare, such as the strategic partnerships with the national tropical disease institutes, in order to increase the access to life saving surgical procedures or the establishments of a first aid help post throughout the rural and suburban areas, in partnership with the International Committee of The Red Cross.

The FSDEA could also represent an important tool for the attraction of other long-term investors and of SWFs' investments. One of the goals of the FSDEA is the promotion of Angola as a destination of foreign direct investments⁷¹ indeed, as it has been the case for the Russian Direct Investment Fund and the Italian Fondo Strategico di Investimento. In fact, the Italian Fund has just recently signed a \$2billion agreement with Qatar

**THE FUND
WILL PROMOTE
INITIATIVES IN
EDUCATION AND
HEALTHCARE**

**THE FSDEA COULD
ALSO REPRESENT
AN IMPORTANT
TOOL FOR THE
ATTRACTION OF
OTHER LONG TERM
INVESTORS AND OF
SWFS' INVESTMENTS**

⁷¹ <http://www.fundosoberano.ao/images/articles/Angola-fund-sees-bright-future.pdf>.

Holding⁷², one of the main arms of the Qatari SWF, Qatar Investment Authority, with the purpose of investing in the Italian excellences of Made in Italy.

3.2 What is the role of the Fundo Soberano de Angola in the development of Angola?

The FSDEA could represent an important tool for the economic and social development of Angola, with specific reference to its capacity to:

1) Fostering the stabilization of the economy against volatility, reducing fiscal pressure and representing a lender of last resort in time of financial turmoil.

SWFs can foster the stabilization of the economy by keeping assets offshore and by insulating resources dependent economies against commodity price swings. They can also function as lender of last resort in time of financial turmoil, reducing the fiscal pressure and the need to rely on external help.

2) Supporting the diversification and internationalization of national economy, and increasing the capacity of attracting Foreign Direct Investments (FDIs).

FDIs are a significant growth driver in developing countries. In this respect, attracting more FDIs is a way to foster the development of the economy. The Angolan SWF could help attract more FDIs by improving the accountability of the country and, eventually, become a direct counterparty for other SWFs and long-term investors. According to

**SWFS CAN FOSTER
THE STABILIZATION
OF THE ECONOMY**

**THE ANGOLAN
SWF COULD HELP
ATTRACT MORE FDIS**

⁷² <http://www.fondostrategico.it/en/news/fsi-and-qatar-holding-sign-jv-to-invest-up-to-2-billion-in-made-in-italy.html>.

the UNCTA⁷³ World Investment Report 2012⁷⁴, “SWFs show substantial potential for investment in development”. Their total FDIs in 2011 reach around US\$125 billion, with about 25% of it invested in developing countries. “SWFs can work in partnership with host-country governments, development finance institutions or other private sector investors to invest in infrastructure, agriculture and industrial development, including the build-up of green growth industries”. Furthermore, the diversification of the economy will help reduce unemployment, which currently stands at 26% of the population.

3) Improving Angola’s credit rating.

The assessment of a country’s credit profile cannot ignore the existence of a SWF. In order to weight positively, the SWF should perform effectively and be part of a set of economic reforms. On this aspect, the newly launched Nigerian Sovereign Investment Authority (NSIA, set up in 2012) is a compelling case in point. Standard & Poor’s and Moody’s raised Nigeria creditworthiness in the aftermath of its creation because it came to life alongside reforms of the banking and electricity sectors. Fitch Ratings identified the establishment of the NSIA as a “key reform” underlining, as well, that it is “an area where progress has been slower than hoped”. As a result, the establishment of a well-managed SWF could improve Angola’s accountability, transparency in the wealth management and attractiveness to foreign investors. Most specifically, the FSDEA could help Angola reach investment-grade category.

**THE SWF SHOULD
PERFORM
EFFECTIVELY AND
BE PART OF A SET OF
ECONOMIC REFORMS**

73 United Nations Conference on Trade and Development.

74 <http://www.unctad-docs.org/files/UNCTAD-WIR2012-Full-en.pdf>.

4) Supporting reduction in poverty⁷⁵ and the increase of the Human Development Index (HDI)⁷⁶.

The reduction in poverty and the promotion of sustainable and inclusive growth are goals common to most of the emerging countries' SWFs. The concept of "inclusive growth" implies sustained and long-term growth that benefits the whole society, including the poorest. According to AfDB definition⁷⁷, inclusive growth is the economic growth that results in a wider access to sustainable socio-economic opportunities for a broader number of people, countries or regions. It also has to protect the vulnerable and must guarantee fairness, equal justice, and political plurality. SWFs could be vehicles to achieve growth of such a nature. A domestic-focused SWF can also increase the human development index (HDI) as the SWF's investments are partly directed to sectors that lead to the improvement of the index such as, among others, infrastructures, water access, health and primary education. In the specific case of Angola, the HDI country's value for 2011 was 0.486⁷⁸ (148 out of 187 countries) and it was constantly ranking in the bottom group ("Low Human Development"). This value is higher than the Sub-Saharan Africa HDI value (0.463) but quite far from other Southern African countries such as Namibia

**A DOMESTIC-
FOCUSED SWF
CAN INCREASE
THE HUMAN
DEVELOPMENT
INDEX (HDI)**

75 Today, in Angola, the level of incidence of poverty is of 36%.

76 The Human Development Index (HDI) is a composite statistic of life expectancy, education, and income indices to rank countries into four tiers of human development. It was created by economist Mahbub ul Haq, followed by economist Amartya Sen in 1990 and published by the United Nations Development Programme.

77 <http://www.afdb.org/fileadmin/uploads/afdb/Documents/Policy-Documents/FINAL%20Briefing%20Note%2006%20Inclusive%20Growth.pdf>.

78 Between 2000 and 2011, it increased from 0.384 to 0.486, an increase of 27.0% or average annual increase of about 2.2%.

(0.625) or Botswana (0.633). On the contrary, it is not so far from Bhutan (which HDI value is 0.522) that is the last “Medium Human Development” country (ranked 141 out of 187). Being part of this intermediary group could be an aim shared by the Angolan SWF and monitoring this index could be a way to assess SWF’s social impact.

5) Supporting national development through the improvement of national infrastructures.

As in all the emerging countries, the need for infrastructures is very high and strictly related to the overall economic development of the country. In the specific case of Angola, the improvement of the infrastructures is one of the main goals to be achieved in order to foster both economic and social growth. A significant example of upcoming project in infrastructure that is supposed to be highly beneficial for the Country is Sonaref, a Sonangol project. Despite being the second oil producer in Africa, Angola has only one small refinery in Luanda that does not have enough capacity to meet the demand of the rapid economic growth. For this reason, Angola annually imports 250 million dollars of petroleum products. To bridge this gap, Sonangol started building Sonaref, a new modern refinery, fully integrating crude oil production and refining.

**THE IMPROVEMENT
OF THE
INFRASTRUCTURES
IS ONE OF THE
MAIN GOALS TO BE
ACHIEVED**

6) Fostering transparency and fight against corruption.

The implementation of a SWF does not guarantee the increase of transparency in the management of public assets on behalf of the sponsor country’s stakeholders. Actually, there are examples of SWFs, which failed to foster transparency in public wealth management and to provide the sponsor country with financial accountability. In order to succeed, a SWF should present a clear and

well-defined mandate and a governance able to assure transparency and accountability through regular reports and audits conducted by independent auditors. In the literature, transparency is identified as a key element of success.

7) Transferring wealth to future generation.

One of the common goals of SWFs is the transfer of the wealth across current and future stakeholders. The capacity of reinvesting current income from natural resources is one of their main tasks. Some SWFs include a fund specifically dedicated to the transfer of wealth across generations, as in the case of Kuwait Future Generations Fund.

**IN THE LITERATURE,
TRANSPARENCY IS
IDENTIFIED AS A
KEY ELEMENT OF
SUCCESS**

CONCLUSIONS

Nowadays SWFs are dramatically growing in popularity and they are increasingly considered as a potential tool for fostering African development. They could represent “a new hope for the resource-rich countries of Africa resolving the paradox of plenty”⁷⁹ as very often the emergence of oil exports brings many benefits such as sustained capital inflows that could lead to current account surpluses and a build-up in foreign exchange reserves but, as well, poses significant challenges such as an increased need for sterilization and, eventually, the threat of Dutch disease.

Currently, international academics wonder whether SWFs, and more specifically the African ones, could succeed in redirecting income

79 Dixon A. D., Monk A. H. B., *What role for SWF in Africa's Development?*, Oil to cash initiative background paper, October 2011, Center for Global Development.

from natural resources to the economy. There are also interrogations on their effectiveness in supporting the social and economic development of the sponsor country and of the entire region, promoting intra-African investments, enhancing productivity, fostering inclusive growth and bridging the infrastructures' gap.

It is difficult to find a unique answer due to the heterogeneity of national economic situations, to the different nature of SWFs and of the tools used in order to measure their effectiveness. However, it is generally acknowledged that in order to be successful, a SWF must have a clear mandate, guaranteeing sound governance principles, accountability and transparency.

Where for Governance it is intended the rules in place defining the role of the Government, of the governing bodies and of the managers and their independency, with specific reference to the inflow and outflow of money. Transparency is related to the detailed communication of the fund role and objectives and, as well, the timely provision of information on the fund's activities and operations. Accountability is best appraised through the degree to which the SWF and its governing bodies are responsible for their decision as in Tsani, Ahmadov and Aslanli work⁸⁰.

This assumption is specifically valid for the Fundo Soberano de Angola, and for the upcoming African Sovereign Wealth Funds, whose effectiveness will be related to these three essential elements and to the capacity of monitoring and communicating the social and economic goals achieved in order to become a model for many other SWFs.

**IN ORDER TO BE
SUCCESSFUL, A SWF
MUST HAVE A CLEAR
MANDATE**

⁸⁰ Tsani S., Ahmadov I., Aslanli K., *Governance, transparency and accountability in Sovereign Wealth Funds: Remarks on the assessment, rankings and benchmarks to date*, Public Finance Monitoring Center, March 2010.

Yet, one of the major challenges faced by the FSDEA and other African SWFs, is the capacity to adapt rules of corporate governance to ensure real independence from short-term political interests.

Consequently, the structure of a SWF is just as important as its investment decisions, if not even more, in terms of SWF's effectiveness and accountability.

A sound governance and a prompt information on the goals, on the results, and on the overall benefits would help the Fundo Soberano de Angola gain trust and support from the public opinion, avoid failures and the possibility that a direct distribution of the SWF's wealth to the population could be wished as a better option for Angola⁸¹.

**ONE OF THE MAJOR
CHALLENGES FACED
BY THE FSDEA IS
TO ENSURE REAL
INDEPENDENCE
FROM SHORT-TERM
POLITICAL
INTERESTS**

81 http://www.cgdev.org/section/initiatives/_active/revenues_distribution.

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**FDI: NEW
BILATERAL
INVESTMENT
TREATIES
2011-2012**

FDI: NEW BILATERAL INVESTMENT TREATIES

BILATERAL INVESTMENT TREATIES (BITS) ARE CRUCIAL FOR PROTECTING PUBLIC OR PRIVATE INVESTMENTS ABROAD. THIS IS A LIST OF AGREEMENTS ENTERED INTO FORCE OR SIGNED IN 2011 AND 2012.

REPORTER	PARTNER	DATE OF SIGNATURE	DATE OF ENTRY INTO FORCE
RUSSIAN FEDERATION	ANGOLA	26-JUN-09	12-JAN-11
FINLAND	NEPAL	03-FEB-09	28-JAN-11
CZECH REPUBLIC	UZBEKISTAN	24-AUG-09	16-FEB-11
CZECH REPUBLIC	GEORGIA	29-AUG-09	13-MAR-11
CZECH REPUBLIC	SAUDI ARABIA	18-NOV-09	13-MAR-11
CZECH REPUBLIC	SERBIA	04-JUN-10	16-MAR-11
CZECH REPUBLIC	INDIA	08-JUL-10	24-MAR-11
KOREA	LUXEMBOURG	12-DEC-06	27-MAR-11
TURKEY	YEMEN	07-SEP-00	31-MAR-11
SINGAPORE	MEXICO	12-NOV-09	04-APR-11
ESTONIA	MOLDOVA	18-JUN-10	21-APR-11
CZECH REPUBLIC	GUATEMALA	20-AUG-09	04-MAY-11
BANGLADESH	INDIA	09-FEB-09	07-JUL-11
SERBIA	SWITZERLAND	07-DEC-05	20-JUL-11
CROATIA	ROMANIA	30-APR-10	20-JUL-11
UNITED ARAB EMIRATES	TURKEY	28-SEP-05	24-JUL-11
SPAIN	VIETNAM	20-FEB-06	29-JUL-11
KOREA	CONGO	08-NOV-06	13-AUG-11
SLOVAKIA	VIETNAM	17-DEC-09	18-AUG-11
SLOVAKIA	MACEDONIA	25-JUN-09	25-AUG-11
CHINA	UZBEKISTAN	19-APR-11	01-SEP-11
CZECH REPUBLIC	MOLDOVA	02-SEP-08	14-SEP-11
KUWAIT	MACEDONIA	08-APR-08	02-NOV-11
CANADA	ROMANIA	08-MAY-09	23-NOV-11
CANADA	LATVIA	05-MAY-09	24-NOV-11
INDIA	LITHUANIA	31-MAR-11	01-DEC-11
AZERBAIJAN	SERBIA	08-JUN-11	14-DEC-11
KOREA	URUGUAY	01-OCT-09	08-DEC-11
OMAN	VIETNAM	10-JAN-11	-
UNITED ARAB EMIRATES	BANGLADESH	17-JAN-11	-
PORTUGAL	SENEGAL	25-JAN-11	-

REPORTER	PARTNER	DATE OF SIGNATURE	DATE OF ENTRY INTO FORCE
ALBANIA	MALTA	27-JAN-11	-
NIGERIA	TURKEY	02-FEB-11	-
BAHRAIN	TURKMENISTAN	09-FEB-11	-
KUWAIT	PAKISTAN	15-FEB-11	-
CONGO	PORTUGAL	03-MAR-11	-
TANZANIA	TURKEY	11-MAR-11	-
BOTSWANA	ZIMBABWE	21-MAR-11	-
CZECH REPUBLIC	SRI LANKA	28-MAR-11	-
CROATIA	ISRAEL	30-MAR-11	-
UNITED ARAB EMIRATES	SUDAN	04-APR-11	-
JAPAN	PAPUA NEW GUINEA	26-APR-11	-
RUSSIAN FEDERATION	EQUATORIAL GUINEA	06-JUN-11	-
INDIA	SLOVENIA	14-JUN-11	-
BOSNIA AND HERZEGOVINA	SAN MARINO	02-AUG-11	-
CHINA	CONGO	11-AUG-11	-
INDONESIA	SERBIA	06-SEP-11	-
COLOMBIA	JAPAN	12-SEP-11	-
AZERBAIJAN	MONTENEGRO	16-SEP-11	-
KUWAIT	CANADA	26-SEP-11	-
QATAR	ALBANIA	18-OCT-11	-
INDIA	NEPAL	21-OCT-11	-
AZERBAIJAN	TURKEY	25-OCT-11	-
UNITED ARAB EMIRATES	PORTUGAL	19-NOV-11	-
KENYA	SLOVAKIA	14-DEC-11	-
RWANDA	UNITED STATES	19-FEB-08	01-JAN-12
LITHUANIA	MACEDONIA	08-MAR-11	13-JAN-12
CANADA	CZECH REPUBLIC	06-MAY-09	22-JAN-12
CZECH REPUBLIC	URUGUAY	15-MAY-09	09-FEB-12
AZERBAIJAN	CZECH REPUBLIC	17-MAY-11	09-FEB-12
QATAR	MACEDONIA	20-MAY-11	13-FEB-12
CANADA	SLOVAKIA	20-JUL-10	14-MAR-12
CZECH REPUBLIC	TURKEY	29-APR-09	18-MAR-12
QATAR	TIMOR LESTE	21-JAN-12	-
RUSSIAN FEDERATION	NICARAGUA	26-JAN-12	-
ALBANIA	AZERBAIJAN	09-FEB-12	-

REPORTER	PARTNER	DATE OF SIGNATURE	DATE OF ENTRY INTO FORCE
ALGERIA	SERBIA	13-FEB-12	-
KUWAIT	JAPAN	22-MAR-12	-
MOROCCO	VIETNAM	15-JUN-12	-
GABON	TURKEY	18-JUL-12	-
IRAQ	JAPAN	07-AUG-12	-
CHINA	TAIWAN	08-AUG-12	-
RUSSIAN FEDERATION	ZIMBABWE	07-OCT-12	-
ARMENIA	IRAQ	07-NOV-12	-
HAITI	SPAIN	17-NOV-12	-

**BOOK
REVIEW**

SILVIA VENTURINI

SOVEREIGN INVESTMENTS – CONCERNS AND POLICY REACTIONS¹

This book includes detailed and carefully collected original data on SWFs and SOEs (state owned enterprises) that will be of enormous value to researchers and policy-makers. The first part gives a general overview of both the rise of SWF and SOE and of their role in the current financial pattern. The second part deals with regulatory concerns, mostly related to SWF and SOE targets and intentions. The third part focuses on changing the rules applicable to state-controlled entities, at national (US, Canada, Germany and European Union laws and regulations are reviewed) and international level (OECD and IMF applicable rules are dealt with).

This book investigates in 21 comprehensive chapters the active role played by sovereign capital in the international market. As investors, States diversify the allocation of their sovereign funds over sectors, industries, and cross borders. Conversely, as investment targets, states provide for a restrictive regulation (mostly ownership restrictions in particular sectors). When states investing abroad ask for a treatment that they don't guarantee to foreign investors domestically, target states claim for reciprocity conditions. An international regulation based on voluntary constrictions and obligations (best practices and codes of conduct) has not been fully implemented

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BY SOVEREIGN
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yet, and anyway, it does not seem to be an adequate deterrent. National regulation is influenced by the fear of SWF political or strategic goals rather than purely business-oriented purposes and by threats to national security or strategic industries, a fear that is intensified by the lack of transparency on governance, investment goals and targets.

One of the main values of the book is that it discusses this trend, focusing on both the two major expressions of state investments in the international market: SWF and SOE, delving into the accompanying concerns and policy reactions of host countries to their growing activity as well. Such approach is crucial because the difference between SWFs and SOEs seems apparently clear, but when it comes to practice it becomes extremely thin. Furthermore, host states often do not differentiate their treatment in respect of sovereign investments according to the vehicle used by the home state to invest (a fund or a company). Finally, there are many types of SWFs (classified by governance, transparency, accountability, goals, targets, types of investments) and models of SOEs (centralized, decentralized and dual models).

A second strong point of the book is its multidisciplinary approach: legal and economical points of view are addressed one after the other allowing the reader to look at the big picture and not only focus on the details. National concerns and consequent reactions restricting foreign investments are investigated, and so is international regulation, highlighting both the legal barriers and their economic *raison d'être* and consequences. This is a critical approach, if one wants to understand the fast-moving changes

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in a new international financial environment and consider their implications for global and regional financial architectures.

A third relevant issue raised by this book is the analysis of the relationship between the changes in the financial environment due to the new sovereign role played by states as investors on one side, and other important consequences of the recent geopolitical developments on the other side. The perspectives of developing countries, the impact and consequences of the crisis (whether and to what extent can SWF be considered as stabilization factors, for their long-term investment horizon), the recent changes in global finance, the relationship between SWFs and mutual funds, hedge funds, pension funds, are all deeply interconnected matters. Hence, the book's interdisciplinary approach gives us a comprehensive vision of the picture from many perspectives at once. And the picture, considering also the current fast-moving changes in global finance exhaustively discussed by the book, looks very much like a Cubist work with a sprinkle of Futurism.

All in all, this book gives us a state-of-the-art pattern of the new role played by many states in the economic scenario, and poses many questions, that law scholars and economists are called to answer, about such aspects as: a possible definition and classification of state investment vehicles (SWF, SOE, etc ...); a comparative analysis of SWF and SOE, highlighting their similarities and differences (in terms of structure, accountability, transparency, governance, purposes); a comparative analysis of national and supra-national regulation, on both sides (active and

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passive, i.e. considering states both as investors and investment targets); how the fast development of state investments abroad is rapidly changing the ways and tools that states use to protect their investments abroad, both at a bilateral and multilateral level; the influence of such trend on related fields of international law and economics, such as human rights and environmental protection, emerging economies' development, sustainable finance.

The debate will certainly move on from this fundamental book towards many directions and deal with specific matters, but it won't make much progress without considering that law, economics and ethics; national, supra-national and international levels; investments, development and human rights are all different, interconnected facets of one big picture.

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SWF LAW CENTRE SERVICES

Legal assistance to SWFs, LTIs, host states, home states, companies and banks.

INTERNATIONAL INVESTMENT REGULATIONS

A fully up-to-date pattern with international multilateral and regional rules on investments and a legal assessment.

NATIONAL REGULATION ON INVESTMENTS

A fully up-to-date database with national laws on investments, and a legal assessment.

COUNTRY LEGAL RISK

Assessment of the legal risk of investing in a target country.

LEGAL STRUCTURE AND GOVERNANCE

Relationships between SWFs and LTIs legal structure, governance rules, and national and international rules on investments.

BILATERAL INVESTMENT TREATIES

Assessment of SWF home state's BITs in force and changes suggested to better protect sovereign investments.

DISPUTE SETTLEMENT RESOLUTION

Legal assessment of BITs' DSR clauses and legal assistance on arbitration.

SOVEREIGN IMMUNITY AND INVESTMENTS

Immunity from jurisdiction and from execution, and investment protection.

PROMOTING SOVEREIGN INVESTMENT OPPORTUNITIES

How to attract sovereign and long-term investments focusing on specific projects or regions.

PROMOTING SOVEREIGN AND LONG TERM INVESTMENTS IN EQUITY, INFRASTRUCTURES, PUBLIC PROJECTS

How to attract sovereign and long-term investments by implementing national laws.

ASSESSING THE LEGAL RISK: BITS AND SOVEREIGN IMMUNITY

Legal risk assessment of sovereign investments according to applicable bilateral and multilateral international rules related to investments and state immunity.

LEGAL ASSISTANCE

Legal assistance on specific investments in target companies, banks, institutions.

