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# Investing in Iraq: Legal and Political Aspects

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## Investing in Iraq: Legal and Political Aspects

*Bart S. Fisher\**

One of my favorite children's books is *What Do People Do All Day* (1968), authored by Richard Scarry. What I do all day is make deals. I am a "deals guy" in the international business arena. Essentially, I run a dating service for U.S. companies wanting to get into Iraq. In April 2002, Rubar Sandi and I co-founded the U.S.-Iraq Business Council. This was almost a year before the war. We could see that Saddam Hussein's reign was coming to an end. He was going to be taken out one way or the other. It was certainly in the interest of the U.S. business community and the U.S. government for Iraq to privatize, join the international economic community, and to remove the state from the commanding heights of the Iraqi economy. These changes would inevitably lead to political reforms. I applied to the Office of Foreign Assets Control ("OFAC") for a license from its director Rick Newcomb, seeking permission to set up something that would be legal under the trade embargo on Iraq at the time. On October 9th, 2002, the OFAC issued a license that authorized us to engage in dialogue and exchange information but no more, since the embargo prevented us from consummating any transactions. We were the only entity with a license from OFAC to open up the market for Iraq before Saddam was out.

I worked on this project for commercial reasons and because I had a confluence of friendships with Iraqis. We could also bring in U.S. companies because we had the information and the Iraqi partner to be able to do so. The only problem was it was illegal to do deals and consummate transactions until the war, which started in March of 2003. I remember that we planned to have a program regarding Iraq's economy at the Center for Strategic and International Studies ("CSIS"). The program was initially scheduled for the end of March. However, CSIS called me about March 10th and told me the program should go forward on March 18th. I realized that CSIS knew something was happening so we moved the program up to March 18, 2003. Thus, I have lived with this issue of privatization of Iraq for the last two years.

In terms of this conference, it is very interesting to compare and contrast the Iraq situation with China and Russia, as there are significant distinctions. For starters, what is happening in Iraq may be the central foreign policy issue in this year's Presidential election in the United States. Although China has political salience in terms of jobs and outsourcing issues, which has recently cropped up is a big political issue, this is not nearly as high on the political Richter Scale as Iraq. Russia appears to be an absolute afterthought in political terms this year, which, to me, is a barometer of the sea of change in the U.S. political dialogue brought by 9/11.

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George Santayana once said that “those who forget history are condemned to repeat it.” The history behind the current Iraq situation is that before the war in Iraq, the country lived under restrictive United Nations (“UN”) sanctions for thirteen years. Iraq faced no-fly zones and an economic embargo that greatly injured the Iraqi people, particularly the most vulnerable of the Iraqi people, children and the elderly. The combination of the negligence of the Saddam Hussein regime, the impact of sanctions, and the March 2003 war in Iraq, left the country with an infrastructure in virtual rubble when the United States marched in.

To come to the topic of the conference, reconstruction of a country that had been really obliterated was the task at hand. I mention these well known facts as background because the salient political question here is how long will the patience of the American people last? Will it last long enough to build the infrastructure required? American tax payers will soon want to spend money on schools and hospitals in Boise instead of Baghdad. The \$18.6 billion dollars of fresh supplemental appropriations is the tip of the iceberg of what will be required. In reality, the cost will be closer to \$70 billion just to provide aid. At the current appropriations level, it would take five years to provide the amount of aid necessary for reconstruction. I do not see that happening. That is the conundrum we have. To put it bluntly, Iraq is a basket case. Under Saddam, the annual per capita income fell approximately eighty percent, to about \$250. This was done by a regime that placed the state at the commanding heights of the economy in Iraqi society. In other words, the storyline of the last half of the twentieth century involves other governments embracing capitalism, selling off companies, and privatizing what they had previously nationalized, seeking to entice multinational enterprises into their domains that they had formerly expelled decades earlier, reducing state control in favor of entrepreneurship and allowing markets, rather than governments, to occupy the commanding heights of society. Well, like the rest of the Middle East, Iraq missed that whole storyline. Instead, the story in the Middle East is one of stagnation. This area languished economically, largely because the state refused to loosen its control of the economy. It is hard to believe, looking at it now, but this area was once the foremost military and economic power of the world.

Whether the United States is an occupying power from a legal standpoint or not, its initial task in Iraq has been to deconstruct the country, reconstruct it, and then try to replace the state-owned enterprises. For example, in the cement industry, there are five state-owned enterprises that make cement. What are we going to do, start new ones? Are we going to take a share of the private ones? How are we going to go forward? And should we dismantle this whole situation? Obviously the order to disband the army caused significant controversy. These are fundamental questions that only history can judge as to whether Paul Bremer, U.S.-Iraqi civilian administrator, made the right decisions here.

I guess a question now is how successful has our mission been? To answer that question, reading today’s newspaper can be very informative. The situation

changes daily. We have a two-tiered governing structure with the Iraqi Governing Council, which was appointed by Bremer on July 13, 2003, advising the Coalition Provisional Authority (“CPA”). The next interesting question relates to the timetable for democracy in Iraq. How is the transition going to happen? By February 28th, the Governing Council will approve a transitional administrative law that defines the structures of a transitional government. In about eight days from now we are going to learn exactly what this choreography will entail. The idea that Bremer floated was that local caucuses choose the delegates for an Iraqi Transitional National Authority, and further that by June 30, 2004, sovereignty would be turned over to Iraq’s Transitional National Assembly. As someone who hardly understands how the Iowa caucus works every four years in Presidential elections, I can tell you this system is not going to work. Clearly, June 30 will remain as the date sovereignty is turned over to the Iraqi government. But there are not going to be caucuses. There will probably be elections in the first part of next year or near the end of this year. The elections issue is very sensitive because it raises parallels to what occurred after the Vietnam War. Unfortunately, there are many parallels with the Vietnam situation. Whether or not this becomes Bush’s Vietnam is yet to be played out.

Parallels can be made regarding voting and elections. In Vietnam, we operated under the Geneva Accords. John Foster Dulles and the U.S. government did not agree to proceed with elections in Vietnam in 1956 because Dulles assumed that Ho Chi Minh would win and the U.S. government did not want that to happen. In the present case, the United States does not want to see the election of a Shiite Muslim fundamentalist regime. This is why elections have not been held already. Ayatollah Sistani wants elections, so we are not holding them right now. There is a rope-a-dope game being played on the elections issue, which is very significant politically in terms of the turnover. My prediction is that sovereignty will be turned over to the Iraqi Council and the Governing Council will be expanded to add to its legitimacy. If the Governing Council expands in a way that increases its credibility in the eyes of the Iraqi people, then there is hope that the turnover will be successful. The Iraqi people must believe that Iraqis are really running the new government, not a bunch of foreigners who did not suffer through the horrors of thirty years under Saddam. The current Governing Council was hand-picked by Bremer and his people, and as a result, it looks too much like an American creation.

As far as privatizing Iraq, a regime has been established. As the occupying power, we have great discretion under the CPA. U.N. Resolution 1483 actually provides the authority to promote economic reconstruction and we have operated under this resolution. In fact, operating under the Resolution is a matter of international law. Occupying powers have broad discretion to change the laws of the country to ensure that it functions. The first pillar is to establish an investment law. In this case, the law is CPA Order No. 39, which provides for equal treatment of foreign investors. The idea is that foreign investors and foreign entities are entitled to make investments in Iraq on terms no less

favorable than Iraqi interests. The exception here is that foreign direct and indirect ownership of natural resources is not covered by this rule. Even given the exception, the CPA established a very foreign investment friendly regime. So the first step to privatize an economy is to have a friendly investment regime.<sup>1</sup>

The second pillar is the creation of banking law. When you are setting up a country, you must have a banking regime. The one set up in Iraq is an extremely liberal, pro-foreign banking regime, which allows foreign banks to control up to six Iraqi banks through the end of 2008. Thereafter, the amount of foreign ownership of banks that can be acquired or controlled by foreign banks is unlimited. After 2008, the market will be completely open. At that point, potentially all the banks could be owned by foreign investors under the law. Obviously these provisions were designed to bring foreign capital into the banking sector of Iraq. Thus, the second pillar, the banking law, has been set up, and that is CPA Order No. 40.

The third pillar is the tax law. A new tax law has been set up, which provides that the highest individual and corporate tax rates shall not exceed fifteen percent. This is important, particularly because it is low, friendly and simple.

The next step is trade liberalization. All charges for goods entering the country have been removed except for a five percent fee, a so-called reconstruction levy. So that is pretty simple—only a five percent tariff is charged. We are seeing a regime set up that is investor friendly, banker friendly, and trade friendly. As a result, privatization has proceeded. Thus far, the U.S. government has tried to promote privatization through foreign aid. The exercise now is to execute contracts with the CPA under tenders that are due back February 5, 2004. The decisions on the \$18.6 billion will be made by March 6, 2004. This decision involves the oil sector, the electricity sector, security, and transportation. Transportation actually is very significant because it includes railroads, seaports, airports, and a huge amount of construction work. The CPA and Agency for International Development (“AID”) contracts created what I call the “New Mandarins.” The New Mandarins are nine big companies who run the economy of Iraq outright, not in tandem with Iraqi Nationals. The group includes companies such as Bechtel, Halliburton, The Louis Berger Group, DynCorp, and Stevedoring Services of America. These are major multinational enterprises based in the United States. Each company has a key point person. This person is not the top person in the company but is in charge of dealings in Iraq. At Bechtel, the key person is Terry Valenzuela. At DynCorp, it is Paul Carter. These are not

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1. Of course, establishing the investment law does not resolve all the problems that might arise for investors. For example, I represent Harris Corporation, a telecom company that has a broadcasting contract for Iraq. At one point, the Iraqi communications minister said that after June 30, 2004, he would no longer recognize the contract. As it turns out, he read about the contract in the newspaper and received misinformation. He was upset about what he had read and spoke out about the contract. Supposedly he calmed down later and said that Harris would still have the contract after June 30, but nothing is certain. This problem happens across the board. This uncertainty is one of the major reasons many of the big oil companies are not investing yet. These companies are not going to invest a lot of money that could go away June 30.

household names like the presidents of the companies, but they are very important people and they all know each other. The interesting thing is what I call the “subcontractor prime game.” This involves the nine primary companies subcontracting work. You always want to be a sub to a prime if you cannot be the prime.

So, I am running a multinational dating service for U.S. companies who want to get into Iraq. However, they cannot get in without an Iraqi partner. Four or five great merchant families of Iraq survived the Saddam regime, like the Al-Bunnia family and others. The purpose of this requirement is to employ Iraqi people. You will not receive a contract if you do not plan on employing a lot of Iraqis. This is a key part of your application.<sup>2</sup>

Looking back now, what are the lessons of this elective war? I think the first and most important is that when you shoot, you have to kill. Having made the decision to enter Iraq, we have no choice but to stay the course and see that the transition does not fail. Otherwise, our credibility will be shot. The second lesson is that it is nice to have friends, especially when you want to pull out of the situation, and this should be our whole attitude. Be nice on the way up because you see the same people on the way down. This lesson applies in Washington as well. Now we are in Iraq, we need the UN, we need allies, and we need friends, or we need to get out politically in a most desperate way. Yet we are still there. Now we are forced to reach back to the UN and that is the irony of this whole situation.

Earlier we heard an interesting discussion regarding Kosovo. Professor Ed Villmoare stated that it will take generations to recover in Kosovo. This begs the question for what is required in Iraq. Thinking about the UN building in Iraq being blown up is sobering. Now the UN is clearing out and does not want to return to Iraq—waiting generations is a very long commitment. In my opinion, Iraq faces possible compounding problems, which people are not talking about. I think there may be a September surprise in Iran as well. We made a major move in Middle East foreign policy by trying to change Iraq around and attempting to create a role model. Iraq is going to be the role model, but the ripples will go in directions that we cannot foresee.

I would say the final lesson we have yet to figure out is how to accomplish the Iraq transition in a way that avoids a major diversion in the war on terror. There is a danger of diverting attention from the war on terror, and that is what troubles me so much. I really think the jury is out on how the events will play themselves out. We are facing imminent deadlines of February 28, 2004, for the

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2. The fundamental purpose of this requirement is that we are supposed to be rebuilding Iraq for the Iraqi people, not large American corporations. Thus far, however, there have been a number of fundamental problems with implementing this notion. The process has really been tilted against the Iraqis, with the exception of those familiar with western culture. For instance, if the tender used is only in English, many Iraqi people cannot read it. If you cannot read the tender, you cannot bid for a contract. Moreover, Iraqis are not used to filling out U.S. government forms. The forms are complicated. To resolve this problem, I hired lawyers from Washington to fill out the forms. Overall, the process needs to be easier for Iraqis to get involved.

announcement of the plan and June 30, 2004, for the turnover of sovereignty. However, our people, our army, and our security forces will not leave. As long as they are there they will be targets, and we all will be, in the Middle East for a long time to come. Given the war, the first concern is security and the ability to just walk down the street safely. We are not there yet.