

The constitutional and legal factors that determine the 51/49 rule, and its effect on foreign direct investment flows.

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Abstract:

Rule 51/49 is an economic law passed in Algeria under the 2009 Supplementary Finance Act, the purpose of which is to regulate foreign investment in the country. The regulation stipulates that Algerian partner, whether from the public or private sector, must hold a majority stake of 51% of the capital in any investment project involving a partnership with a foreign investor, while the foreign investor's stake is limited to 49%. The introduction of this regulation was driven by the objective of safeguarding the national economy and ensuring economic sovereignty, with a particular focus on maintaining control over investment projects in vital and strategic sectors such as energy, hydrocarbons, mining, transport, and pharmaceuticals.

Keywords: rule 51/49; foreign investment; strategic sectors.

1. INTRODUCTION

The 51/49 rule is an Algerian economic law that regulates foreign investment. The agreement stipulates that the Algerian partner (whether public or private) must hold a minimum of 51% of the capital in any foreign investment project in Algeria, while the foreign investor is permitted to own a maximum of 49%. This regulation was endorsed under the 2009 Supplementary Finance Law, which was presented to parliament by the then-Prime Minister, Ahmed Ouyahia. The objective of the law was to safeguard

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national economic sovereignty and ensure Algeria's control over its resources and economic initiatives.

During the 1990s and early 2000s, Algeria experienced economic challenges due to low oil prices and the aftermath of civil war. In response, the government implemented policies designed to attract foreign investment while preserving national control.

Prior to 2009, Algeria had permitted a greater degree of freedom for foreign investors, a move that gave rise to concerns regarding the possibility of foreign takeovers of strategic sectors, including hydrocarbons and natural resources.

the 51/49 rule was incorporated into the supplementary finance law as part of a strategy to strengthen economic sovereignty. The objective was to guarantee that control over investment projects remained with Algerian partners, particularly in key sectors.

The regulation stipulated that foreign companies must partner with an Algerian entity to hold a majority stake (51%) in any project, whether in the productive or commercial sectors. This requirement applies to all foreign investments.

In light of the aforementioned points, the following question can be posed:

What are the constitutional and legal foundations that underpin the application of Rule 49/51?

This issue gives rise to several questions: What impact has this regulation had on the influx of foreign investment into Algeria?

Despite the regulatory constraints, could digital transformation enhance Algeria's attractiveness as a potential investment destination?

The research is based on an analytical approach to Algerian legal texts, drawing on a number of studies, particularly when examining the relationship between foreign direct investment flows and the application of the 51/49 rule in foreign partnerships.

1- The stages and circumstances surrounding the adoption of the 49-51% foreign investment rule in Algeria:

1-1partnership that occurred during the socialist phase:

France leveraged its advantageous position to safeguard its investments in

Algeria under the Evian Agreement. This agreement ensured that French companies operating on Algerian soil and companies predominantly owned by French nationals could conduct their operations under conditions that prevented any form of discrimination. In return, Article 19 of the agreement permitted the transfer of real estate to the Algerian state, with the exception of real estate deemed necessary for the operation of temporary or permanent facilities, in agreement with the Algerian authorities. Decree No. 64/258 of August 27, 1964, established a national commission tasked with confiscating the property of individuals who committed acts contrary to the revolution. Prior to that, French Order No. 58/1111 of 22/11/1958 regulated oil investments in the aftermath of independence, under which several long-term contracts were concluded with foreign companies with reduced tax burdens.

Following the political change of 1965, Decree No. 66/284 dated 15/09/1966 was issued, containing the Investment Law. The authorities moved towards adopting the partnership model and relied on the national institution, Sonatrach.

This is a tool that can be used to gradually acquire shares in foreign companies.

Examples of such companies include British Petroleum, Mobil, Izo, and Total. Consequently, it has monopolized distribution channels without exerting control over exploration and exploitation, and it has adopted a 51% participation rate.

The 1970s were a significant period in reducing the role of foreign investment in Algeria. A nationalization policy was implemented, affecting several sectors before and after 1971.

In 1971, the 51 percent rule was imposed on partnerships with foreigners, regarded as a sovereign principle that could not be waived. Despite the government's attempts to raise the percentage of foreign investment in 1986 and 1989, these efforts were unsuccessful due to the rejection of the people's representatives. (berrahlia, 2018, p. 10)

The 49-51 rule has been a topic of considerable debate, especially following its extension to other sectors through the 2009 supplementary finance law, which saw it applied for the first time outside of the hydrocarbons sector. It is possible that the government's decision to

implement these measures was influenced by the entry of the French group Lafarge into the Algerian market and its subsequent repurchase of the cement manufacturers in Mascara and M'Sila, which were previously owned by Orascom Cement, without prior notification.

In this transaction with Lafarge, Orascom Construction Industries made significant capital gains, including a profit of around \$2 billion after three years of presence in the Algerian market.

The group has also benefited from a number of facilities from banks in the country, as well as investment aid and significant tax exemptions.

Six months later, the state conducted a comprehensive review of foreign investments in Algeria, introducing the right of pre-emption and the 49/51 rule. Many investors and businessmen have since attested to the adverse effects or deterrent effect of these measures on investment.

A number of partners in Algeria have formally requested the removal of this rule as part of the ongoing process.

The negotiations for its accession to the World Trade Organization have been ongoing since June 1987. (djebbar & lebig, foreign investment rule 51-49 in Algeria between two conjunctures: the necessity of adoption and the call for abandonment, 2019, p. 195)

1-2the market entry phase:

From 1993 to 2009, the 49/51 partnership rule was not in force in the field of foreign investment. It was applied at the discretion of the parties involved, with the exception of the legal controls that were in place in this context. Despite the security challenges experienced in Algeria during the 1990s, which resulted in a decline in economic activity, particularly foreign investment, the subsequent period of enhanced security was sufficient to attract foreign investment to the country.

It is also important to note the negative repercussions of these investment projects. This prompted the legislator to adopt the rule of majority partnership for the national party.

Please find below the relevant article, which refers to Article 58 of the 2009 Supplementary Finance Law.

Order 03-01, which relates to investment development, was amended, and Article 4 bis 1 was added. The second paragraph of this article states that:

"Foreign investments are permitted only within the framework of a partnership where the national contribution constitutes a minimum of 51% of the share capital. The national contribution refers to the aggregate contributions made by all partners."

Indeed, the Algerian legislature has once again adopted the minimum partnership rule.

The field of foreign investment served to legitimise the political authority's position within the state. On 21 December 2008, the head of government issued four directives regarding new investment arrangements, which were described as restrictive provisions on investment freedom. Among these

Please find below instructions relating to the requirement that foreign partners should own no more than 49% of the capital of the investment project. At the time, the government sought to reassure foreign investors and mitigate the severity of the President of the Republic's statement on the reality of investments. The instruction stated that foreign investors could be the first contributors in Algeria, given that the national party's share would be distributed among several shareholders. Following the decline in investments in Algeria by approximately 54% during the second half of 2008, the political authority's initiative was only taken after the 'Jazzy' case.

In 2008, it was discovered that this was due to the transfer of profits to the parent company, Orascom Holding, without reinvesting them in Algeria. The situation was further exacerbated by the company's refusal to settle its debts to the Algerian treasury in the form of tax arrears, which resulted in

A situation involving tax evasion, in exchange for the privileges obtained from the Algerian state by the company.

The provisions contained in the 2009 Supplementary Finance Act can thus be described as a robust response by the Algerian state to the behaviour of many foreign investors.

the policy pursued through the 1993 Investment Law (Decree 12-93) needs to be reviewed. However, after years of applying these provisions

the question of constraining foreign investment freedom in Algeria was once again raised, with particular reference to the 51/49 rule. (bouhlais, 2019, p. 143)

1-3 the reservation of a percentage of the partnership for foreign

entities.

Prior to the enactment of Law 09-16, it was anticipated that the legislator would explicitly state its position on the 51/49 investment rule, either by including it in the text or by abandoning it altogether. Many researchers had anticipated the latter position. However, the legislature did not wait for the investment law to be passed but announced its position on the minimum partnership rule in advance through the 2016 Finance Law, which states in Article 66 that foreign participation in the production of goods and services and imports is linked to the establishment of a company in which the national resident holds at least 51% of its capital.

This is a clear application of the minimum partnership rule, whereas Law 09-16 completely disregarded the partnership rule, as the latter repealed all provisions of Order 03-01, including the text of Article 4 bis, added and amended by the Finance Laws as part of Order 03-01. It is also important to note that the legislator repealed Article 55 of the Finance Law of 2014.

This refers to the necessity of respecting the minimum partnership rule with regard to benefiting from tax and quasi-tax privileges. (bouhlais, 2019, p. 144)

-2Constitutional and legal determinants of the 49/51 rule:

1-2Constitutional framework:

The principle of freedom has always been considered a fundamental tenet within the domain of investment law, as articulated in Article 4 of Decree 03-01 on investment development. This principle is in alignment with the new economic policy and liberal approach that has been introduced by Article 37 of the 1996 Constitution. Notably, the principle of freedom of investment and trade has been formally adopted as a constitutional principle. (amirouche, Constitutional enshrinement of freedom of investment in Algeria, 2017, p. 1228)

In 2009, the legislature approved a new legal framework for foreign investment in Algeria, pursuant to Order 01-09 relating to the Supplementary Finance Act for 2009. This new framework, known as the 49/51 rule, allows for investment within the framework of a partnership. The same principle was confirmed by the Finance Act for 2010. From the legislator's perspective,

and in line with the field of regulated activities, the principle of partnership is not considered an exception or restriction on the freedom of investment, which is already subject to a specific legal framework.

Article 4 bis of Decree 09-01 stipulates that 'foreign investments aimed at producing goods and services must be made within the framework of a partnership in which the resident national partner holds 51 per cent of the capital'. The same applies to foreign trade activities, which require

The adoption of the partnership principle, with at least 30 per cent of the capital value allocated to the national operator, is essential for the successful implementation of this initiative.

In this context, some texts in various fields of economic activity have defined the partnership principle in accordance with each field.

Here we refer to the provisions of Article 11 of Decree 183-09, which specifies the conditions for practising maritime transport assistance, requiring a minimum participation of 40 per cent of the capital value for the benefit of the national operator in relation to the foreign investor, whether a natural or legal person.

With regard to banking activities, Decree No. 04-10, amending and supplementing Decree No. 03-11 on currency and credit, stipulates that the minimum partnership ratio for national operators in the banking sector is 51 per cent of the capital. In fact, this is not the first time that the Algerian legislature has imposed this principle. Partnership was first included in Decree No. 22-71, which defines the framework within which foreign companies may operate in the field of liquid fuel exploration, and then in Law

13-82 4, amended by Law 13 -86 on mixed economic companies, which set a maximum participation rate for foreign partners at 49% 49% of the capital. At the time, the application of this principle was criticised for violating the principle of freedom of international investment and the principle of non-discrimination between foreign and national investors, until it was repealed by the 1990 Monetary and Credit Law. Article 43 now provides the necessary legal basis for the application of compulsory partnership to foreign operators in the context of investment, as it is included in the highest legal text in the Republic. (amirouche, 2017, pp. 1233-1234)

2-2 Legal framework:

the Algerian government has placed significant emphasis on investment as a key driver of economic growth, recognising the need to address shortcomings in various sectors. However, recent amendments in legislation suggest a lack of commitment to the principle of legislative stability, which has led to a decline in foreign investment. Therefore, this principle must be respected due to its great importance in activating the policy of attracting foreign direct investment.

2.2.1. The legal environment in attracting foreign direct investment:

Algerian law has enshrined the principle of freedom of investment in its constitution since 1996, whereby All natural and legal persons, both local and foreign, are at liberty to engage in any activity they wish without discrimination. However, Article 3 of Law 16/09 stipulates that 'The investments referred to in the provisions of this law shall be carried out in compliance with the laws and regulations in force, in particular those relating to environmental protection, regulated activities and professions, and, in general, the exercise of economic activities.' As a prerequisite for conducting business in Algeria, foreign investors are required to obtain a licence from the relevant authorities.

As stated in the article, the objective is to safeguard the environment, public health and national security. Regulated activities are limited to those that generate industrial waste and its conversion, such as the pharmaceutical industry, because they require a study of their environmental impact and the effects of their waste on the environment, both now and in the future. In addition to other activities for which foreign investors are prohibited from obtaining licences, such as the manufacture of weapons and military equipment, environmental taxes must also be imposed on them. (bouhabel & lakhlef, 2021, pp. 314-315)

22.2. Administrative guarantees:

Foreign investors may benefit from all legally established guarantees to encourage investment in host countries, including tax exemptions and financial and monetary facilities that guarantee the right of transfer and freedom of disposal in the investment project. However, these efforts may be rendered futile if foreign investors encounter obstacles at the administrative

level, such as a lack of guidance and information about the investment project, as well as difficulties in completing necessary administrative procedures. These challenges often stem from the bureaucracy that characterises administrative bodies in general.

Investors frequently encounter bureaucratic and routine complications in many sectors related to investment. The banking sector, which still operates in traditional and inefficient ways, is a prime example of this. The customs sector also poses a significant obstacle to foreign investors. In this regard, the matter has adopted these streamlined procedures in the process of accepting investments, and, more importantly, established a new principle that goes beyond the centralisation of the agencies responsible for receiving investments and dealing with investors by enshrining the principle of decentralisation of the one-stop shop. (sellami, 2015, pp. 72-73)

2.2.3. Financial guarantees: Financial guarantees granted to foreign investors include the freedom to transfer funds abroad and compensation for non-commercial risks.

-Freedom to transfer funds: Guaranteeing the transfer of funds is considered one of the most important incentive measures taken by the host country, because not allowing such transfers is considered a form of confiscation. A foreign investor would face significant disadvantages if he were deprived of the right to transfer the funds he invested in the host country, as well as his profits, investment returns, and the proceeds from the transfer or liquidation of his project.

Therefore, the legislator was keen to explicitly enshrine this guarantee in Decree 01-03 on investment development, under Article 31, which states: Investments made through contributions to capital in freely convertible hard currency, the price of which is regularly set by the Bank of Algeria and whose importation is verified as legal, shall benefit from the guarantee of transfer of the invested capital and the returns generated therefrom. This guarantee also covers the net proceeds resulting from the transfer or liquidation, even if this amount exceeds the investor's initial capital."

By extrapolating the provisions of this article, we conclude that the funds subject to transfer are: invested capital, returns on capital investment, and profits resulting from the transfer or liquidation of the investment project,

even if the value of these profits exceeds the value of the invested capital. (salem, 2011-2012, p. 111)

-The impact of applying the 51-49% rule on investment in Algeria:

The multiplicity and inconsistency of laws are among the shortcomings that make the investment environment unattractive. The subject is as follows:

The current legal environment is characterised by a proliferation of successive and inconsistent laws, as well as the inconsistency of certain economic decisions pertaining to investment, some of which have been reversed. This has led to the perception of instability, resulting in the deferral of foreign investment operations that necessitate stable prospects in the medium term. The most recent example of this is the reintroduction of Rule 49/51. (medioune, 2013, p. 287)

Legislative instability is one of the factors that contribute to legal uncertainty, which could result in the freezing of all foreign investment projects in the country. When considering the legislative environment and the current legal framework for investment in Algeria, it becomes evident that there is a degree of uncertainty surrounding legal security. This is a fundamental pillar and requirement for investment, and as such, it is essential to address this issue in a professional and strategic manner.

It is the belief of certain researchers that the rule was enacted in the 2016 Finance Act, yet omitted from the 2017 Finance Act.

This is a clear indication of the instability of the legal environment.

It is the belief of some researchers that the legislator intentionally included the 51-49% rule in the Finance Law but not the Investment Law, with the intention that it should remain in force and be relied upon if...

The government has indicated its intention to apply this rule to specific foreign investments.

The Algerian legislator's selective approach to the application of this rule contravenes a fundamental principle: the requirement for legislative stability.

Its primary objective is to ensure the fulfilment of contractual obligations, a guarantee that is often a prerequisite for foreign investors. (djebbar & lebig, 2019, p. 202)

3-List of strategic activities subject to the 51/49 rule:

In accordance with the recently amended Article 50 of Law No. 20-07.

In light of the 2020 Finance Act and the report by the Minister of Trade, the Minister of Energy and Mines, the Minister of Pharmaceutical Industry, and the Minister of Public Works and Transport, the Prime Minister has issued Executive Decree No. 21-145 dated 17 April 2021. This decree stipulates the list of strategic activities in the energy, mining, pharmaceutical, transport, and military industries, which are subject to a 51% participation requirement by local national shareholders.

In this context, Article 1 of the annex to this decree sets out the detailed list of activities related to the above-mentioned sectors that are of a strategic nature. Please find these activities below: (khallaf, 2021, p. 104)

1-3 Activities related to the energy, mining and pharmaceutical industries:

The Algerian legislator has identified eight strategic activities in the pharmaceutical industry, namely: the manufacture of pharmaceutical products, the manufacture of medical supplies, the wholesale trade in pharmaceutical products, the wholesale distribution of medical supplies, contract research organisations, pharmaceutical institutions for the exploitation of pharmaceutical product registration decisions, pharmaceutical institutions for the exploitation of medical supply approval decisions, and finally, a company for the promotion and dissemination of medical and scientific information on pharmaceutical products. (BENSEGHIR, 2023, p. 39)

3-2: strategic activities related to the energy and mining sector

With regard to the matter of hydrocarbons.

As outlined below, precious and sensitive metals are also involved.

The extraction of liquid and gaseous hydrocarbons, along with the transportation of liquid and condensed hydrocarbons via pipelines, is a key aspect of our operations.

The company is involved in the extraction and preparation of iron ore, bauxite, non-ferrous metals, as well as metals and alloys.

Ferrous metals, precious metals, various ferrous metals, uranium metals and all other radioactive metals.

The activities are centred on the extraction of coal.

We specialise in the extraction and preparation of various quarry products not intended for construction materials, as well as potassium salt.

- Phosphate extraction and preparation activities.

In addition, other salts are present, including salt marshes and salt flats. (khallaf, 2021, p. 105)

3-3 Strategic activities related to the air and land transport sector: (benseghir, 2023, p. 40)

the following activities are included:

Passenger transportation by rail is a key component of our business.

The transportation of goods by rail

We offer a professional private air transport service.

We specialise in the air transport of goods.

We are pleased to offer air services for the agricultural sector.

Management of road transport infrastructure is a key responsibility of the company.

Airport services.

The provision of light aircraft services.

The process of renting or leasing an aircraft.

Results:

We have reached a number of conclusions which we summarise below.

1- Since the rule's implementation in 2009, Algeria has experienced a substantial decrease in foreign direct investment. For instance, the number of foreign investment projects decreased from 93 in 2007 to only four in the year the rule was implemented, and it continued to decline to around 34 projects during 2010-2011.

According to a 2019 report by the United Nations Conference on Trade and Development (UNCTAD), foreign investment increased slightly in 2018 to \$1.5 billion, compared to \$1.2 billion in 2017. However, the majority of this investment remained concentrated in the oil and gas sector.

-2Foreign investors viewed the rule as a significant impediment due to its restrictions on their ownership stake and its requirement to partner with a local majority partner, which diminished.

-3 The Algerian government has defended the rule, stating that it protects national sovereignty and prevents foreign capital from controlling the local economy. It was also believed that it encouraged technology transfer and supported local investors.

However, some experts noted that the rule did not achieve its intended objectives, such as technology transfer. Instead, it contributed to the transfer of large profits to local businessmen without reinvesting them in the national economy.

the appeal of the Algerian market in comparison to neighboring markets that offer greater autonomy.

-4 Foreign direct investment plays a pivotal role in catalyzing economic growth by fostering job creation, modernizing infrastructure, and facilitating technology transfer. However, empirical studies have shown that its impact in Algeria has been limited due to the restrictions imposed by the 51/49 rule.

With the abolition of the rule in non-strategic sectors, the 2020 Finance Act forecasts GDP growth of 1.8%, reflecting optimism about improved investment flows.

Conclusion:

In light of the above, it is evident that Rule 49/51, established under the 2009 Supplementary Finance Act, signified a pivotal shift in Algeria's policy toward foreign direct investment. The objective of this regulation was to safeguard economic sovereignty and fortify local partnerships. However, it also ignited significant controversy due to its deleterious effect on foreign investment flows. Studies and statistics have indicated a substantial decrease in the number of foreign investment projects following the implementation of the rule. The number of projects fell from 93 in 2007 to only four in 2009, reflecting foreign investors' reluctance due to the restrictions imposed by the rule. Despite the state's claims to preserve national sovereignty, this policy has led to a decline in Algeria's attractiveness as an investment destination compared to neighboring countries.

Algeria has begun to regain the confidence of foreign investors by offering a more open and flexible environment, as evidenced by the gradual abolition of the rule in non-strategic sectors under the finance laws for 2020 and beyond, reinforced by the 2022 investment law. However, a delicate balance

must be struck between safeguarding national interests and fostering foreign investment to stimulate economic growth and diversify the economy beyond hydrocarbon reliance. It is therefore recommended that legislative reforms be continued, that the business climate be improved, and that transparency and institutional stability be enhanced to ensure the attraction of sustainable foreign investment that contributes to comprehensive economic development.

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