Cuba
Considerations for US investors

By Jesse Shapiro and Dan Scott
Starting in December of 2014, the world began to witness a series of events that would cause radical changes in relations between the United States and the Republic of Cuba, a small communist country approximately 90 miles off the coast of Key West, Florida. For the first time in over 50 years, the two countries have re-established diplomatic relations and are slowly re-establishing economic ties, leading to a new framework for trade and business opportunity. As events unfold and restrictions associated with the US embargo of Cuba begin to ease, both speculation and confusion have arisen. This article will summarize the recent changes, discuss what investors are considering to be potential business opportunities, examine some obstacles and provide some words of caution.

A brief history of US and Cuban economic relations

Those who are old enough to remember the Cuban Missile Crisis of 1962 will recall vivid memories of widespread worry and panic, fallout shelter installations, the daily sound of civil defense sirens, and round-the-clock news blaring from every television set and radio. Subsequent generations may only remember their history lessons about the intense two-week standoff between the United States, the former Soviet Union and Cuba, sparked by the Soviet Union’s installation of nuclear warhead-bearing missiles on the island. The situation added to pre-existing tension that had been built up from a series of events including (i) the severing of diplomatic relations between Cuba and the US after communist leader, Fidel Castro ousted the US-backed Cuban government, (ii) the failed Bay of Pigs invasion, a CIA-sponsored attempt at removing Castro and (iii) the broader economic trade embargo imposed by the Kennedy administration that followed the Bay of Pigs. The Cuban Missile Crisis was ultimately averted, but the aftermath saw a frigid cold war that would last between the US and Cuba until the Obama administration. The Cuban embargo (the Embargo), or “el bloqueo” as Cubans refer to it, started as a partial restriction on exports signed by President Eisenhower in 1960 after Fidel Castro seized billions of dollars of US interests in Cuba. The partial embargo later became a full embargo, under President Kennedy, restricting trade, business, travel and communication with the island nation. As part of the regulation of the Embargo, the US Department of the Treasury issued the Cuban Assets Control Regulations (CAGC) in 1963, under the Trading With the Enemy Act (TWE Act), which is enforced by the Office of Foreign Assets Control (OFAC). The passing of the Helms-Burton Act in 1996 tightened the Embargo and stipulated that it could only be lifted with the removal of Fidel Castro, and the establishment of free press and elections, among other things. When Fidel Castro became ill and handed over the reins to his brother, Raúl, in 2008 after a 49-year tenure, many saw potential for change with the turnover. In 2009, President Obama lifted certain travel restrictions and began allowing Cuban-Americans to send money to their friends and family. On December 17, 2014, President Obama and President Raúl Castro announced their intentions to restore diplomatic and economic relations following a prisoner swap and a series of secret talks. In conjunction with this meeting, President Obama also announced his intention to further ease certain restrictions imposed by the Embargo that are within his power to do. In January 2015, on the back of President Obama’s announcement, the US Department of the Treasury and the US Department of Commerce made revisions to the CAGC, easing certain travel and commerce restrictions. Following a historic meeting of Presidents Obama and Castro at the April 2015 Summit of the Americas in Panama, the US State Department removed Cuba from its list of state sponsors of terrorism in May 2015 and in July 2015, the US Embassy re-opened in Havana. Shortly thereafter, the Cuban embassy was reopened in Washington. Secretary of State John Kerry made a historic visit to Cuba in August 2015 to meet with senior Cuban officials and perform the opening ceremony for the US embassy, making it the first time a Secretary of State has traveled to Cuba in 70 years. Following this, in October 2015, US Secretary of Commerce Penny Pritzker made a trip to Cuba to speak with Cuban officials about business opportunities between the two nations.
The easing of the Embargo has led to a wave of speculation over the potential for Cuba as the next frontier market. New opportunities in areas such as internet and telecommunications, travel, distressed debt investing, banking and credit, and insurance have piqued the interest of potential US investors.

In January 2015, the CACR and the Export Administration Regulations (EAR) were amended by the US Department of the Treasury and the US Department of Commerce, respectively, to enact the changes announced by President Obama. One of the most prominent of the changes related to US citizens’ ability to travel to Cuba. Before then, the categories of allowable travel were narrow, and some required prior authorization from OFAC.

The changes now allow for travel to Cuba for 12 categories under a general license, which is a self-executing and self-documented license that does not require an application to OFAC. The 12 categories of approved travel consist of (1) family visits; (2) official business of the US government, foreign governments, and certain intergovernmental organizations; (3) journalistic activity; (4) professional research and professional meetings; (5) educational activities; (6) religious activities; (7) public performances, clinics, workshops, athletic and other competitions, and exhibitions; (8) support for the Cuban people; (9) humanitarian projects; (10) activities of private foundations or research or educational institutes; (11) exportation, importation, or transmission of information or information materials; and (12) certain export transactions that may be considered for authorization under existing regulations and guidelines.

On September 21, 2015, OFAC made further amendments to the CACR (September Amendments) to permit persons subject to US jurisdiction to visit close relatives in Cuba while traveling for one of the authorized purposes. The potential for providing, or investing in companies that provide, ancillary services to US persons conducting authorized travel and business has also been made possible by these recent amendments. Airlines and cargo companies may provide services, under general license, to those US persons that are authorized to travel. In August 2015, it was reported that President Obama was working with Cuba on a deal for commercial flights to operate regularly between the two countries by the end of 2015. US insurers can provide health, life and travel related insurance for authorized US travelers as well. US banking and depository institutions are permitted to enable and process authorized transactions, including depository services, wire transfers and credit and debit card services, and as of the time of writing of this article, it has been reported that there was at least one US bank based in Florida that has set up a banking deal with Cuba’s Banco Internacional de Comercio. The September Amendments enable legal services to be provided to Cuba or non-government Cuban nationals, and allow persons subject to US jurisdiction to establish and maintain a physical presence to establish news bureaus and provide authorized mail, parcel and cargo transportation services. It should be emphasized, however, that these ancillary services are only allowed in support of underlying transactions that are otherwise authorized (such as payment for goods lawfully shipped to Cuba); the Cuban market is not “open for business” to US businesses across the board.

Another critical area of change in the CACR relates to the easing of restrictions related to telecommunications, which will enable US telecom providers to engage in certain commercial activity with Cuba. The White House states in a fact sheet posted on the Office of the Press Secretary’s website that “Cuba has an internet penetration of about 10% of the population — one of the lowest rates in the world. The cost of telecommunications in Cuba is exorbitantly high, while the services offered are extremely limited.”

The commercial sale to individual consumers in Cuba, other than certain government and Communist Party officials, and independent NGOs of communications devices and telecom-related hardware, certain low level computers, software, and related services is now allowed, which would in turn make way for US companies to provide certain internet services, radio and television feeds, news wire feeds, satellite transmissions, or generally establish or enhance telecommunications between the two countries. The September Amendments permit persons subject to US jurisdiction to establish and maintain a physical presence in Cuba, including “through subsidiaries, branches, offices, joint ventures, franchises, and agency or other business relationships with any Cuban national” in order to provide authorized telecommunications and internet-based services as well.

Taken together with the fact that President Raúl Castro lifted a ban on the use of personal cell phones in Cuba in recent years, the opportunities for business activity in this area may also appear attractive to some potential US investors looking to back US companies foraying into this space. The fact that these products can be sold to Cuba, however, does not cover all possible sales arrangements, and potential investors should exercise caution. It should also be noted that many commercial telecom hardware and network infrastructure items are controlled at a higher level than is now authorized, and hence would still require specific approvals from the US government before export to Cuba.

In addition to exploring direct investments in both US and Cuban companies that stand to benefit from the aforementioned authorized offerings, some US investors are waiting for an opportunity to enter into the relatively European-dominated market for Cuban distressed sovereign debt, which has been in default since the 1980s. Speculators in this space point to historic surges in the prices of distressed sovereign debt of certain nations that occurred immediately following a re-establishing of relations with the United States after a period of disconnect (e.g., Vietnam). Some global distressed debt investors are also banking on the potential rise in recoverability rates as money begins to flow back into Cuba from the US. These activities are not yet available to US businesses, however, and US investors interested in this area should consult counsel.
Investment hurdles and words of caution

While US investors have taken a keen interest in these business opportunities in Cuba, many agree that they will come with significant challenges intrinsic to a frontier market. Telecommunications and financial systems infrastructure still requires significant investment and development before US and other foreign financial services can have a clear road into Cuba. Although Cuba passed the Foreign Investment Act of 2014, which creates favorable conditions for foreign investment such as tax concessions and vehicles that provide for investment without government partnership, there is a perception that the Cuban court system is not currently set up with reassuring means for US businesses to utilize the legal system to protect their interests. There is always the perceived risk that Cuba will once again expropriate foreign assets despite provisions of the Foreign Investment Act that address such actions. Lastly, there is no stock exchange currently in Cuba. La Bolsa de Valores de la Habana was once one of the largest stock markets in Latin America, but was closed down in the late 1950s as part of the Cuban revolution. These problems should not be of immediate concern, however, as actual investment in Cuba is still not allowed without specific authorization.

US investors will also need to consider the application of the US Foreign Corrupt Practices Act (FCPA), which makes it unlawful for certain companies and individuals to make payments (e.g., bribes), either in cash or gifts, to foreign government officials to obtain business. Given that Cuba is a communist state and all foreign-owned businesses currently must be partnered with some element of the Cuban government, it may be difficult to discern who would fit into the definition of a “foreign official” in the context of FCPA. US companies are responsible for monitoring the activities of any Cuban based consultants or other intermediaries that they may have engaged to help in securing business. In addition to the FCPA, investors will need to consider the Currency and Foreign Transactions Reporting Act of 1970, which is also known as the Bank Secrecy Act. The Bank Secrecy Act is designed to help detect money laundering. As a result, investors will need to be diligent in implementing anti-money laundering (AML) controls.

Perhaps the most important thing for potential US investors to note is that despite the recent partial easing of restrictions, except to the extent of the specific relaxation steps announced, the embargo otherwise is still in effect and strictly enforced by OFAC. Per the US Treasury Department’s website, “the Cuba embargo remains in place. Most transactions between the United States, or persons subject to US jurisdiction, and Cuba continue to be prohibited, and OFAC continues to enforce the prohibitions of the CACR.” President Obama does not have the authority to lift the embargo; only Congress does. The Helms Burton Act makes it clear that there are several conditions that still need to be met before the embargo will be lifted, and as of the writing of this article, there are many members of the House and Senate that are opposed to lifting the embargo before these changes occur. Equally important to note is that travel and other activities related to tourism are still strictly prohibited, and tourist is not part of the 12 categories of travel that are permitted by general license. Savvy investors know that a good business deal requires advanced preparation and getting in on the ground floor. However, despite all of these recent changes, business with Cuba still has many gray areas and “getting in on the ground floor” brings with it the risk of inadvertently violating the CACR. Communication between the US and Cuba is permitted under the CACR ($515.542) as are professional research and professional meetings in Cuba. However, the CACR is clear that anyone straying from these purposes (e.g., adding tourist activities onto their trip) or conducting communications and business meetings to discuss activities that are still prohibited by the embargo may cause OFAC violations and sanctions.

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SCORE No. CK1010
BSC No. 1510-1736382
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