Concept and Relevance of Investment Contract

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Abstract

Contracts defines how the process of investment has to be done. Investment contracts are required to include the ground principles upon which the parties had negotiated, in addition to the distribution of rights, duties, liabilities, and interests. These criteria covered, in particular, the choice of a venue for conflict settlement and the legislation that applied to the program. The role of contract in investment process is full of complexity of rules regarding the investment as they are shaped by negotiation between parties except in case of standard form of investment agreements which are often used for security investment such as investment in stocks etc. The entities conclude contracts for better realization of collaboration and coordination. The current work analyses the concept and relevancy of investment contracts along with necessary functions of investment contracts and the framework pertaining to investment contracts.

Introduction

Economic expansion and the supply of essential goods and services in almost any community depend critically on investment. And, Contracts define how investment operations are conducted. Generally speaking, a contract is any commitment involving more than one entities that creates enforceable obligations under the law. Contracts are a crucial component of the network of legal relationships that support international investment since they serve as the foundation for substantial investment in several industries. The contract offers a crucial platform for attorneys to clarify not just the specifics of an investment as well as the stories and presumptions that support it; these elements are occasionally expressly represented in the agreement's preamble provisions.

The relevance of contract in investment decision is evident not only during the phase of project development whenever the deals are written, but also across the duration of the project. Renegotiations of agreements have been the focus of several investor-state conflicts. In specific industries and geographical areas, contracts play a particularly important role in investor interactions.

In some circumstances, such as when investing in a portfolio of shares of a publicly listed corporation, the associated contract may be rather straightforward. Other investment activities, such as the building and running of a power plant sponsored by a venture, could necessitate a complicated web of contracts that address the legal connections between the project's sponsors, among other things. The contract may also stipulate the plans for the power plant's development, the government's obligation to purchase the energy generated, the financial procedures with different institutions, and investment insurance from systemic risk, to name a few. The applicable contracts taken as a whole make up the investment's contractual legal structure. For the objectives of this section, any contract that regulates or corresponds to an investment is referred to as an "investment contract."

Review of Literature

Dolzer and Schreuer in their work “Principles of International Investment Law” expressly introduced in a detailed manner the foundations of investment law and resolution of disputes. A juristic analysis of the case law from international tribunals is combined with a thorough analysis of the texts and guiding principles of investment law. The authors thoroughly explores the many forms of investment contracts as well as the rules that apply to the agreements. It goes on to analyse in depth the stability and renegotiations features of investment contracts.

Salacuse in “The Three Laws of International Investment: National, Contractual, and International Frameworks for Foreign Capital” examines legal rules and procedure affecting investment flow, the nature of respective right of investors and the process that may be used to resolve disputes. The work examines the legal framework for international investment and how they affect the process of international investment transactions. There are many literatures on this subject however their major focus is mostly on the international law regulating investment. The current work explores the two major sides of investment- the national laws and investment contracts as an understanding of both of these works is very vital for a smooth flow on any kind of investment. The work studies contracts role in investment process and the complexity of rules regarding the investment contracts that are shaped by negotiation between parties. The article examines contractual stability and renegotiation because investment agreements are usually a long in character and susceptible to vagaries of shifting circumstances.

Research Objective, Question and Methodology

The objective of the current study is to examine meaning and nature of investment contract. Its main aim is to study the concept and relevancy of investment contract for which it becomes necessary to study the contractual framework and functions of investment contract.

Questions

- What is meaning of investment and investment contract?
- What is the contractual framework of investment contract?

- What is the relevancy of investment contract?
- What is the framework of investment contract?
- What are the various functions of investment contract?

Methodology

The research approach used to perform the current study is based on doctrinal research. As a result, the information gathered here is both primary and secondary and comes from a variety of sources, including library, public records, judicial findings and laws.

Meaning of Investment and Investment Contract

'Investment' as a terminology is a quite fundamental concept appropriated in contracts, and national & international legislations, hence, it become pivotal to understand what constitutes as an investment in order to study contracts relating to investment. The engagement of assets to a certain goal by a human or legal person for the purpose of generation of profit or receive a return would be the concept of the term "investment" at its most fundamental level. There are two common applications for the word investment. The procedure or transaction through which an individual or corporation initiates an investment is such example. As a result, making an investment would be like acquiring a hundred shares in capital market or a business to sell things out of. The asset obtained as a consequence of investment is the focus of the second interpretation. Both the acquired assets and the acquired business are regarded as investments in this respect.

Investment contract is a unique kind of contract that controls the interactions between an organisation, a government, or a business and the financiers who will provide the capital for their expansion. The goal is to preserve the investor's interest without compromising the project's progression or the correct establishment, while also ensuring that entrepreneurs will satisfy their financial obligations.

As per Aiyer, investment contract means:

> "New forms of securities that are investments of money in a common enterprise from which the investor is led to expect profits derived solely from the promoter's efforts."[i]

The Securities Appellate Tribunal decided in Maitreya Services Private Limited Lawrence Trade Centre CO OP HSG SOC Ltd. v. SEBI[ii] that "investment contract" is an arrangement amongst participants to engage money with the expectation of receiving a return.

In SEC v. W.J. Howey Co[iii], the Supreme Court of the United States ruled that investment contract means:

> "A trade or strategy in which a client puts their capital in a group venture and is persuaded that they may anticipate a return exclusively through the promoter's or another group's endeavours. It symbolizes a malleable concept as opposed to a rigid one that can be adjusted to match the diverse and varied strategies created by individuals who wish to utilize other people's assets with the assurance of gains."

Moreover, foreign investments are governed by complex web of contracts that is also covered under investment contract, however such investment contracts are generally negotiated between two or more states, or between state and enterprises.

Relevancy of Investment Contract

Whether or not a particular transaction is investment is heavily dependent on the meaning of investment and the investment contract. A transaction that is considered as an 'investment' by an entrepreneur may not qualify as 'investment' under relevant national legislations, contractual provisions or international regulations & treaties.

For instance, in one incident that occurred in DRC in 1999, state's military shut down a successful legal company founded by an American, completely eliminating the American's business. The arbitrators denied the American attorney's request to file a lawsuit against the government of Congo before an international arbitrator to comply with the U.S.-Congo

Mutual cooperation Investment Agreement on the premises that his company did not qualify as an "investment" under the agreement.[iv]

Investment contracts regulate both investments and investors, or the people and entities who make investments. As a result, there are literally millions of people, businesses, and organisations that may be investors, and that number is only growing. Non-compliance with the regulations governing investment in the investment agreement might possibly have an impact on each of these millions of people, businesses, and organisations, together with their billions of dollars in capital.

Moreover, MNCs have generated a lot of discussion and analysis, as well as strong and divergent opinions. Multinational firms are significant drivers of economic growth for some populations. Others view them as environmental and labour exploitationists.[v] Sometimes the parties involved in investment transaction require much liberation for economic growth from the constraints of onerous regulations and rules. While, sometimes, others require stringent law, regulation, and agreements to restrain the capacity for “self-enrichment at the expense of other party or national sovereignty, human rights, and the environment.” Because of this, the investment contracts and regulations governing investment play a crucial role in global economic activity.[vi]

Salacuse, points that Numerous long term contractual agreements between parties may qualify as investment insofar as they call for one party to invest assets in a something with the hope of obtaining a return in the future.

> “Concession contracts between persons and entities based in different countries to run public services, mineral exploration arrangements, development agreements, construction contracts, land purchase agreements, and innumerable other contractual devices may all be considered international investments. Exposure to sovereign risk and corruption can be significant obstacles even when contracts are in place.”[vii]

International Organizations and States invest billions each year through loans, equity participation, share capitals, and holding public enterprises in order to support economic development and earn a return on their invested capital. For example, The World Bank, IFC, Asial Development Bank and InterAmerican Development Bank are institutions whose objective, among others, is to promote economic development through funds secured by states and private capital exchequers. All investors are simultaneously worried about the hazards posed by the proposed investments. Investments that have a significant risk are those where there is a likelihood that projected profits won't manifest. Investors assess possible investments based not just on the quantitative profits that may be predicted from a certain investment, but also on the capital appreciation compared to the anticipated risks involved. For the majority of investors, a larger rate of profit is required for justifying an investment when the risk is increased.[viii]

All investors, private, state, mixed, and foreign, also attempt to organise and run their assets in a manner that will boost their profits and reduce their risks, to get this objective they employ a range of tools, like as investment contracts, laws, and international agreements. For example. Two corporations may get into deep negotiations concerning their interests and then formulate the contract consisting provisions that will be in their best interest.

The Contractual Framework of Investment Contract

Investment is controlled by the principles outlined in one or more agreements, in in addition to the statutory standards set forth by national legislation. The organisation, administration, execution, and functionality of the transaction, as well as the rights and duties of the investors, are all governed by these contracts, which are operationalised and made effective by some appropriate system of domestic law. They make up the investment's contractual legal structure as a whole. The capacity of the participants to establish specific terms for their transaction is also contingent on domestic law, which affects both the enforcement of contracts and the ability to enter into a contractual relationship. So, while arranging an investment, a key concern for participants and their legal counsel is to determine if the national law would allow them to create regulations by contract and whether or not the federal law forbids such private law-making, a topic known as "party autonomy" which is a policy matter under the domain of domestic law. Party autonomy is universally recognized except in cases of purely domestic transactions.[ix]

Kehinde v. Registrar of Companies[x], is a Nigerian case that perfectly illustrates the role of domestic legislation on contractual framework of investment. The Nigerian parliament approved the Nigerian Enterprises Promotion Act that obligated Nigerian shareholding in some kinds of companies be not less than 60%, in an attempt to indigenize the Nigerian economy, promote the growth of Nigerian innovators, and give Nigerian citizens higher say over the country's available capital. The Nigerian Companies Act also offered company founders considerable latitude, or contractual flexibility, to distribute administrative decision-making authority in accordance with their preferences. A joint venture was incorporated with 70:30 funding from Nigeria and Japan respectively thus fulfilling the obligations mandated under NEP. However, despite the minority position of the Japanese, the contractual framework provided the Japanese a special effective veto over corporate actions. Thus, by the contract, the partners tried to incorporate a governance structure the suited their requirements. However, upon reviewing the corporate structure of the venture, the registrar refused to register the venture. The Court held that

> "joint venture, being 70 percent owned by Nigerians complied with the NEP Act, despite the control structure agreed by the parties; consequently, the Registrar of Companies could not refuse to register the joint venture company."

Therefore, the contractual legal framework depicts the parties to the investment transaction's respective negotiating strength. Further, the contractual framework was created to govern a specific transaction, so it has a high level of particularity and specifics and may even be singular, if not idiosyncratic. In contrast, the national legal framework includes rules that are somewhat general in order to encompass a class of transactions.

Although investment contracts involving state and private parties are often governed by the domestic legislation of a particular jurisdiction, they differ from agreements between only private parties due to the extraordinary authority that states utilise to create and enforce such agreements. Because of this, they belong to a specific kind of investment contracts called "state contracts." State contracts differ from regular commercial and investment contracts involving private parties in a number of ways, which contribute to their unique nature. First, from the perspective of the respective government, their goal is to execute a state activity or duty rather than just make profit. The procedure of forming state contracts is typically governed by specific

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statutory regulations and laws which do not operate in solely commercial transactions due to the distinctive function and objective.

For the purpose of Securities Law, there are certain standard forms of investment contracts which are as follows[xi]:

- Stock Purchase Agreement and Restricted Stock Agreement
- Statutory and Non-statutory Stock Option Agreement
- Convertible Debt Agreement, Note and Promissory Note
- Royalty, Commission, or Percent of Revenue and Deferred Compensation

Each of these several Investment Contract forms has a specific purpose, and many of them can be put together to form the ideal Contract depending on the circumstance. But if performed improperly, this area might result in very severe fines under the Securities Laws.

The Functions of Investment Contract

Investment contracts serve as more than just formal agreements outlining the stakeholders' rights and duties. They represent social structures between people who are involved in business activity. According to a renowned researcher, the goal of every contract is to ensure collaboration to realise societal goals via the utilisation of promises that were made in agreements reached through negotiation.[xii] Investors conclude agreements to ensure the collaboration and coordination, i.e. desired behaviour, from other stakeholders, regardless of whether private businesses or governmental organisations, to reach the specified ends, such as the building and establishment of a power plant in India, a loan to a governmental organisation in Peru at an advantageous interest income, or the acquisition of privatised assets in Poland etc.

The Investment contract serves some economic functions and it is not merely a document stating rights and duties.

Risk Allocation

Allocating particularly to individual partners the risks and expenses resulting from their joint endeavour is one of the key purposes of the contract. Therefore investment contracts, may be viewed as tools for allocating risk. The contractual parties generally have two options for handling certain risks in the transaction. They might decide to assign the risk to a 3rd - party insurer or they could negotiate that one or both entities would take on the responsibility.

Investment Planning

A contract also serves as a planning tool, outlining the duties that each party to the venture is accountable for carrying out. Every investment contract contains a cooperative strategy that the parties intend to use to accomplish their goals. The concise mechanism of the investments that the entrepreneur must undertake and the requirements of quality that it needs to comply in providing the service will be specified in the contract in certain detail.

Investment Control

Investors look for strategies to manage the behaviour of people and organisations whose activities can have an impact on the venture in order to guarantee the desired collaboration, which is a requirement for the sustainability of any transaction. Contracts are crucial tools for ensuring this control. The contractual restrictions show a wide range of characteristics. The kind of investment undertaken and the investor's negotiating strength determine the degree and character of management that the investor acquires through contracts.

Benefit Extraction, Regulation and Governance

Earning a return, a gain, or a profit is the aim of both investors and governments who participate in the investing process. Contracts are crucial tools for obtaining that return on investment. The specifics of the profit desired rely on the investor's corporate ambitions of the parties. Different avenues exist for investors to gain through their investments. Investment agreements could also serve as tools for the parties' supervision and governance in two key areas. First, they might be a way for one party to control how the other party carries out different actions connected to its investment. Second, a party to an investment contract may acquire some administrative responsibilities, rights, or privileges that would typically belong to the other party.

Warranties, Restrictions and Confidentiality

Warranties are statements of truths and details issued by a corporation to an investor regarding the investment. Investors may seek legal action depending on assurances that were shown to be deceptive or false. An investment contract's prohibitions will outline the manner through which the investor is constrained in terms of ownership, shares, or other roles within the company. The contract's declarations of confidentiality will require the willing parties to maintain details about the transaction private.

No matter how comprehensive the investment contracts seem to be, it is important to keep in mind that they are merely guidelines for the parties' behaviour and that the requirements of life, both social and economic, may interfere with the parties' ability to fulfil their commitments under the agreements. Therefore, there is a constant conflict in all investment contracts between the requirements of life and the contractual legal framework.

Conclusion

Investment contract is a unique kind of contract that controls the interactions between an organisation, a government, or a business and the financiers who will provide the capital for their expansion. Investment contracts regulate both investments and investors, or the people and entities who make investments. Non-compliance with the regulations governing investment in the investment agreement might possibly have an impact on each of these millions of people, businesses, and organisations, together with their billions of dollars in capital. Investment is controlled by the principles outlined in one or more agreements, in in addition to the statutory standards set forth by national legislation. The capacity of the participants to establish specific terms for their transaction is also contingent on domestic law, which affects both the enforcement of contracts and the ability to enter into a contractual relationship. Therefore, the contractual legal framework depicts the parties to the investment transaction's respective negotiating strength. The Investment contract serves some economic functions and it is not merely a document stating rights and duties.

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