

# Applicability of ordinary law of Sri Lanka in Foreign Direct Investment: A critical study of Port City Project in Sri Lanka

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**Abstract:** *This study examines the practical application of ordinary law of Sri Lanka in FDI, with a particular focus on the Colombo Port City Project in Sri Lanka. The objective of this study is to critically examine the applicability of ordinary law in Sri Lanka's Port City Project, where the unique phase of foreign investment plays a major role to attract foreign investments to address Sri Lanka's balance of payment crisis and provide local job creation. The country's approach to FDI has two key drivers: (I) the urgency of attracting FDI; and (II) greater politicization of foreign investment projects. The latter arose from geopolitical concerns, which affected several of the Executive branch's significant investment decisions. It should be noted that Sri Lanka is significant in this geopolitical war because of its advantageous location in the Indian Ocean. It has grown troublesome as China becomes more involved in important industries including ports, transportation, and energy. It is worthy to be noted that, whether Port City Project investments are subject to the ordinary law and which institutions have the authority to approve such projects in accordance with the concepts of transparency and public accountability for such decisions. The study, therefore, primarily concentrates on the Sri Lankan legal jurisprudence and how the investment law plays its role when it comes to the public-private partnership between the Government of Sri Lanka and a project company called CHEC Port City Colombo (local subsidiary) which is the*

*arrangement to develop Sri Lanka's first-ever Special Economic Zone(SEZ).*

**Keywords:** *foreign direct investment, national security, and sovereignty, Geo-politics.*

## 1. Introduction

The Port City Project is billed as, a gateway to South Asia, which was first conceived of under the previous administration (2005–2015) and was unveiled during Xi Jinping's visit to Sri Lanka in 2014. The CPC is a flagship initiative of China and a key component of Xi's Belt and Road Initiative (BRI). The project, which spans 269 hectares of reclaimed sea land, is valued at the US \$1.4 billion and is Sri Lanka's single greatest investment. With Colombo being one of the top 25 busiest ports in the world, the proposed project is being sold not just for Sri Lanka, but for South Asia as a "world-class metropolis". Even though it appears to be an intriguing proposal, it should be underlined where it is being hatched and how it is being developed by reclaiming many hectares of land from the sea to provide China with a strategic edge in the Indian Ocean.

It is believed that the previous administration had originally suggested plans for a Colombo Port City in 2004 by purchasing property in the Colombo city region, and this proposal would have presented issues with regard to shifting the populace to alternative territory within the city. Therefore, the previous administration made the decision to build the port city by reclaiming the water in order to solve these

issues. Hence, a 600-acre stretch of sand from the bottom of the Indian Ocean was dredged by tens of Sri Lankan ships that were financed by China to build the metropolis. Since the details of this project, which the Sri Lanka Ports Authority (SLPA) claims to be the greatest private sector development initiative in Sri Lankan history, are not in the public domain and the people of this nation are unable to evaluate its potential effects on the environment, society, and economy.

Indeed, the first major investment decision which was to build SEZ through Colombo Port City raised serious concerns related to Sri Lanka's territorial sovereignty. It was argued that the establishment of such SEZ through a public-private partnership between the Government of Sri Lanka and a project company called CHEC Port City Colombo would lead the landfill into a "Chinese colony" thus, such a zone is not subject to Sri Lanka's territorial sovereignty. At the same time, the process by which Sri Lankan Government approved such FDI decisions has been criticized and increased public awareness owing to their potential geopolitical influence and related challenges to sovereignty and national security, as well as the transfer of Sri Lanka's national assets to foreign powers. In this context, this research critically evaluates how the Port City Act (PCA) works under the ordinary law and whether such FDI decisions with related to CPC project operates in accordance with the concepts of transparency and public accountability or not.

## **2. Methodology**

The primary source of information for this research was scholarly texts, journals, conference papers, and legislation. This legal research utilizes open-domain data for the analysis. The study also made reference to the current Sri Lankan Constitution, administrative directives, and national policies, particularly the Foreign Exchange Act

2017, the Board of Investment Law 1978 (BOI Act), and the Strategic Development Projects Act 2008 (SDP Act), with special emphasis on the Port City Act, which was controversially passed in May 2021. As the secondary sources, the data were collected from the books, e-books, reports prepared by the NGOs and INGOs, statistical reports, journals, scholarly articles and empirical data available at both library and electronic databases.

## **3. Discussion**

### *A. Investment policies and identified CPC Project issues with related to the ordinary law of Sri Lanka.*

Sri Lanka has implemented an investment policy that is generally hospital towards foreign investments since the liberalization of the country's economy in 1978. In accordance with the Exchange Act 2017, foreign investment shall not be allowed money lending, pawn broking, retail trade capital of less than US one million and coastal fishing. It is further stated by relevant laws that the business activities in which limited investment is allowed or restricted due to the facts of promoting local industries or security-related issues. As per rule, foreign investments should be observing by domestic laws governing issues such as land, labour and the environmental. It should be noted that, certain exemptions on investment projects can be applying over the domestic laws such as inland revenue, customs and exchange and the projects which are located in geographically demarcated areas are governed by a separate regulatory framework apart from the rest of the country with related to such issues in the customary manner.

Moreover, The Board of Investment Law 1978 indicates that projects are eligible for exemptions from certain laws based on "eligibility incentive criteria", such as the minimum level of capital and employment that

will be generated by such project. Under the Strategic Development Projects Act 2008, investment projects which are identified as a "Strategic Development Project" can be granted exemptions from laws specified in the schedule of the act. In addition to these two national laws, the Board of Investment has the sole authority to identify projects eligible for exemptions in consultation with relevant line ministries, taking into account factors provided for in the SDP Act, such as the strategic importance of a given project and the amount of foreign exchange involved therein.

Colombo Port City Economic Commission Act (Port City Act) which was controversially come into effect in May 2021 excludes the application of several laws within the area of authority of the Port City. The law which has been listed in Schedule III of the act does not have any application within the Area of Authority due to the fact that the subjects regulated by those laws have been incorporated into the Port City Act itself. Moreover, the companies which are engaged in the offshore banking business shall be registered as offshore companies and such companies' general administration activities are exempted from the application of provisions of the Company Act of Sri Lanka. It shows that Port City Act has reduced burden of compliance and controversially impacted on the ordinary law of Sri Lanka. Significantly, Schedule II of the Port City Act includes the Casino Business Act and Termination of Employment of Workmen Act. It should be highlighted that these laws are from which foreign investment projects can be exempted and thus, including these laws was controversial and are not included in the BOI Act and SDP Act.

*B. Identified CPC issues with related to the concepts of public transparency and public accountability.*

Investment projects initiated by foreign individuals or corporate investors (who may choose Sri Lanka as their investment destination) will be approved by the BOI or, beginning in May 2021, by the PC Act. In accordance with this, there are two aspects to be highlighted: which institution has the authority to approve the CPC Project and how these decisions are made.

Firstly, the BOI can approve projects under Sections 16 and 17 of the Act, but the Foreign Exchange Act prevents the BOI from approving foreign investment in non-permitted sectors such as coastal fishing or money lending. Similarly, it cannot approve foreign investment in sectors governed by specific laws, such as manufacturing arms and military hardware. When it approves foreign investment of more than 40% of the equity in companies proposing to carry out restricted business activities such as mass communication, deep-sea fishing, mining and primary processing of non-renewable natural resources, thus the BOI takes a case-by-case approach to approving foreign investment projects. Secondly, the Port City Commission has been established, but the Act establishing it does not provide any specific criteria for evaluating applications for investment in the Port City SEZ. The section 30 of the Act only stipulates that the Commission is responsible for deciding whether to accept or reject any application for "good reasons". Thus, it clearly indicates that there is no institutional framework for public procurement in order to regulate and oversee such decisions. Furthermore, the failure of showcase the transparency and public accountability of such decisions leads the CPC project in question with related to the "Public participation" in the international and national law. In the case of Eppawala Phosphate Case, it was held that the public participation in such decision making relating to "prescribed projects" which is constituted in the National

Environmental Act has been considered by the Court to be an essential right vested with people directly affected by such projects and a vital element in ensuring the sustainability of the development driven by them.

In the *Chunnakam Power Plant Case*, it was decided that BOI, acting in its capacity as a Project Approving Agency (PAA), had violated its legal and regulatory obligations to implement the environmental impact assessment (EIA) which was constituted under NEA. The Court has further held that when approving investment projects, the Supreme Court has to be required to determine that the EIA as an indispensable element of ensuring public participation in the decision making process. The possibility of circumventing the EIA framework through contractual arrangements between the foreign investor and the government was rejected by the Court. Hence, these cases indicate that the BOI Act and the Port City Act don't demand that contracts involving foreign investment be made public or that Parliament or the Cabinet approve them. The Court has specifically called attention to how foreign investments affect public scrutiny.

The Right to Information Act of 2016 (RTI Act)<sup>13</sup> has gained significance in this context as a result of specific foreign investment regulations' failure to ensure transparency. The RTI Act strengthens the basic right to information granted by Article 14A of the Constitution while recognizing citizens' right to access information in the possession, custody, or control of a public authority. There are, however, arguments both in favor of and against the RTI Act's application to government foreign investment contracts that an investor has with a pertinent statutory authority. Hence, the RTI Act 2016 (RTI Act)<sup>13</sup> contains a number of exemptions with related to FDI, but most exemptions are subject to override by a public interest override. It

indicates that the failure to conduct a public procurement process for CPC large-scale projects may be argued to have denied the public an opportunity to participate in those investment decisions, undermining their transparency.

#### *C. The constitutional framework of CPC project in Sri Lanka and related issues.*

The 1978 Constitution of Sri Lanka does not offer a framework for evaluating investments. However, Sri Lanka's bilateral investment treaties have a legal foundation according to Article 157 of the Constitution. The purpose of BITs is to safeguard (private) investors and their international capital investments. It should be noted that parliamentary approval will directly incorporate provisions of international investment treaties into Sri Lankan law. To translate an investment treaty into domestic law, no enabling legislation is required. As a result, domestic courts may now hear cases involving the substantive and procedural rights granted to foreign investors protected by such BITs. Foreign investors do not, however, have a right to challenge governmental or administrative actions that go against the terms of these agreements under Article 157 of the Constitution. Thus, it can be argued whether the agreement between China and the government of Sri Lanka does have any remedial system for CPC or not.

#### **4. Recommendations and Conclusion**

As mentioned above, Public dissent against some development projects has resulted in landmark lawsuits that challenged them on multiple different grounds, including their incompatibility with fundamental rights as contained in the 1978 Constitution. The Sri Lankan judiciary has used these lawsuits as a vehicle through which to safeguard the country's natural and national resources. In some cases, the Court indefinitely blocked and/or nullified high-profile investment

projects proposed or concluded by the Executive with foreign entities interested in investing in the country. Eppawala and Chunnakam power plant cases indicates where the domestic courts interfere and provide the legal protection for country's' natural resources and significant of the public transparency and accountability. The Court urged the Executive to exploit Sri Lanka's natural resources in trust for the public benefit. Importantly, the Court denied favoring foreign investors against members of the public in a manner that violates citizens' fundamental rights under Article 12(1) of the Constitution.

It should be highlighted that the fundamental rights of our country should be merged with other frameworks(RTI) in order to improve the effective compliance and disclosure requirements when it comes to the FDI decisions. Moreover, judicial review can be the domestic mechanism to improve the public transparency and accountability in the FDI decision making process. In the case of CPC Project, the details of such significant elements such as EIA and other component's to be made such large-scale infrastructure project are not in the public domain and the people of this nation are unable to evaluate its potential effects on the environment, society, and economy. Hence, it should be noted that, such decision making process can be led through the judicial review and can be questioned its public transparency and accountability for such decision making.

In addition to that the fundamental rights of the Citizens of Country should be taken into more consideration when it comes to the sovereignty of people and territorial sovereignty of our country. It is worthy to be noted that other frameworks for investments should be complied with Supreme Law of the country and when it comes to the decision making of such mega scale investments, the

agreement should be led through the special requirements to be followed in order to safeguard the nation's territorial sovereignty. As mentioned above, the PC Act shows that separate legal framework for such investments without compliance with Supreme Law of the Country lead to controversial issues. Hence, it is vital to enhance the all other frameworks in accordance with safe guard the territorial and people sovereignty.

Owing to the insecurity of the economic policy environment, the unpredictable and outdated regulatory system, stringent administrative procedures, enhanced bureaucratic discretion, and public sector corruption, attracting an increased volume of foreign investment has been somewhat difficult for Sri Lanka. Addressing such concerns is critical to making Sri Lanka a welcoming and appealing destination for FDI. However, equal emphasis must be placed on ensuring democratic oversight of the investment decision-making process, particularly decisions made by the Executive branch.

The Supreme Court nullified and voided the Share Sales and Purchase Agreement between the Sri Lankan Government and the chosen investor (whose consortium included a foreign company) to sell 90% of the shares in the Sri Lanka Insurance Corporation in the case of *Vasudeva Nanayakkara v. K N Choksy and Others* (SLIC). This is because it was discovered that improper and illegal Executive and administrative acts were present throughout the whole privatization of the SLIC. It's significant that the Court determined that those activities violated the petitioners' and citizens' fundamental rights protected by Article 12(1) while stating that using executive power in a way that serves the public good is "positively related to the right to equality."

Furthermore, it was held in the *Eppawala Phosphate* case that the Court denied favouring

foreign investors over members of the public in a manner that violated citizens' fundamental rights under Article 12(1) of the Constitution (the right to equal protection of the law). Hence, the above mentioned cases indicate that the lack of a transparent and reliable public procurement process, as well as the lack of policy of government procurement practices, has eroded foreign investors' confidence. Lack of transparency has also influenced public perceptions of foreign investments, with many people now viewing foreign investment as a form of foreign interference. Because of this perception, domestic politicians have been able to use foreign investment as an emotive electoral issue to shape their short-term political agendas, undermining the use of foreign-funded development projects as an effective economic tool to achieve the country's national interests. Thus, it has been somewhat challenging for Sri Lanka to draw in more foreign investment because of the unstable nature of the country's economic policy environment and the unreliable and antiquated regulatory system. It is essential to address these issues if Sri Lanka is to become a friendly and alluring location for FDI. Equal importance must be given to establishing democratic scrutiny of the investment decision-making process, especially for executive branch decisions.

Significantly, judges in Sri Lanka have invalidated FDI rulings on the grounds of abuses of human rights. Such litigation could now result in arbitrations under investment treaties against Sri Lanka. In other words, it can be considered as violation of investment treaty protection which was accepted by the home state. The fundamental rights petition that contested the hedging agreements reached by the Ceylon Petroleum Corporation is the best illustration in this regard. This petition ultimately led to several international

and domestic legal proceedings, including a treaty-based investment arbitration. In the case of *Deutsche Bank AG v. Sri Lanka*, it was held that Sri Lanka is partially accountable for the decisions made by the judiciary, and the claimant investor, Deutsche Bank, received a US\$60 million settlement. It demonstrates that Sri Lanka's domestic and international investment treaty-making processes have not received much attention, leaving important questions unanswered, such as whether it is appropriate and constitutional to give foreign investors access to international law in order to resolve their disputes without going through Sri Lanka's national court system. The above mentioned analysis emphasizes that the sufficient policies related to public transparency and accountability should be compliant with both international and national law in order to protect the territorial and people's sovereignty, which could also create the platform for protecting the national security of Sri Lanka.

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### **Abbreviations and Specific Symbols**

FDI – Foreign Direct Investment  
BOI – Board of Investment  
CPC – Colombo Port City  
SEZ – Special Economic Zone  
CHEC – Chinese Harbor Engineering Company  
SLPA - Sri Lanka Ports Authority

NGO – Non Governmental Organization  
INGO- International Non-Governmental Organizations  
RIT - Right to Information  
EIA – Environmental Impact Assessment  
PAA – project Approving Agency  
SDP – Strategid Development Project

### **Author Biography**



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