

## Faulty Investment Regimes Jeopardize Peru and Ecuador FTAs

For the last year, the Andean countries have seemed headed for a free trade agreement with the United States. Negotiations were announced during the FTAA Ministerial in Miami last fall and several negotiating sessions were held this year. At the fifth round of talks on October 26 in Guayaquil, Ecuador, the three countries involved—Colombia, Peru and Ecuador—will present improved offers for industrial, textile and agricultural products. But US Trade Representative Robert Zoellick and Deputy USTR Peter Allgeier recently expressed doubt about the agreement, and on October 6 Assistant USTR Regina Vargo told the House International Relations Subcommittee on the Western Hemisphere that an Andean FTA would go ahead without Peru and Ecuador if they do not do more to improve investment protections. “Their window is rapidly shrinking,” was Vargo’s assessment of the two countries’ chances for an FTA.

Zoellick has told the Peruvian and Ecuadorian trade ministers that they must improve investor protections and settle outstanding investment disputes, and House Subcommittee Chairman Cass Ballenger has questioned whether the two countries should continue to receive benefits under the Andean Trade Promotion and Drug Eradication Act. Making matters worse, Ecuador’s politically ambitious solicitor general, José María Borja, has called for the abrogation of the existing bilateral investment treaty to “pave the way for expropriations.”

### *Investor Disputes Are Sticking Issue*

Ecuador’s state-owned companies violate contracts, and investors report almost universal problems with Ecuadorian courts. Assistant Secretary of State Earl A. Wayne cited such complaints as unclear and contradictory policy signals from different governmental entities, inconsistent implementation of laws and regulations affecting investors, a turgid judicial process, and lax enforcement of contracts. Of Ecuador’s nine outstanding investment disputes, the U.S. Chamber of Commerce cited four, including the possible termination of a contract with Occidental Petroleum Corporation after an international arbitration panel ordered Ecuador to pay the company \$75 million. Borja’s statement, a chamber representative added, calls into question Ecuador’s readiness for a FTA and its ability to live up to FTA commitments.

Assistant Secretary of State Wayne noted that Peru has 12 unresolved investment disputes but that the situation there is considerably better than in Ecuador because most of the cases are under arbitration or adjudication. Most concern actions by SUNAT, the Peruvian tax authority. The Council of the Americas has claimed that SUNAT has embarked on a campaign to retroactively assess taxes on foreign investors. In one case, the Englehard Corporation complains that Peru owes it \$30 million for unrefunded VAT taxes; in turn, the Peruvian government accuses the company of fraudulent invoicing. All parties hailed Peru’s recent creation of new commercial courts and a tax ombudsman to limit SUNAT’s power to appeal court judgments against it.

### *Local Press Coverage*

Media reaction to the House Subcommittee testimony was relatively muted given the importance of the matter and the obvious potential for political grandstanding. Ecuadorian columnist Abelardo Pachano urged the FTA negotiations to proceed at all

levels with a full accounting of advantages and costs. In a radio interview, consultant Marco Navas called Ecuador less prepared than Peru or Colombia to negotiate a FTA, citing limited understanding of the process and a lack of technically qualified personnel. Ecuador's Federation of Chambers of Production announced it was suggesting a candidate to serve as a private sector representative on the official team of negotiators, but the chief negotiator, Christian Espinosa, maintained that there would be no changes in the team.

In Peru, an editorial in *La República* (Oct. 13) charged that the US Congressional Subcommittee had "crossed the line" and gone from pressure to threats. It praised the SUNAT as one of Peru's "better institutions" and argued that its actions in the Engelhard case had been appropriate. The General Confederation of Peruvian Workers announced that it was gathering signatures in favor of holding a popular consultation on the FTA. For its part, *El Comercio* (Oct. 17) ran an extensive commentary on the FTA by Economics Professor Mario Tello of CENTRUM Católica. He said the Peruvian sugar industry had to increase its efficiency to meet an expected increase in demand and in general counseled that entrance into the US market will require careful planning. Professor Tello explained that the success of the treaty "depends fundamentally on what businessmen plan to do in the face of the opportunity and increase in competition that these agreements bring."

#### *Observations*

Public statements by administration officials before Congressional Subcommittees cannot be construed simplistically as pressure to effect change in the behavior of the Peruvian and Ecuadorian governments, because the US Congress will not let the administration back off easily from such statements unless substantial progress is made. Whether a final agreement is reached with Colombia only, or also with Peru and Ecuador, the window of opportunity for Congressional approval is indeed narrow. The agreements would not be sent to the US Congress until spring 2005, shortly before the president's Trade Promotion Authority expires in the summer. Timing is everything if Central America and the Andean countries want to get their respective FTAs approved next year.

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