UNITED STATES TRADE DISPUTES IN PERU AND ECUADOR

HEARING

BEFORE THE

SUBCOMMITTEE ON
THE WESTERN HEMISPHERE

OF THE

COMMITTEE ON
INTERNATIONAL RELATIONS
HOUSE OF REPRESENTATIVES

ONE HUNDRED EIGHTH CONGRESS

SECOND SESSION

OCTOBER 6, 2004

Serial No. 108–151

Printed for the use of the Committee on International Relations

Available via the World Wide Web: http://www.house.gov/international_relations

U.S. GOVERNMENT PRINTING OFFICE

96–358PDF WASHINGTON : 2005

For sale by the Superintendent of Documents, U.S. Government Printing Office
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UNITED STATES TRADE DISPUTES IN PERU AND ECUADOR

WEDNESDAY, OCTOBER 6, 2004

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON THE WESTERN HEMISPHERE,
COMMITTEE ON INTERNATIONAL RELATIONS,
Washington, DC.

The Subcommittee met, pursuant to call, at 2:30 p.m. in room 2200, Rayburn House Office Building, Hon. Cass Ballenger (Chairman of the Subcommittee) presiding.

Mr. BALLENGER. The Subcommittee will come to order.

This afternoon the Subcommittee will receive testimony from two panels regarding the United States investment disputes in Peru and Ecuador. Our first panel will present testimony on behalf of the Administration, and the second panel will present perspectives from the private sector.

We informed the Embassy of Peru and the Embassy of Ecuador that we would have welcomed testimony from representatives of their Governments in this open hearing. Neither Embassy chose to accept this offer.

I would like to thank my colleague from New Jersey, the Ranking Member of this Subcommittee, Mr. Menendez, for his leadership in pursuing this hearing. Our views may differ on some matters, but we both have been watching as U.S. investment disputes in these countries, involving hundreds of millions of dollars, have dragged on and on with no end in sight.

In Peru, I am especially concerned about the mistreatment of a number of American companies by Peru's national tax authority, SUNAT. We have received a long list of American companies that all tell a similar story of arbitrary taxation. We are aware of problems faced by Doe Run Corporation, Duke Energy International, Global Crossing, PSEG Global and Sempra Energy, and the Engelhard Corporation.

We will hear a first-hand account of these abuses from an Engelhard executive on our second panel.

I know that President Alejandro Toledo and many leaders in Peru are serious about promoting free trade and encouraging foreign investment, but in my considered opinion, it looks to me more like Peru's tax authorities see American companies as some sort of money tree.

Similarly, in Ecuador, I am told that President Lucio Gutierrez and key members of his Government, such as the Minister of Trade, Yvonne A-Baki, and Foreign Minister Zuquilanda support

creating economic opportunities through free trade with the United States.

But there are real problems in Ecuador that raise serious questions about the basic rule of law. The Solicitor General in Ecuador, Jose Marie Borja, is pursuing action to expropriate, without compensation, nearly a billion dollars in assets owned by an American company. Mr. Borja has apparently even suggested changing Ecuador's bilateral investment treaty to pave the way for expropriations.

Chevron Texaco is facing a one-sided environmental lawsuit in Ecuador. It is not at all clear that Chevron Texaco will get a fair hearing despite having complied with its obligations and receiving a full release from further liability and responsibility from Ecuador's state oil company and Ecuador's Ministry of Energy.

I strongly support the U.S. Trade Representative's effort to negotiate a free trade agreement with Colombia, a country which is a strong ally in the war on drugs and the war on terrorism. Colombia has demonstrated that it can resolve investment disputes with United States companies in a fair and timely manner.

It remains to be seen if Peru and Ecuador can demonstrate that they are equally serious. Time is running short. Peru and Ecuador should not drag a free trade agreement with Colombia down.

In my considered opinion, Peru and Ecuador need to know that we are prepared to hold off on further free trade negotiations until they can resolve these investment disputes and assure that American companies are treated in a fair and equitable manner.

Quite frankly, maybe we need to also take a look at whether Peru and Ecuador deserve the trade benefits that the U.S. Congress granted under the Andean Trade Promotion and Drug Eradication Act.

Mr. Menendez, I recognize you for an opening statement.

Mr. MENENDEZ. Thank you, Mr. Chairman, for holding this hearing, and for your support and leadership on this issue. I personally regret that we are having this hearing, that we have to have this hearing. I regret that all of our private treaties—directly to the respective countries, to their representatives, to the State Department, to the Trade Representative and others—have not had a receptive ear in the respective countries, because I know that both the Chairman and I are enormous advocates for our relationships in this hemisphere. We are enormous advocates for development opportunities and investment opportunities, but you cannot be advocates when there is no transparency and a lack of rule of law.

So today we are here to talk about the rule of law which protects the Peruvian people, Peruvian businesses, and international investors. As President Dwight D. Eisenhower once said,

> "The clearest way to show what the rule of law means to us in everyday life is to recall what has happened when there is no rule of law."

Imagine if there was no rule of law in the countries we are here to discuss today. Clearly, that is not true. There is a rule of law, but clearly the rule of law, at least in terms of international investment, is seriously threatened in Peru.

The rule of law is fundamental to the health of any nation. It protects a country's citizens, creates a safe environment for business to flourish and economies to grow, and encourages investment by international businesses. But the rule of law is seriously threatened when the Government or a branch of Government acts in violation of a country's own laws, violates legal contracts, and arbitrarily changes agreements.

Mr. Chairman, we have both been deeply concerned about the investment climate in Peru for several years now. Numerous United States companies have consistently reported that the Peruvian Government, specifically the tax authority, SUNAT, has violated legal contracts signed with these companies and unlawful or retroactively changed tax assessments.

In addition, the Peruvian Government and SUNAT have persisted in their actions against these companies. Even when their own courts have overturned these actions, the Peruvian Government and SUNAT have circumvented these rulings and used the appeals process in order to circumvent what have been the legal decisions of the law of the land in their country.

Now, I understand that serious and similar concerns have also been raised about the investment climate and the rule of law in Ecuador, specifically related to the expropriation of foreign assets. I hope the witnesses will provide us with more information on those important issues as well.

I want to take one case as emblematic of the problem. In the case of Engelhard in Peru, the Peruvian Government seized over $30 million in Engelhard assets and tax refunds based on false charges and unproven accusations. In spite of 5 years of numerous court rulings and independent audits which support Engelhard's actions as legal and appropriate, Engelhard is still waiting for due process, fair treatment by the system, the return of their $30 million and the exoneration of their employees.

A second company, PSEG, has invested in Peru, has been a friend of Peru, and has contributed to Peru's economy and future. Yet, over the past 6 years, PSEG has been subject to judicial decisions based on a moving target. Every time the court finds in PSEG's favor, SUNAT, which I believe is a rogue agency, discovers a new basis to assess back taxes and evade the ruling.

Even good companies playing by the rules of Peru that want to invest in Peru's economy, have been caught in the web of SUNAT's capricious and, I believe, illicit behavior. I have held numerous meetings over the past 6 years, as the Ranking Member on this Committee, with the Peruvian Government and was repeatedly assured these cases would be resolved.

Mr. Chairman, you and I, along with a number of other Members, wrote a letter on April 4, 2003, noting the unfair treatment of U.S. companies, and raising concerns over future trade agreements and investment projects. We wrote a letter on February 12, 2004, before the beginning of negotiations on the Andean Free Trade Agreement, stating our belief that the United States should not enter into negotiations until these issues were resolved. I would like to submit those letters for the record.

[The information referred to follows:]

Congress of the United States

Washington, DC 20515

April 4, 2003

Dear Colleague:

We want to bring to your attention the unfair treatment a leading American *Fortune 500* company, Engelhard Corporation, continues to receive from the Government of Peru. Engelhard, a world-leading surface and materials science company with more than 6,000 employees, is headquartered in New Jersey and has operations around the world and in 18 states including Alabama, Georgia, Kentucky, Mississippi, New York, Ohio, South Carolina, and Texas.

Other American companies, such as New York-based Princeton Dover, continue to receive unfair treatment at the hands of the Peruvian Government, and this troubling fact is best represented by Engelhard's four-year struggle for true justice in Peru.

An impartial look at the record will show that in 1999, corrupt members of the Fujimori government used an ex-post facto executive order (which has since been declared unlawful by the Peruvian Tax Court) to seize $20 million in Company assets in Peru, unlawfully withheld another $10 million in tax refunds legally due the Company, asserted frivolous claims to recapture previous refunds, and concocted false information in order to prosecute its employees. Two court rulings, three independent audits and a non-partisan Peruvian Congressional investigation have all concluded that there is no evidence that the company or its employees acted improperly.

Furthermore, the non-partisan Peruvian Congressional Commission's corruption investigation concluded that Engelhard was the victim of an aggressive conspiracy involving ex-spy chief Vladimiro Montesinos and senior officials at Peru's tax agency.

The Congressional Commission's final report stated, in part:

"... the Commission believes there are sufficient grounds to charge Alberto Fujimori as ex-President of the Republic and Jaime Iberico as National Administrator of the Tax Administration (SUNAT) with the crimes of Criminal Conspiracy against the state and several gold companies..." *(of which Engelhard was one.)*

A key Peruvian official who investigated Engelhard's case, the renowned and reputable former Finance and Economic Minister, Pedro-Pablo Kuczynski, found that the company was victimized, a conclusion he shared in a conversation with a U.S. Senator.

Minister Kuczynski, who oversaw the tax agency, was removed from his position last summer before he could fairly resolve the case and return the company's funds. Since his departure, Peru has patently resumed manipulating the courts against Engelhard, including issuing an incredible, precedent-setting tax court decision this February which has the same prejudicial impact on Engelhard as the ex-post facto law (referenced above) this same court declared illegal last June. All the while, Peruvian

officials routinely tell U.S. Congress and Administration officials that the company is receiving "fair treatment and due process."

Even today, we have serious misgivings about the veracity of the information distributed by the Government of Peru when meeting with U.S. Government officials and Members of Congress. Peru's Embassy recently distributed to some Congressional offices a "PowerPoint" presentation that is demonstrably replete with information that is simply false and distorts the true nature of its unlawful actions against Engelhard.

Engelhard Corporation heeded the call of both US and Peruvian officials to invest in Peru. It did so in good faith and has been a good corporate citizen. The result has been a bitter disappointment for the company and a loss for Peru. At the time Peru seized Engelhard's assets, the company was completing the construction of a state-of-the-industry gold processing facility that would have generated significant economic activity and employed many Peruvians. As a direct result of Peru's actions, the company never opened the facility and those jobs were never created.

We understand that the Peruvian Government will seek direct investment treaties and additional U.S. foreign assistance resources for the next fiscal year. These requests are in addition to U.S. support for multilateral funding, through the Inter-American Development Bank, for a natural gas pipeline known as the CAMISEA project. We hope that consideration of U.S. support for CAMISEA and any future trade treaties and funding actions by the House in support of Peru will be weighed against how quickly it corrects the egregious wrong it has committed against Engelhard, and other American companies such as Princeton Dover.

If you and your staff have questions or need additional information, please call Pedro Pablo Permuy with Congressman Robert Menendez (202-225-7919) or Alex DelPizzo (202-225-5361) with Congressman Mike Ferguson.

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Member of Congress

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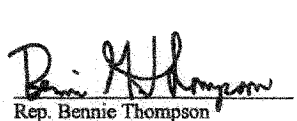
Member of Congress

Rep. Cass Ballenger
Member of Congress

Rep. Charlie Norwood
Member of Congress

Rep. Charles W. "Chip" Pickering, Jr.
Member of Congress



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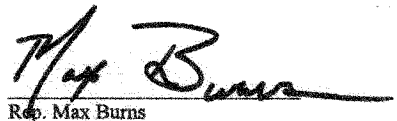

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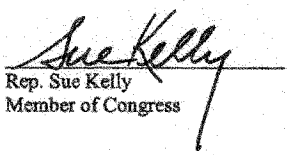

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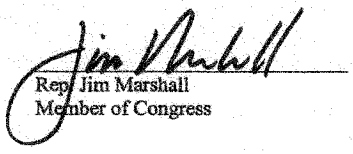

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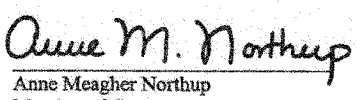

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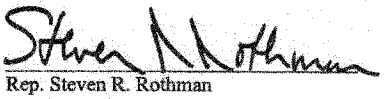

Rep. Steven R. Rothman
Member of Congress

cc: The Honorable Colin L. Powell
U.S. Secretary of State

The Honorable Donald L. Evans
U.S. Secretary of Commerce

The Honorable Robert B. Zoellick
U.S. Trade Representative

Congress of the United States
Washington, DC 20515

February 12, 2004

The Honorable Robert B. Zoellick
United States Trade Representative
600 Seventeenth Street, N.W.
Washington, D.C. 20508-0001

Dear Ambassador Zoellick:

You recently announced that the United States would begin negotiations on bi-lateral trade agreements with the Andean countries, including Peru. In the context of a potential free trade agreement with Peru, we are writing to express our concern over the treatment of several U.S. companies by agencies of the government of Peru. Specifically, we do not believe that the U.S. should enter into negotiations on a free trade agreement with Peru until these issued have been resolved.

The United States, Canada, and other international investors have made significant investments in Peru, amounting to over $3.5 billion in recent years, and have contributed to Peru's economy and to job creation. The Peruvian government entered into specific agreements with these companies regarding tax assessment and collection and under the premise of a transparent tax and judicial system.

SUNAT, the tax collection agency, has retroactively changed these agreements and applied tax rulings in a non-transparent, capricious manner against a variety of U.S. companies. SUNAT's apparent disregard for the rule of law and the failure to provide transparency in government actions is detrimental to foreign investors in Peru.

In order to attract foreign investors in the 1990s, the Peruvian Government entered into Legal Stabilization Agreements with U.S. companies expressly to provide protection from specific changes in Peruvian laws and regulations, and tax regime stability. Through SUNAT's actions against these companies and other foreign investors, the Government of Peru is breaching its obligations under those Agreements.

Moreover, in light of the terms of the Andean Trade Promotion and Drug Eradication Act (ATPDEA), we note that these actions constitute the imposition and enforcement of certain taxes against corporations that are more than 50% owned by U.S. citizens, the effects of which amount to: (a) the repudiation of an agreement previously entered into by the Peruvian Government; and (b) the expropriation or seizure of property by the Peruvian Government.

SUNAT's apparent disregard for the rule of law and the failure to provide transparency in government actions is detrimental to foreign investors in Peru and amount to a creeping expropriation. The United States should clearly communicate to the highest authorities in the Peruvian Government that SUNAT's recent actions are incompatible with free-market principles, and violate the spirit and letter of the ATPDEA.

We are deeply concerned about the Peruvian government's treatment of these companies and that, in the future, other U.S. companies may receive similar treatment. The United States government must set clear standards for countries based on their treatment of U.S. companies and functioning and transparent judicial systems, particularly as it is beginning the process of negotiating numerous free trade agreements.

The US must ensure that its trading partners do not misuse their own justice systems to gain unwarranted advantage in groundless administrative proceedings, particularly against US owned corporations. This causes irreparable damage to free trade and to a country's own citizens. This conduct must be remedied promptly and fairly before any free trade agreement is considered.

We support the Peruvian government's efforts to improve Peru's economic future and, in so doing, improve the quality of life for all of Peru's citizens. All Peruvians will benefit from a transparent and stable legal system that promotes the rule of law. Peruvian and foreign companies need this stable environment so that they can create jobs and invest in the Peruvian economy. U.S. companies, which have invested in Peru for many years, have the potential to play a significant role as investors in Peru 's economy.

We urge the Peruvian government to take immediate action to address these concerns which will create a positive legal and investment environment for both Peruvian and foreign companies and contribute to the economic development of Peru. We believe it would be both difficult and imprudent for the United States to conclude any bilateral trade agreement with Peru before these concerns are fully resolved.

Sincerely,

Rep. Cass Ballenger
Chairman
Western Hemisphere Subcommittee

Rep. Robert Menendez
Ranking Member
Western Hemisphere Subcommittee

Mr. MENENDEZ. The time for waiting is over. Let me state what I have said privately in meetings. I will not support an Andean Free Trade Agreement that includes Peru unless these cases are resolved.

I agree with the Chairman in his statement that the United States may need to reconsider benefits granted under the Andean Trade Promotion and Drug Eradication Act. I state these beliefs not simply for the sake of resolving these cases or these issues, but to set a precedent for the respect for the rule of law for future United States companies that invest in Peru.

Let me also state clearly that I respect the sovereignty of the country of Peru. I remain, however, deeply concerned when the judicial system, no matter how slow, rules in favor of a company and yet SUNAT continues to circumvent rulings and appeal cases.

Our concern cannot simply be for U.S. companies, however. It is in Peru's interest to create a climate that attracts rather than repels foreign investors. It is in Peru's interest to create a stable business environment which will benefit local companies. It is in Peru's interest to clearly establish the rule of law for all of her citizens.

So let me be clear. Multiple companies for many years have suffered the same mistreatment under the hands of SUNAT. We see a clear and persistent pattern that simply must change. The time for words and rhetoric is over. The time for action is long past due.

Mr. Chairman, thank you again. I look forward to hearing from the witnesses and for the questions I intend to pose to them.

Mr. BALLENGER. Mr. Weller, do you have an opening statement?

Mr. WELLER. Thank you, Mr. Chairman. It is good to have these witnesses before the Subcommittee today.

Chairman Ballenger, Ranking Member Menendez, I want to thank you today for holding this hearing highlighting our challenges and opportunities in the Andean region. The United States has a strong partnership with Ecuador, Peru, Bolivia and Colombia. We have an opportunity to strengthen our relationship through the proposed Andean FTA.

As many know, I recently led a codel over August recess to both Ecuador and Peru, as well as Venezuela and Bolivia, where we discussed a variety of issues, including security, narcotics, terrorism, and trade. There are significant benefits to be gained for all countries involved in a free trade agreement not only economically as our region competes with Asia, but also in hemispheric partnership and security.

For the United States, we want to open markets for our products. For a district like mine, which has a significant manufacturing and agricultural presence, this means increased export opportunities and real jobs. For the Andean countries, an FTA would mean guaranteed market access and increased investment. For all of our countries, it would mean increased hemispheric cooperation and reinforce our efforts at narcotics eradication and hemispheric security. For these reasons, I want to see a successful Andean FTA being negotiated and completed.

That being said, it is important that we move forward with negotiating this agreement that Peru and Ecuador act in good faith to resolve outstanding investment disputes. Several United States

companies have current and active disputes in Ecuador and Peru. While there has been progress in many cases, there are still several which remain outstanding. I am pleased with the efforts made toward resolution on many of these disputes, but these outstanding cases should be resolved expeditiously in a fair and transparent manner.

On my codel, in meetings with President Gutierrez of Ecuador and President Toledo of Peru and leaders of their respective congresses, we raised these concerns which are of paramount concern to the United States. Not only do these cases, in particular, represent serious cost to these United States businesses, but they also represent serious concerns not only for investors, but for future investors in these countries and for our Government as we seek to solidify our trading partnership.

As our countries move forward with negotiations over the coming months, it will be critically important for the United States to see serious and measurable progress on these outstanding investment disputes. Open, quick, and fair resolution of these cases is crucial to moving forward in successful completion of the proposed free trade agreement.

These cases set a standard and precedent for how United States investment will be treated in Ecuador and Peru. We must know with certainty that laws, regulations, and taxing bodies in Peru and Ecuador allow for fair resolution of disputes in an efficient and timely manner. It is my hope that Peru and Ecuador will continue to take the steps necessary to resolve outstanding investor disputes and that each of our countries is able to move forward with the proposed Andean Free Trade Agreement.

Thank you, Mr. Chairman.

Mr. BALLENGER. I welcome Representative Delahunt and Representative Faleomavaega.

Mr. FALEOMAVAEGA. Mr. Chairman, I do have an opening statement.

Mr. Chairman, I thank you and our Ranking Member, Mr. Menendez, for holding this hearing. I welcome today's witnesses, especially Ms. Regina Vargo, Assistant U.S. Trade Representative for the Americas.

I have had an opportunity to share with Ms. Vargo my concerns about the impact the Andean Free Trade Agreement may have on my district, and I commend her for taking my concerns into account as negotiations move forward. For the record, I would like to state I am uneasy about trade negotiations moving forward at a time when political instability has undermined the rule of law in Ecuador. Despite promises made by President Gutierrez's administration to adopt economic reforms and protect American investments, his efforts are often muted by special interests, even within his own administration.

Today, there continue to be commercial disputes between American companies and the Government of Ecuador. The most egregious examples, to the detriment of American companies, involve Bell South, Chevron Texaco and Occidental Petroleum.

While I am pleased that the USTR has traveled to Peru and Ecuador and threatened to drop them from trade talks due to their unwillingness to cooperate on investment issues, that becomes an

obstacle to a pact with Colombia. I have concerns that tuna may once again be used as an instrument of foreign policy.

Presently, the Andean countries have the capacity to destroy the entire United States tuna industry as it currently operates in my district (American Samoa), Puerto Rico and California. Ecuador and Colombia have the capacity to jointly process 2,250 tons of tuna per day, or in other words, produce 48.6 million cases per year. Given that United States total consumption is about 48 million cases per year, the Andean countries definitely will destroy the U.S. tuna industry if we allow them the same benefits given in terms of our tariffs and trade negotiations. Given the fact that the labor costs are so cheap, and the fact that a fish cleaner in an Andean country gets paid only about 60 cents an hour, gives us real concern in terms of the variable here that we want to explain a little further.

Fleet capacity is another area of important consideration. The Andean countries have the capacity to expand their fishing fleets if provided with incentive to do so. There is no barrier preventing the Andean countries from bringing fish in from the western tropics for processing. Japan, Thailand, Taiwan, to name a few, could ship frozen tuna loins to the Andean countries for final processing; therefore, defeating the intent of the United States-Andean trade, which is to create jobs and build capacity in the Andean region. In other words, I do not want to see the United States give Ecuador tuna in exchange for Ecuador's commitments to resolve investment disputes involving Chevron Texaco, Bell South, and Occidental Petroleum.

I also do not believe that a discussion about tuna should be included with the rhetoric of antidrug campaign. Although I want to be helpful to Ecuador in its efforts to curb drug production, I continue to believe that the issue of preferential treatment for canned tuna should be debated on its own merits, and I am hopeful this will be the case.

Mr. Chairman, I thank you and look forward to hearing our witnesses' testimony.

Mr. DELAHUNT. Mr. Chairman, I want to recognize the Deputy Assistant Secretary, Bureau of Western Hemisphere. We have known Mr. Shapiro for some time. It is nice to see him in Washington. I am sure it is a different experience for him.

I should say publicly that the Ambassador served his country well during his tenure to Venezuela. It was a difficult experience for all of us. I think his contribution in a true bilateral relationship is important. As we all look back on the experience of the past 3 years, progress is being made. It is good to have you here.

Mr. BALLENGER. Since I am a gentleman, I will ask the lady on the panel to go first.

Ms. Regina Vargo is Assistant U.S. Trade Representative for the Americas. Ms. Vargo is a veteran trade policy expert with extensive experience in the Western Hemisphere region. She joined the USTR in June 2001 after spending nearly 30 years with the Commerce Department, serving in a number of high-level positions specializing in trade with countries in the Western Hemisphere.

With that, it is all yours.

STATEMENT OF REGINA K. VARGO, ASSISTANT U.S. TRADE REPRESENTATIVE FOR THE AMERICAS

Ms. VARGO. Thank you, Mr. Chairman, Congressman Menendez, and other Members of the Subcommittee. I appreciate the opportunity to appear today to discuss the Administration's position on the topic of United States investment disputes in Peru and Ecuador. This is a matter that not only I, but also Ambassadors Zoellick and Allgeier, senior officials at the Department of State, the Commerce and Treasury Departments, and the U.S. Ambassadors to those countries have followed very closely. Allow me to begin by placing the issue in context.

Successive Administrations and the U.S. Congress have shared the view that we have a stake in the success of the Andean region. Colombia, Peru, Ecuador, and Bolivia are partners in the fight against narcotrafficking and terrorism. I know this Subcommittee knows that well.

In 1991, Congress passed the Andean Trade Preference Act, or ATPA, to strengthen the economies in the region as part of our overall counternarcotics strategy. In 2002, Congress worked with the Administration to renew and expand the program to previously excluded products.

The ATPA program contains a number of criteria in order for countries to be eligible for the benefits. The Administration sought public comment in the fall of 2002 on the question of whether the countries fulfilled the criteria of the renewed program. A number of United States investors in Peru and Ecuador, in particular, identified issues or cases in which the countries may have run afoul of the criteria. We also heard concerns regarding workers' rights in Ecuador.

The Administration secured from the Andean countries a number of actions and commitments before designating them as eligible for the program's benefits.

Ambassador Zoellick continues to press his Peruvian and Ecuadorian counterparts to advance our objectives in these areas and we have consulted closely with Members of Congress. We also worked very closely with the affected companies and will continue to do so.

Subsequently, in November 2003, the Administration notified Congress of its intent to initiate the negotiation of a free trade agreement to ultimately include Colombia, Peru, Ecuador and Bolivia. In that notification we made the case for why an FTA with these countries would be in the interest of the United States. We also indicated that particular Andean countries needed to make further progress to address inadequate protection of worker rights and to ensure the fair and expeditious resolution of a number of disputes involving United States investors.

In May 2004, when the Administration announced the launch of the Andean FTA negotiations, we indicated that the Peruvian Government had recently resolved certain additional outstanding disputes with United States investors and had taken significant steps to resolve others. Similarly, we noted that the Ecuadorian Government had taken important steps to address certain concerns regarding the protection of worker rights and had resolved certain investor disputes. We went on to say that work remained to be done

in order for all outstanding issues to be completely resolved, and that the U.S. Government would continue to work with Peru and Ecuador to follow through on these matters as the negotiations proceeded.

The following month Ambassador Zoellick strongly reinforced this message in meetings with President Toledo and President Gutierrez during a trip to the region. In fact, he did so just this morning in a meeting with Peruvian Trade Minister Alfredo Ferrero, and last month with Ecuador's Trade Minister Ivonne Baki.

It is important to acknowledge that the Governments of Peru and Ecuador have, in fact, resolved some investor disputes and have made progress in addressing several others during the period I described. However, a number of disputes remain unresolved and progress to date has not been sufficient.

This issue has significance on several levels. The U.S. companies involved collectively have hundreds of millions of dollars at stake in the resolution of these disputes. Beyond this, the countries in question need to consider what signal they are sending to potential new investors, given the uncertainty created by the way a number of our companies have been treated.

Finally, the Administration and Members of Congress need to have confidence that the rule of law is fully respected by our prospective FTA partners.

I must say I have heard nothing to suggest any disagreement on this side of the table with those expressions we have heard the Members suggest in their opening remarks.

We have worked hard to ensure that the Governments of Peru and Ecuador understand the stakes and the need to find the will to ensure that these matters are resolved in a transparent manner, consistent with due process. We have been scrupulously careful not to call for specific outcomes in these cases. What we have insisted on is a fair, prompt, and transparent treatment of our companies when they seek to enforce their rights either through the countries' courts or through arbitration. We strongly believe that such treatment will not only benefit our companies but will also benefit Peru and Ecuador.

Thank you, Mr. Chairman, for inviting me to testify before the Subcommittee today on this important issue. I would be happy to answer any questions that you or your colleagues may have.

Mr. BALLENGER. Thank you.

[The prepared statement of Ms. Vargo follows:]

PREPARED STATEMENT OF REGINA K. VARGO, ASSISTANT U.S. TRADE REPRESENTATIVE FOR THE AMERICAS

Mr. Chairman and Members of the Subcommittee, I appreciate the opportunity to appear before you today to discuss the Administration's position on the topic of U.S. investment disputes in Peru and Ecuador. This is a matter that not only I, but also Ambassadors Zoellick and Allgeier, senior officials at the State, Commerce and Treasury Departments, and the U.S. Ambassadors to those countries have followed very closely. Allow me to begin by placing the issue in context.

Successive Administrations and the U.S. Congress have shared the view that we have a stake in the success of the Andean region. Colombia, Peru, Ecuador and Bolivia are partners in the fight against narcotrafficking and terrorism. In 1991 Congress passed the Andean Trade Preference Act, or ATPA, to strengthen the economies in the region as part of our overall counternarcotics strategy. In 2002 Congress

worked with the Administration to renew and expand the program to previously excluded products.

The ATPA program contains a number of criteria in order for the countries to be eligible for the benefits. The Administration sought public comment in the fall of 2002 on the question of whether the countries fulfilled the criteria of the renewed program. A number of U.S. investors in Peru and Ecuador, in particular, identified issues or cases in which the countries may have run afoul of the criteria. We also heard concerns regarding worker rights in Ecuador. The Administration secured from the Andean countries a number of actions and commitments before designating them as eligible for the program's benefits.

Ambassador Zoellick continues to press his Peruvian and Ecuadorian counterparts to advance our objectives in these areas and we have consulted closely with Members of Congress. We also worked very closely with the affected U.S. companies and continue to do so. Subsequently, in November 2003 the Administration notified Congress of its intent to initiate the negotiation of a free trade agreement (FTA) to ultimately include Colombia, Peru, Ecuador and Bolivia. In that notification we made the case for why an FTA with these countries would be in the interest of the United States. We also indicated that particular Andean countries needed to make further progress to address inadequate protection of worker rights and ensure the fair and expeditious resolution of a number of disputes involving U.S. investors.

In May 2004, when the Administration announced the launch of the Andean FTA negotiations, we indicated that the Peruvian Government had recently resolved certain additional outstanding disputes with U.S. investors and had taken significant steps to resolve others. Similarly, we noted that the Ecuadorian Government had taken important steps to address certain concerns regarding the protection of worker rights and had resolved certain investor disputes. We went on to say that work remained to be done in order for all outstanding issues to be completely resolved, and that the U.S. Government would continue to work with Peru and Ecuador to follow through on these matters as the negotiations proceed. The following month Ambassador Zoellick strongly reinforced this message in meetings with President Toledo and President Gutierrez during a trip to the region.

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This issue has significance on several levels. The U.S. companies involved collectively have hundreds of millions of dollars at stake in the resolution of these disputes. Beyond this, the countries in question need to consider what signal they are sending to potential new investors given the uncertainty created by the way a number of our companies have been treated. Finally, the Administration and Members of Congress need to have confidence that the rule of law is fully respected by our prospective FTA partners.

We have worked hard to ensure that the Governments of Peru and Ecuador understand the stakes and the need to find the will to ensure that these matters are resolved in a transparent manner consistent with due process. We have been scrupulously careful not to call for specific outcomes in these cases. What we have insisted on is the fair, prompt and transparent treatment of our companies when they seek to enforce their rights either through the country's courts or through arbitration. We strongly believe that such treatment will not only benefit our companies but will also benefit Peru and Ecuador.

Thank you, Mr. Chairman, for inviting me to testify before the Subcommittee today on this important issue. I would be happy to answer any questions that you or your colleagues may have.

Mr. BALLENGER. Next, we will hear from Mr. Earl Anthony Wayne. Mr. Wayne is Assistant Secretary of State in the Bureau of Economic and Business Affairs. Issues under Mr. Wayne's purview include international finance, development debt, investment policy, economic sanctions, international energy trade policy, international telecommunications and information issues, international transportation and aviation and commercial and business advocacy overseas.

You have my condolences there. I turn it over to you.

STATEMENT OF THE HONORABLE EARL ANTHONY WAYNE, ASSISTANT SECRETARY, BUREAU OF ECONOMIC AND BUSINESS AFFAIRS

Mr. WAYNE. Thank you, Mr. Chairman. Thank you Ranking Member Menendez and everybody else for giving us this opportunity to discuss this very serious issue.

Our investors do face serious challenges, a number of them in Peru and Ecuador. We have been working hard, as you have, to try to address these for several years now.

I also want to say that we very much appreciate your role as Chairman of the Subcommittee and all of the work the Subcommittee has done to help highlight our focus on improving trade regulations within the Western Hemisphere. I know you were a strong supporter of this, Mr. Chairman, when we announced that we intended to rejoin the International Coffee Organization, which was well received in the Hemisphere, as on other continents.

In fact, I think holding these hearings is very important to reinforce the efforts we have been making from the official side, diplomatically and in our trade discussions, to underscore to these Governments how important these issues are.

As the number of disputes suggest, the investment climates in both Peru and Ecuador present serious challenges. In Peru, we have a larger market. There is a large U.S. company presence—about 150 companies present there—but we have had very serious specific cases which have endured longer than any of us think they should have endured, and we share the frustration that we heard from all of you in your initial comments, to get these resolved. We have repeatedly raised them in different meetings with different cabinet members from President Toledo on down to the official level; and there has been some progress, but not enough progress.

In Ecuador, we have a smaller number of United States investors, but I think they, relative to their size, find an even more difficult investment climate. The number of problems there is greater, relevant to about 50 U.S. companies that are present there. Here again, from the Presidential level in Ecuador on down we have repeatedly stressed the importance of resolving these issues, both because of the interest to the United States and for U.S. companies, but in general for their ability to attract more investment and to grow.

I don't believe that U.S. investors are receiving particularly discriminatory treatment in these countries. I think the problems that our companies have faced are faced by indigenous companies and companies from other investors also. However, our Ambassadors have made addressing these problems an extremely high priority, and they have been championing long, hard and consistently the interest of U.S. firms.

As Regina Vargo indicated, we have been using a number of tools to try to move these processes forward. We have been using the ATPDEA process and the comment process that that opens for everybody to offer their complaints, their thoughts, their comments, for us to take into account as the U.S. Government reviews the benefits that are available. We also have been trying very hard to use the leverage and the promise of a free trade negotiation to bring solutions to these problems.

We do believe that there is benefit in having a free trade agreement with these countries because it puts higher standards in place. It helps encourage better performance.

At the same time, we have been quite clear that it is an evident fact that completing these negotiations and bringing an agreement forward to Congress will take seriously into account the status of these investment disputes and what has happened. We know that, and your sentiments expressed today reinforce that message.

Right before we started the negotiations, I personally went to all three countries, Ecuador, Peru and Colombia, and tried to underscore to them the importance of finding solutions to these problems. Frankly, my colleagues and I have been disappointed by the progress we have had since that time.

We will continue to work hard and caution these countries about the danger for the FTA, as well as the necessity for finding solutions. At the same time, we will keep in mind, as several of your statements have underscored, that these countries represent political and economic systems that are still developing. Both countries are democracies, but they have governance structures that are still fragile; political institutions that are weak; and vested interests that are still quite entrenched. This is part of the reason that we are providing development assistance and technical capacity-building assistance to these countries.

We think that senior leaders in both Governments are very serious about tackling the problems ahead. We think that they want to see their countries progress, and they realize that involves creating a good investment climate. They are fighting drugs and strengthening democracy and improving good governance and raising the level of prosperity of their peoples and those in the Hemisphere.

Just yesterday and the day before, I participated in a series of meetings with Peru and other representatives from the G–8 Governments on a transparency pilot project that we are working on to support anticorruption efforts and increase transparency in Government in Peru, as well as in three other countries that we have chosen from around the world. We are very much committed to working with these Governments across the board, as well as addressing these specific issues and ways to improve the investment climate in general.

Let me close by reiterating something that several of you have already stressed. This is a very important region to us. We have a lot at stake. We have broad economic, political, and security interests that rest in the Andean region. That is why we and you, too, are investing so much energy and have helped to approve so many resources to put to work on a range of issues from promoting good governance to fighting narcotics, from negotiating the FTA to improving transparency.

There are flaws in the investment climate, and we have to seriously address them and correct them. You can be assured that we will work hard, and our Ambassadors have this at the top of their agendas. At the same time, we recognize we have a shared interest with Peru and Ecuador that we will continue to develop. I thank you for your partnership in this effort.

I look forward to answering your questions. Thank you.

[The prepared statement of Mr. Wayne follows:]

PREPARED STATEMENT OF THE HONORABLE EARL ANTHONY WAYNE, ASSISTANT SECRETARY, BUREAU OF ECONOMIC AND BUSINESS AFFAIRS

Chairman Ballenger, Ranking Member Menendez, and Members of the Committee, thank you for inviting me to appear before your Subcommittee to discuss the challenges facing U.S. investors in Peru and Ecuador and the steps we are taking to improve the investment climate and help facilitate the resolution of current disputes. Mr. Chairman, the Administration appreciates your leadership on Hemispheric relations and the outstanding attention that this Subcommittee has given to our efforts to strengthen U.S. trade and investment relations with Latin America. Thank you.

Support for American investors and businesses operating overseas is a front-burner issue for Secretary Powell and all of us at the State Department and in our Embassies and Consulates overseas. It is an issue that we in the Bureau of Economic and Business Affairs consider integral to our mission: building prosperity and economic security at home and abroad. As part of this goal, and cooperating closely with our interagency colleagues, we work to ensure that foreign governments do not discriminate against or improperly harm the investments or business activities of U.S. investors or businesses.

The Department's policy with regard to assisting U.S. businesses and investors has four primary elements: (1) encouraging foreign countries to open their markets, improve their investment and business climates, and provide nondiscriminatory and transparent operating conditions for U.S. investors and businesses; (2) negotiating investment agreements, including Bilateral Investment Treaties (BITs), investment chapters of Free Trade Agreements (FTAs), and other international accords that help protect the interests of U.S. investors operating outside the United States; (3) providing advocacy and other assistance to U.S. businesses and property owners abroad; and (4) using diplomatic and other tools to urge the prompt resolution of commercial and investment disputes involving U.S. nationals.

Under the first of these policy elements, work to improve the business and investment climate, we focus on removing investment and trade barriers and fostering actions that enhance transparency and rule of law. We have a persuasive message: those countries that have made the most progress towards open markets and democratic rule of law are the ones that have been most successful in attracting private sector U.S. investment. Still, entrenched special interests and poor governance and regulatory/judicial practices in many countries often make this a challenging process, and one that will continue to require our attention.

Our work is supported by our development assistance efforts. For example, the Millennium Challenge Account channels U.S. development assistance resources toward developing countries that have a proven record of governing justly, investing in their people and encouraging economic freedom. We are also moving forward through the G–8 on a number of initiatives intended to improve the business climate in developing countries, including the G–8 Action Plans on Entrepreneurship and on Fighting Corruption and Improving Transparency. On Monday, October 4, Under Secretary of State Larson hosted a meeting of his G–8 counterparts that discussed pilot business climate projects in several developing countries, and that also advanced pilot transparency projects with four countries, including Peru.

Second, we have an active program of negotiating investment agreements with foreign governments. These include Bilateral Investment Treaties (BIT), investment chapters of FTAs, and other investment agreements designed to promote fair investment regimes. We have BITs with 46 countries, including Ecuador; the US-Ecuador BIT entered into force in May 1997. NAFTA and our FTAs with Chile, Singapore, Australia and Morocco all contain investment chapters that cover much the same ground as a BIT. Our investment agreements have several specific aims:

- Protect the rights of American investors by granting them the option to settle certain disputes by referring them to binding international arbitration, instead of pursuing them in the local legal system;
- Protect investment abroad in those countries where investors' rights are not already protected through existing agreements (such as modern treaties of friendship, commerce and navigation);
- Encourage the adoption of market-oriented domestic policies that treat private investment in an open, transparent, and non-discriminatory way; and
- Support the development of international law standards consistent with these objectives.

One of the core benefits provided to investments by U.S. bilateral investment treaties and investment chapters of FTAs is that they establish clear limits on the expropriation of investments and provide for payment of prompt, adequate and effective compensation in the event an expropriation takes place. Also, BITs and investment chapters of FTAs give investors from both Parties the option to submit an investment dispute with the treaty partner's government to international arbitration, instead of pursuing the dispute in that country's domestic courts. This can be a key benefit for U.S. investors in cases where the local court system is seen as slow, ineffectual, or compromised.

However, it is important to note that expropriations are not per se illegal under international law (just as they are not per se illegal under U.S. law). The United States believes that an expropriation violates international law if the taking is discriminatory, is not for a public purpose or is not accompanied by provision of prompt, adequate and effective compensation.

Third, we provide various types of assistance to U.S. nationals and entities embroiled in commercial and investment disputes abroad. Both here in Washington and at our Posts overseas, we monitor disputes closely, and, although we cannot counsel U.S. investors on how to handle their disputes, we often share with them relevant information about foreign laws, judicial systems and claims procedures. In addition, the Department provides information about attorneys in the foreign state who have indicated an interest in representing U.S. nationals. The Department also provides consular assistance to all interested claimants who are currently U.S. nationals, including those who were not U.S. nationals at the time of expropriation.

Fourth, we make extensive use of all the tools at our disposal to communicate to foreign governments the U.S. interest in seeing disputes resolved fairly. Sometimes, formal diplomatic representations can help lead to resolution of the dispute. In other cases, we may explore using possible leverage to persuade the foreign government to work toward resolution. Whatever the strategy or tactic, our goal remains seeing a successful and transparent outcome. To that end, we have strengthened Embassy work on claims and disputes of U.S. nationals. We have also strengthened coordination in Washington of assistance to U.S. nationals, sent expropriation experts to meet with other governments and assess claims resolution progress, and encouraged other governments to adopt procedural avenues for investors to seek redress.

THE SITUATION IN THE REGION

As in many countries, American investors and businesses in Peru and Ecuador face a variety of difficulties, but most are nonetheless able to operate successfully. Yet while significant problems may not be the norm, the number of on-going and unresolved disputes underscores that there is clearly room for improvement.

Ecuador:

Nearly every U.S. company doing business in Ecuador has faced problems with Ecuadorian government entities, from regulatory bodies to the courts and the customs agency. The Section 527 Report to Congress on Expropriation Claims and Certain Other Investment Disputes lists for 2004 nine active disputes in Ecuador. The problems that these investors have reported to us include unclear and contradictory policy signals from competing governmental entities, inconsistent implementation of laws and regulations affecting foreign investors, and opaque judicial processes. The Ecuadorian judicial system suffers from processing delays, inconsistent rulings, limited access to the courts, and impunity, particularly in corruption cases. Since the existing system presents opportunities for malfeasance, undermining the enforcement of property and concession rights, more work is needed to ensure that strong anti-corruption measures are in place—and enforced—in the judiciary.

Lack of enforcement of contracts is another significant hurdle facing businesses in Ecuador, whether foreign or Ecuadorian. We have heard complaints that many government entities, especially the state oil, telephone, and electricity companies, routinely violate their contracts with domestic and foreign private firms.

Regrettably, a few officials seem to see foreign investors as targets for monetary or political exploitation and use regulatory schemes and questionable legal interpretations to achieve their ends. Whatever the motivation, this is precisely the wrong signal Ecuador needs to send. As Secretary Powell has stated, "Capital is a coward." Once scared away, it is hard to attract it back.

Peru:

Fortunately, the situation in Peru is considerably better. Although the Section 527 Report to Congress on Expropriation Claims and Certain Other Investment Disputes lists 12 active investment disputes in Peru, many of these are either under

arbitration or the jurisdiction of the local courts, including one under government appeal after a judgment that was favorable to the investors.

Notwithstanding these positive trends, in many cases investors in Peru reportedly face some of the same problems encountered by those in Ecuador. A 2003 World Bank study revealed a number of areas that had the effect of damaging Peru's business environment, including frequent changes in laws, regulations and some government economic policies and long delays and reports of corruption in the judicial system.

Actions by the Peruvian tax agency to revisit tax payments by a number of large foreign investors, some of which are U.S. companies, have generated unexpected potential liabilities of tens of millions of dollars for these companies. These disputes have indisputably harmed U.S. investors' views of the investment climate in Peru.

Senior Peruvian government officials, well aware of the problems with Peru's business climate, are promoting a number of reforms to address them. Improving the judicial system is one of President Toledo's stated priorities. For example, the Government of Peru in February established an inter-ministerial team headed by Peru's Prime Minister that oversees the commercial disputes and international trade negotiations. The group has met with the Ambassador on three occasions, the most recent on October 4 to review progress toward resolving the pending commercial disputes.

We are further encouraged by the September 30th Peru Supreme Court decision to proceed with the creation of specialized commercial courts with jurisdiction over, among other things, commercial and investment disputes. The 22 new first instance courts and 2 second instance courts for commercial cases—which we helped establish with training, assistance and equipment—should make adjudication in these cases more professional and equitable, and are enthusiastically welcome by the local and international businesses operating in Peru

WHAT WE ARE DOING

We are working on a number of fronts both to address the overall challenges to the investment climates in Ecuador and Peru, as outlined above, and to urge the prompt resolution of the specific outstanding disputes.

"Sunshine," as Justice Holmes once remarked, "is the greatest of all disinfectants." Leaders and senior officials in both Ecuador and Peru are committed to opening closed doors to let the sunshine in, and we are working to support this process. We find common ground in believing that greater transparency can help reduce the potential for the bribery and corruption that serves as a steep barrier to trade and investment. Translating political commitments into action, however, can itself be a challenge.

We have a number of initiatives underway on transparency and anti-corruption; while the focus is largely in encouraging change in the countries' domestic regimes, the ultimate beneficiaries of our initiatives would be both domestic and foreign investors. We are working to ensure that countries that signed various multilateral anti-corruption instruments fully implement their obligations. Both Peru and Ecuador are signatories to the Inter-American Convention Against Corruption. In addition, Peru is one of four pilot countries worldwide that signed transparency compacts with the G–8 at the Sea Island Summit this year, and we are working closely with Peru on follow-up.

USAID maintains several projects designed to improve the business climate in both countries. In Peru, these include, among other activities, a project to help establish sustainable commercial law systems; and a project to develop a proposal for municipal business registration to be completed at a single office with a single registration form, to dramatically lower registration time and costs.

We have also worked, and are still working, to enhance the protections available to U.S. investors in both countries. One significant benefit for American investors in Peru and Ecuador is that both countries accept binding international arbitration of investment disputes in accordance with national legislation or international treaties to which they are parties.

As noted above, a US-Ecuador Bilateral Investment Treaty entered into force in 1997, providing investors with a greater level of assurance that their disputes will be adjudicated fairly and in accordance with international norms. We see two current high profile disputes, involving firms in the telecommunications and petroleum sectors, as test cases regarding Ecuador's intentions with respect to honoring arbitral awards in accordance with its obligations.

Although the United States does not have a BIT with Peru, that country does permit international arbitration of disputes between foreign investors and the govern-

ment or state-controlled firms. As a result, binding international arbitration is an option for the resolution of investment disputes in Peru.

We have vital tools at our disposal that have proven to be effective in encouraging the governments of both countries to resolve their outstanding disputes. In pressing for progress in the resolution of outstanding disputes in both countries, we have made—and continue to make—active use of eligibility criteria in the Andean Trade Preference Act of 1991 and its successor program, the Andean Trade Promotion and Drug Eradication Act (ATPDEA), which provides beneficiary countries, including Ecuador and Peru, duty-free access to the U.S. market for a wide range of products. Moreover, with the granting of ATPDEA benefits in September 2002, Ecuador as well as Peru committed to resolve a number of commercial disputes.

Together with the U.S. Trade Representative's office and other agencies, we have also made clear in our Free Trade Agreement negotiations with Colombia, Ecuador and Peru that a successful negotiation depends on tangible progress in the resolution of outstanding investment disputes involving U.S. companies. When we announced the launch of FTA talks, we noted that Peru and Ecuador had resolved some disputes and had taken steps to resolve others.

DEPARTMENT OF STATE EFFORTS

Pressing for a resolution to the outstanding investment disputes in Peru and Ecuador remains a top priority for us here in Washington and for our Embassies in Lima and Quito. I have repeatedly engaged senior Ecuadorian and Peruvian officials on this, including during visits to Quito in January 2004 and to Lima in February 2004 and on a number of occasions since then I have met with Ecuadorian and Peruvian Ministers visiting Washington, most recently Ecuador's visiting Finance Minister, Mauricio Yépez, on September 7. My staff coordinates closely with our Embassies, where Ambassadors Struble and Kenney and their teams have been extremely energetic in pressing senior Ecuadorian and Peruvian officials, from the President down. In our approaches, we have cautioned both countries that, left unresolved, these disputes are a stumbling block to achieving an FTA. Both President Toledo in Peru and President Gutierrez in Ecuador have stressed the importance they attach to an FTA with the United States.

This hearing, Mr. Chairman, and other expressions of Congressional interest are very useful in reinforcing our diplomatic efforts. Individual Members have usefully raised the issue with Peruvian and Ecuadorian officials. We appreciate that.

I wish that I could assure you that developments with respect to several key disputes in Ecuador are moving in the right direction, but frankly the prognosis is still unclear. I believe that Ecuador's leaders clearly understand that we are watching events closely, and realize that the foreign investment community pays close attention to developments, weighing the opportunity costs of sticking it out in Ecuador versus investing in greener pastures elsewhere. Unfortunately, progress in Ecuador has been slow and at times uncertain, as recent developments with respect to a leading U.S. energy investor suggest.

In Peru, the news is somewhat more encouraging, but not yet satisfactory. Since 2003, one dispute involving a significant American investor has been resolved, and some—but not enough—progress has been made towards the resolution of other cases. We are not alone in understanding the importance of resolving these cases. Several concerned Peruvian private sector leaders have urged the President of the Supreme Court and the Minister of Justice to comply with the legal timeframes under Peruvian law. Private sector representatives have also spoken out publicly, calling for resolution of the disputes so that Peru does not lose a potential FTA that would give it duty-free access to the largest market in the world.

CONCLUSION:

Mr. Chairman, this is but a brief summary of our efforts to ensure that the rights of U.S. investors are fully respected in Peru and Ecuador and that all outstanding investment disputes are resolved. Although more work lies ahead of us, I believe we continue to make progress.

I would be happy to answer any questions.

Thank You.

Mr. BALLENGER. Being Chairman, I get first shot.

Ms. Vargo, Deputy U.S. Trade Representative Peter Allgeier is reported, referring to Ecuador and Peru, in the media as saying,

> "We will not endanger a free trade package with Colombia by having countries attached to it that are going to detract from

the congressional approval rather than add to it. There needs to be a lot more progress in both of those countries for us to be in a position that we, in confidence, can put forward a free trade agreement with those countries through the Congress."

That is a polite way of what I have been saying all along, but that is a good statement.

Do you mean it and is it the policy of the U.S. Trade Representative?

Ms. VARGO. Yes and yes, Mr. Chairman.

Mr. BALLENGER. Thank you kindly.

Ambassador Shapiro, the State Department's testimony highlights that a United States-Ecuador bilateral investment treaty entered into force in 1997. Is it true that Ecuadorian Solicitor General Borja has suggested abrogating or changing this treaty if it stands in the way of his plans to expropriate major American investments in Ecuador?

And why is Mr. Borja behaving this way? I understand he is running for President.

Mr. SHAPIRO. Yes, he has suggested that, sir. You have answered your own question. The gentleman has aspirations for higher office.

Mr. BALLENGER. In your opinion, can one person in a government such as that carry that much weight?

Mr. SHAPIRO. What he suggested was, the Congress of Ecuador abrogate the treaty. I don't believe that they are necessarily inclined to do so. Obviously, matters of treaties are the prerogative of the Executive Branch. Their Congress could abrogate the treaty.

Our Ambassador, U.S. Trade Representatives, our Embassy in Quito, our consulate general in Quito, the State Department here, the National Security Council—we have all told various Ecuadorian Government officials at various times that the investment climate is very important. Anything that would abrogate the bilateral investment treaty would sour that climate, and rather than attract investment, which Ecuador needs, would scare away that investment.

Mr. BALLENGER. Mr. Menendez.

Mr. MENENDEZ. Thank you, Mr. Chairman.

Well, I want to thank you for your testimony. I am disappointed in it. In my days as a trial attorney, I would say that this is the equivalent of "on one hand, this, and on the other hand, the other." I never quite know what that means. It is rather wishy-washy to me.

I don't agree, Mr. Secretary, with your statement where you say that we have positive trends with Peru and where you say there are significant steps. If I was one of these companies and others that are going down this road, as well, I wouldn't think there are any significant steps.

It is almost like a Texas two-step, one small step forward, an enormous step backwards. It will get you down the road where you are too far gone then they get their trade preferences and trade agreements and our companies are left hanging. The rule of law does not change, and in the context of the cost of trade at any price, we leave American companies exposed.

Let me ask you, Mr. Secretary, do you believe that SUNAT taxes international companies beyond the standard norms?

Mr. WAYNE. I believe that SUNAT's actions have continued to present serious problems to our companies, and they have kept us seriously busy, engaging the Government of Peru, particularly the Executive Branch, to find rapid due process solutions for our companies.

We are not satisfied with the progress which has been made. There has not been enough progress, but there has been some progress. The Government did establish a tax ombudsman and a decree requiring that before SUNAT can appeal a finding of a court case, it has to have the approval of the tax ombudsman and of the finance minister before it can do that. So if SUNAT loses in court, it cannot automatically, like it could before, make an appeal of that case.

Also, there has just been approval in Peru to set up a set of commercial courts that will be specifically aimed at dealing with commercial disputes that come up in a faster process than has been the case right now.

I think, as you probably know, the Peruvian court system has a tremendous backlog of cases, both criminal and civil cases, and this has troubled not only American companies, but Peruvian companies and other companies. One of the capacity-building responses to this has been to establish and put into place these commercial courts. But there is no question that the continued actions of SUNAT have been a real point of frustration for all of us as we have tried to find solutions.

Mr. MENENDEZ. Let me go back to my question.

First of all, the new ombudsman does not apply in every tax case, so that does not necessarily satisfy the opportunities for U.S. companies or international companies to be protected from arbitrary and capricious decisions.

Yes or no, does SUNAT tax international companies beyond the standard norms?

Mr. WAYNE. I will take that question and come back to you. I don't have a good answer.

[The information referred to follows:]

RESPONSE SUBMITTED IN WRITING BY THE HONORABLE EARL ANTHONY WAYNE, ASSISTANT SECRETARY, BUREAU OF ECONOMIC AND BUSINESS AFFAIRS TO QUESTION ASKED DURING THE HEARING BY THE HONORABLE ROBERT MENENDEZ, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF NEW JERSEY

Question:

Does Peruvian tax agency SUNAT tax international companies at levels beyond international norms?

Response:

Peru's corporate tax rates are considered to be relatively high but comparable to those of other countries in the region. Corporate tax rates, which are set by Congress not SUNAT, appear to be applied evenly to domestic and foreign firms alike, with the exception of some foreign firms that receive preferential tax rates as a result of favorable tax stability agreements. In that sense, international companies are not directly taxed in excess of international norms.

Partly to allay foreign investor concerns about SUNAT, in 2004 the Peruvian government stepped in and limited the agency's powers to, among other things, continue pressing its case after being told by the courts that it had no grounds to seek collection.

Ms. VARGO. I could do the same.

Mr. MENENDEZ. Does it violate tax agreements?

Mr. WAYNE. Mr. Menendez, I am not aware that it has violated a tax agreement with the United States.

Mr. MENENDEZ. Does it make arbitrary tax assessments?

Mr. WAYNE. I know there are a number of allegations it has made arbitrary tax assessments. That is part of the court cases going on in the country.

Mr. MENENDEZ. It seems to me we could take judicial notice of what a court, a Peruvian court, says against our own companies. We could take notice of when the entity in that country is subject to Peruvian law, when a court says that it makes arbitrary tax assessments, when courts advocate that they have violated tax agreements. Doesn't our Government say, your own courts take these positions? Do we have to hesitate about that?

Mr. WAYNE. No. We have gone back into the Executive Branch of Government and talked to them frankly about the decisions their courts have taken. From our Ambassador and our Trade Representative and many others, including myself, we have frankly raised that with that Government and said, there needs to be a more rapid due process that takes place here.

When we have talked to the Government officials, they have expressed support for that. The steps they have taken are steps in that direction.

But it is quite true that we do not have resolution of these several very important cases.

Mr. MENENDEZ. If we continue down this road—I think your answer to the Chairman's question, but I want to make sure—I think the quote that the Chairman was referring to in terms of the U.S. Trade Representative, is Peter Allgeier's quote, who made comments that the USTR understands that the inclusion of Peru may endanger the Andean Free Trade Agreement. I read those comments. But then I look at that juxtaposed to your comments which say that we indicated the Peruvian Government had recently resolved certain outstanding disputes with United States investors and had taken significant steps to resolve others when you announced the launch of the Andean free trade negotiations.

Which is the standard that is going to be decided? Is it the standard that they have made some progress and, therefore, we entered into a free trade agreement with them? Or is it the standard that your deputy representative put, that we may well create a problem for continuing the free trade agreement with Colombia if these things do not get resolved?

Ms. VARGO. I think these cases and this process is one that has evolved. At the point in time that the earlier comment was made, we were at a stage in the ATPA process. We were reviewing a snapshot of commitments that had been made at that time.

Our comment now, and I don't think there is a disconnect between those two, is reflecting that there has been a lack of progress during the intervening period, from our perspective; and that, from their point of view, if their interest is to successfully conclude an FTA and get it passed by our Congress, their window for producing a better record is rapidly shrinking.

Mr. MENENDEZ. Well, it seems to me we have been at this for quite some time. This is not just a snapshot of the moment; this is a continuum, and in that continuum we have seen the Peruvian

Government do just enough, just enough to keep you all on the line.

I want to say, I am a big advocate for Peru. I want to see our investment flow there, but I want it to be fair, transparent. We think that is important for Peru as much as it is for our companies.

One other question: PSEG, I understand they have filed an appeal regarding their case. Apparently SUNAT in its most recent action levied a $30 million tax assessment against PSEG based on a new set of tax rules.

SUNAT changes their rules so they can attach a $30 million assessment against a U.S. company. They have shown their intention to change the rules of the game midstream. What hope do you have for resolving processes like that?

Ms. VARGO. I would like to ask Bennett Harman to speak to that particular case, which I think involves the tax year 1999.

Before doing that, one comment I wanted to make: In fact, one of the areas of progress that we did see in Peru between the earlier announcement that you mentioned—when we announced going forward with the free trade agreement with them, and now—is the creation of a tax ombudsman and PSEG is one of the companies that has benefited from that.

The tax ombudsman did not allow SUNAT to go forward with an appeal. That was one evidence of some progress. But there is this one tax year outstanding.

Mr. HARMAN. It is 1999, the year still in contention. We understand PSEG, as you indicated, is appealing to the tax court. If this scenario plays out as it did with the other tax years, the tax court could uphold PSEG and the ombudsman could not allow an appeal to go forward. That hopefully would be the end of the road. We are not in any way defending the methodology used by SUNAT.

Mr. MENENDEZ. Mr. Chairman, I heard you make a comment that you have been in constant consultation with Members of Congress. Certainly this Ranking Member on this Committee has not had that privilege. I hope you will change the dynamics.

Secondly, a statement to all of you: I do not believe that enabling countries ultimately inures to their benefit or ours. I believe holding the rule of law, of transparency, of fairness in the process of international investments is in the interest of whatever country we are talking about, if it happens to be Peru and Ecuador right now, as well as the United States. But enabling countries and thinking that we are helping countries by enabling them is a huge mistake.

Thank you, Mr. Chairman.

Mr. BALLENGER. Mr. Weller.

Mr. WELLER. Thank you, Mr. Chairman. Let me welcome Ambassador Shapiro. I congratulate you on your new position and echo Mr. Delahunt's comments.

Ambassador Vargo, it is good to see you. Let me congratulate you on the good work that you and Ambassador Zoellick have been performing over the last several years, and breaking out trade barriers that stand in the way of Illinois farmers and manufacturers and being able to sell our products in markets overseas. I congratulate you on that and want to reinforce my commitment to work with you toward ratification of the Dominican and Central American FTA, which are good, fair, balanced agreements, as well as moving

forward on the Panamanian and this Andean trade agreement we have before us.

I think the message is pretty clear. As one of those who is working toward the enactment and ratification of free trade agreements that are good, fair, and balanced for all partners involved, issues like this can be a deciding factor on whether or not Congress will ratify any Andean Free Trade Agreement. I would like to see one ratified by Congress.

Many of my colleagues have pointed out the importance of fairness and transparency of law as being reflected in free trade agreements, as well as the treatment of investors in the countries involved. You noted in your testimony some progress has been made on resolving investors' disputes, but others have not been sufficient.

Can you lay out for us essentially how many disputes are outstanding? How many have been resolved in Ecuador and Peru? And frankly, what is standing in the way of Ecuador and Peru resolving the remaining disputes?

Ms. VARGO. I don't have the information quite set up that way, and to give you a complete listing, I would need to get back to you. I do not have the information set up that way.

I would say, both countries during the course of this process resolved some of the easier issues, particularly those under the jurisdiction of the Executive Branch. A number of other contentious issues were put into binding arbitration. From our perspective, that is a good course. That is what we try to do.

Let me just say in that regard, a more recent and troubling development in Ecuador has been whether or not a ruling on those binding arbitrations leads to an expeditious payment and outcome; and the follow-through is very, very important.

The most difficult cases have been those that are already within the court system and where there are a variety of options that different players in the Government have regarding whether or not they choose to pursue appeals and extend the cases. The lack of timeliness on these cases is extremely frustrating and costly and, I think, damaging to the reputations of the countries themselves as a good place to do business.

If I might comment for a moment to Congressman Menendez, I think that in the gold case, in particular, which I think is one right now that stands out, it was a good thing that last spring a Peruvian court ruled that there had been a violation of due process.

That ruling was appealed. The court is late in yielding its judgment on that appeal.

It is opinion, but I think that you can see the process turning; and so what we are looking forward to is hoping that the internal dynamics of the Peruvian institutions can actually move on that and yield a good outcome in that case.

I know that from Ecuador's side there are several disputes, and I would not want to minimize any of them, but the Occidental case stands out since they are the largest investor in Ecuador. And since they did win a binding arbitration, I think that there have been some cooler comments recently by the Solicitor General in that regard; and they do have an appeal in on a procedural technicality, but that should not take too long to rule on.

Mr. WELLER. Ambassador, we appreciate your offer to share with us essentially a status report on outstanding disputes. It would be helpful if your office can provide that.

[The information referred to follows:]

MATERIAL SUBMITTED BY REGINA K. VARGO, ASSISTANT U.S. TRADE REPRESENTATIVE FOR THE AMERICAS, AS REQUESTED DURING THE HEARING BY THE HONORABLE JERRY WELLER, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF ILLINOIS

Summary of ATPDEA Commercial Disputes in Peru
October 5, 2004

With the granting of ATPDEA benefits in September 2002, Peru committed to resolve nine commercial disputes. The Toledo administration made significant progress in early 2004, resolving some cases and setting forth agreed paths to resolution in others. To date, Peru has resolved two cases: 3M and Big 3 Marine. Two other disputes are on track to resolution: Northrop Grumman (in local arbitration) and Duke (in ICSID arbitration). Three disputes need further work: LeTourneau, Arcadis, and Luz del Sur. Disputes to be resolved within the judiciary are: Engelhard and Princeton Dover.

ATPDEA Cases Resolved

3M – In March 2004, the U.S. company obtained its zoning and operating permit, ending a six-year delay.

Big 3 Marine - A court ruling determined that the statute of limitations had expired in this case (the company did not file in time). There were no indications that the court departed from judicial norms.

ATPDEA Cases in Arbitration (on track for resolution)

Northrop Grumman – The GOP and U.S. company agreed to resolve their differences in arbitration, which began on June 1, 2004. A final outcome is expected before the end of the year, concluding a contractual dispute over a radar system purchased by Peru in 1996.

Duke Energy – The GOP and Duke submitted the company's tax case to arbitration in the World Bank's International Center for the Settlement of Investment Disputes (ICSID) in October 2003. Disappointed by an unfavorable Tax Court ruing in May 2004, Duke's local company in August 2004 paid a tax assessment to SUNAT to settle a disputed tax bill. Duke contends the tax was unjust, but decided to pay to prevent further accumulation of interest and penalties. Through ICSID arbitration, Duke seeks compensation for taxes it has paid in error. Duke indicates it had a tax stability agreement with the GOP that should have precluded such taxes.

Disputes Under Executive Purview

LeTourneau -- The GOP acknowledges it owes compensation, but the two parties have not been able to reach agreement on the compensation owed. In March 2004, the Toledo Administration established an ad hoc commission to make recommendations to the Peruvian Government about possible solutions. After several meetings between the commission and LeTourneau's attorney, the two sides remain far apart. There is disagreement on the 1971 value of the road and how to adjust that figure to 2004 values. The GOP is recommending that the two sides appoint independent appraisers to settle the dispute.

Arcadis -- The company and GOP in March 2004 agreed to bring the dispute to Peru's Controller General for a final determination. The Controller's report noted that the second contest was not closed and that the third bid process was invalid (bolstering Arcadis' claim). Furthermore, the report noted that Petroperu should clean up the environmental mess as quickly as possible. Without consulting the executive, Petroperu cancelled the second bid process, claiming that the Controller's report is ambiguous and it gave Petroperu the option to cancel the second bid and launch another contest. The GOP is analyzing how to reverse the decision taken by Petroperu.

Disputes in Judiciary/Tax Court

Engelhard – After a delay, a judge in May ruled in favor of Engelhard on its injunction. He concluded that Engelhard could not be held responsible for irregular actions by third parties and dismissed several resolutions against the U.S. company. Engelhard awaits a ruling by the Superior Court (the final step in the injunction) that could uphold the earlier ruling. There was a two-month strike among employees of the judiciary, which has delayed the Superior Court ruling.

There is a separate criminal case (against two local Engelhard executives) that is still in the investigative phase. In October 2000, a judge began a criminal proceeding that includes more than 250 individuals accused of defrauding the government.

Princeton Dover -- In May 2004, Princeton Dover filed an injunction challenging an earlier Tax Court decision. The Tax Court issued a resolution that deferred making a decision until the criminal trial against the company concluded. Princeton Dover argues that the Tax Court should issue a decision now, not wait.

Luz del Sur (PSEG and Sempra Energy) – The Executive limited SUNAT's ability to go to the Judiciary over Tax Court decisions with which SUNAT disagrees. An executive decree established the position of the Tax Ombudsman, and it is now requires that before SUNAT can appeal a Tax Court ruling to the judiciary, the Tax Ombudsman and Finance Minister must first give their permission. Without this permission, the Tax Court ruling is final. On April 8, 2004, the Finance Ministry appointed its new Tax Ombudsman. The Tax Ombudsman on April 21 disallowed a request by SUNAT to appeal a January 2004 Tax Court ruling that was favorable to Luz del Sur.

A January Tax Court ruling that was generally favorable to Luz del Sur, allowed SUNAT to challenge the company's valuation of assets used for its depreciation allowance. After several months of delay, SUNAT on September 16, 2004 issued a resolution that disallowed part of LDS's asset revaluation. LDS is in the process of appealing this ruling to the Tax Court.

Mr. WELLER. Mr. Secretary, can you add to that? Specifically, can you identify what you see as the biggest roadblock to fair and transparent and expeditious resolution of these investors' disputes in Ecuador and Peru?

Mr. WAYNE. I can give a thumbnail sketch on the status of the various cases.

We did our initial review. There was a problem with the 3M Company, which has been solved, in Lima. There was a problem with a company, Big Three Marine, where the Peruvian courts determined that the statute of limitations for their complaint had run out. The Big Three Marine is appealing that to the Supreme Court.

There are several cases in arbitration or proceeding in that direction, including a dispute with Northrop Grumman and with Duke Energy. There are two issues, two other cases with Le Tourneau and Arcadis. There has been serious engagement, but there are still differences between the company and the Executive Branch of the Government. In one case, they are looking to find a neutral appraiser to come up with the value of the property under dispute. In the other case, there was a Government meeting to sort out and find a way forward.

Then there are the three cases in the judiciary: The Engelhard case, a Princeton Dover case, and the PSEG energy case.

In the case of Ecuador, we had—the primary commercial case that we cited was, in fact, Occidental Petroleum going to arbitration over what they felt was an unfair value-added taxation by the Government of Ecuador. The arbitral panel found in their favor. This was an arbitral panel that took place in the United Kingdom under an agreed process with our bilateral investment treaty. The Government of Ecuador had the right to appeal that in England, and they have done that. That is the appeal process that Ms. Vargo was referring to.

There are also two commercial issues with IBM and the company TMAS. Those have been solved. There were also a number of conditions related to a labor dispute and child labor. There have been a number of steps and progress in both of those disputes as we have gone forward.

Mr. WELLER. Thank you.

Mr. Chairman, I have one last question, and I will attempt to be quick. I appreciate that.

Ambassador Vargo, in our trade agreements we ask our partners to make commitments, as we do to them, and to honor those commitments. Can you review, as part of the Andean Trade Preference Act, the commitments that Ecuador and Peru committed to? And what is the status of their commitment? Have they honored all of those commitments to this day?

Ms. VARGO. Mr. Weller, I would like to get back to you with that information as opposed to reciting it here.

I would say at this point some of the commitments have been fulfilled. Some have been fulfilled—although there is no outcome yet—by a move to binding arbitration. As long as the outcome of the binding arbitration is honored when the process is complete, we would consider those fulfilled.

And, again, in the cases for which commitments that were made regarding the cases that were in the courts, clearly, the process has not been as expeditious as we would like to have seen.

Mr. WELLER. Secretary Wayne, can you add anything?

Mr. WAYNE. We have been in the process of inviting comment for this year on the ATPA process. We are hearing from the private sector and others on a range of issues that went forward.

In the investor sector, the problems that I mentioned were the main ones. There were also some commitments that were discussed, and as Ms. Vargo has said, a lot have not yet come to conclusion.

We may hear some new issues raised in this process. USTR will be managing this process.

Ms. VARGO. The period just closed, we are compiling the number of issues that are out there. The broadest range of new issues would seem to be with relationship to new issues with Ecuador.

Mr. WELLER. Ambassador, you said some of the commitments have been fully honored. Do you have a glaring example of one that was not honored, of a commitment made by Ecuador or Peru in ATPA?

Ms. VARGO. As I said, some of the cases are still evolving, proceeding through the courts, etcetera. To the extent that has not been as expeditious as we would have liked, that is a disappointment. But I cannot think of a commitment made that was clearly violated.

I would just follow up on Assistant Secretary Wayne's comment to note that we focused on investment disputes, but there were a number of other commitments made, some relating to intellectual property, software legalization, great deterrence for piracy violations, and very significantly in Ecuador with respect to some workers' rights issues where they have taken a series of important steps. Again, the workers' rights issue is one that we are going to be working on with Ecuador for quite some time.

But we asked for some concrete steps to be made, and they were. The remaining investor disputes are not the total tale. There has been a lot of good work accomplished. Nonetheless, what we are really looking at here is, these are not small disputes. These are large disputes and there is a significant enough number of them to be very troubling. So they continue to be at the forefront of our discussions.

Just let me note while we do not negotiate these in a free trade agreement, each of the rounds that we have been having has provided us with an opportunity to again meet with both our colleagues in the Embassy and our counterparts in the other Governments to stress the importance of these cases and review the progress of what has happened or not happened in the intervening period.

Mr. WELLER. The comment period on the ATPA is what period of time?

Ms. VARGO. It is actually closed now, I believe. It closed September 15.

Mr. WELLER. It is now concluded. Thank you.

Mr. BALLENGER. Congressman Delahunt.

Mr. DELAHUNT. Thank you, Mr. Chairman.

I think you just indicated, Ambassador Vargo, there is a disconnect obviously between negotiations relative to FTA and these individual disputes.

Am I being fair in my characterization?

Ms. VARGO. If that is what I said, what I intended to say was that the agreement itself will not make reference to specific cases and say, with respect to this case, this is what happened.

Mr. DELAHUNT. I understand that.

My point is, I think these cases, at least to this particular Member, are evidence of the capacity and the ability of these nations to enforce the appropriate provisions of an agreement.

I don't know if I speak for my colleagues, but why an agreement if the enforcement of those provisions is respected in the breach? There is a maxim that is old, but true, about justice delayed is justice denied. There has to be some finality.

You speak of progress and steps going in the right direction, but let me suggest, those are real baby steps. You and Secretary Wayne have expressed concern about the end result; even if a binding arbitration award should be issued, whether it is going to be respected. I am not particularly optimistic, given what I hear here today.

Correct me if I'm wrong. It would appear that the judiciary—particularly in Peru, but presumably also in Ecuador—seems to be playing its role and issuing decisions, but there is a relationship between the judiciary and the Executive Branch which is unknown to our democratic experience that supersedes, if you will, the judicial decisions or delays enforcement of them.

Mr. WAYNE. Let me take the first crack at that, and then ask Ambassador Shapiro to add.

There is no question that the judiciaries in both of these countries are in need of being strengthened and are strengthening themselves. In Peru, there is a great backlog of criminal and civil cases. The system is generally recognized as not working as well as it should. That is one reason they just established that we need to create some commercial courts, because we need faster resolution for the sake of business cases that come up.

The courts, I would say, given that delay—and, for example, in the Engelhard case we are waiting for a court ruling. It is beyond the normal period of time, but they just had a 2-month strike by court employees in Peru beyond that delay problem. They do seem to have been rendering judgments, but part of the challenge is the tax authority has found ways to challenge those judgments, and that has been part of the frustrating series of events we have all faced.

Mr. DELAHUNT. Mr. Secretary, you have indicated it would appear this is a nondiscriminatory operation of their institutions. In other words, American companies are not being singled out, that this is universal, presumably, in their relationship with other foreign nations. Did I understand you correctly?

Mr. WAYNE. My understanding is that this is not discriminatory, that Peruvian companies and international companies have faced the same kind of thing.

Mr. DELAHUNT. So we are talking about a real, structural problem, a problem of governance, if you will. I guess this goes back to

conversations and discussions that Members have had about the need to strengthen institutions in the Hemisphere so that they are truly democratic institutions. And let me pose the question to Ambassador Shapiro, or to you, Mr. Wayne, or to anyone. What are we doing in terms of providing assistance as far as democratic governance is concerned to strengthen these institutions so that at least we can consider whether we should entertain such agreements as FTA?

Mr. WAYNE. I do know that in both Ecuador and Peru there are very sizable USAID programs, a good portion of which are aimed at governance and improving governance.

I also know that Peru has itself instituted nationwide governance-improving programs, and they have the World Bank, the Inter-American Development Bank and others helping.

Mr. DELAHUNT. Are you satisfied with the level of improvement that you have seen? Are we getting any bang for our buck? Obviously, this transcends just commercial relationships.

Mr. SHAPIRO. Let me answer that. What we want in our commercial disputes, whether they are in these countries or elsewhere, is fair, prompt, and transparent resolution of disputes. We are working through AID with judicial systems in Ecuador and Peru. Working with other than Executive Branches is very difficult in terms of measuring the results.

What you have got in all of these countries, if I am not mistaken, is the tax authority is semi-independent. In Ecuador, the Solicitor General is autonomous; he is elected by the Congress and cannot be removed. So as you work with these organizations, these entities, it becomes much more difficult; and our goal is to achieve fair, prompt, and transparent resolution of our commercial disputes here and elsewhere.

Mr. DELAHUNT. Since you are developing a litany of cases in dispute, I would ask you—and this is obviously not part of the ATPA, but given the criticism that has been leveled at the Venezuelan Government, I would like to see for my own purposes a list of cases that are in dispute with the Venezuelan Government so we can make a contrast and comparison.

There has been a lot of criticism being leveled at the Government in Venezuela, but it would appear to me that the problems in Venezuela, certainly in my experience, do not amount in terms of magnitude to what is occurring in Ecuador and Peru.

With that, I would yield for a moment, Mr. Chairman, to my Ranking Member, Mr. Menendez.

Mr. MENENDEZ. I just want to follow up, Mr. Secretary. I want to make sure I understand what you are saying.

Are you saying that Peruvian companies face the same, the exact issues as international companies, like some that we have been talking about such as Engelhard, with $30 million of their assets taken?

Can you give me examples of Peruvian companies that are facing those types of actions?

Mr. WAYNE. Mr. Menendez, thank you for your question. What I was trying to say, I am not going to say the same scope of problems, but my understanding from our Embassy is that the same type of problems—the type of delay, the type of difficulty in dealing

with the tax system—is faced probably, in my judgment. And what I said was I didn't think U.S. companies were being singled out. I would have to go back and get you more detail because I honestly don't have that, but I would be happy to do that for your, sir.

Mr. MENENDEZ. I would like to have that. I would like to have the comparative nature of what is happening to United States and other international companies investing in Peru versus what is happening to Peruvian companies within Peru in terms of both SUNAT and the legal system and everything. I thank the gentleman.

[The information referred to follows:]

RESPONSE SUBMITTED IN WRITING BY THE HONORABLE EARL ANTHONY WAYNE, ASSISTANT SECRETARY, BUREAU OF ECONOMIC AND BUSINESS AFFAIRS TO QUESTION ASKED DURING THE HEARING BY THE HONORABLE ROBERT MENENDEZ, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF NEW JERSEY

Question:

I would like to have the comparative nature of what is happening to U.S. and other international companies investing in Peru versus what is happening to Peruvian companies within Peru in terms of both SUNAT and the legal system.

Response:

Generally, corporate tax rates are applied evenly to foreign and domestic investors alike, but there are exceptions to this rule. One of the most notable of these concerns is the government's policy of negotiating tax stability agreements with U.S. and other foreign investors. These agreements serve the purpose of creating incentives for investors in the form of low tax rates, which are intended to remain constant for a period of up to ten years. Attracted to the possibility of a stable, relatively enticing tax structure, a number of international businesses have made significant investments in Peru, but these advantages are not typically available to Peruvian firms already operating in the country. In this sense, tax stability agreements tend to discriminate in favor of American and other foreign investors, as they provide preferential treatment to foreign investors that is not available to domestic ones.

Ironically, it is from these very preferential arrangements that many of the most significant problems for U.S. and other foreign investors emerge. While SUNAT appears to abide by the tax rates negotiated in these contracts, the tax agency has recently created other problems by reassessing the underlying value of the assets of some of these foreign investors. These reassessments have affected not only American investors like PSEG, but also a number of other foreign businesses that had negotiated tax stability agreements with SUNAT. According to Eric Farnsworth of the Council of the Americas, multiple European and South American investors are embroiled in disputes with SUNAT that are very similar to the problems facing U.S. companies in Peru.

As Peruvian businesses are generally unable to negotiate tax stability agreements, they do not typically encounter these types of problems. Still, many businesses which are wholly, majority or partly Peruvian owned currently face tax claims by SUNAT leading to hotly contested disputes not dissimilar to those faced by international investors.

Legal backlogs, however, affect both foreigners and locals alike. The Peruvian court system is chronically logjammed and underfunded and both criminal and civil cases can linger for months, if not years.

Mr. WAYNE. I would also add, if I could, Congressman Delahunt, that each year we have due to you a report called the Section 527 Report, which is a report on expropriation cases and other investment disputes. And just yesterday this year's report was delivered, and it treats every country in the world where we have reports of investment disputes. And so we certainly would be happy to——

Mr. DELAHUNT. If you could just extract from that the three, the Andean countries including Venezuela, I would be interested in that.

[The information referred to follows:]

INFORMATION SUBMITTED IN WRITING FROM THE HONORABLE EARL ANTHONY WAYNE, ASSISTANT SECRETARY, BUREAU OF ECONOMIC AND BUSINESS AFFAIRS BY REQUEST OF THE HONORABLE WILLIAM D. DELAHUNT, A REPRESENTATIVE IN CONGRESS FROM THE COMMONWEALTH OF MASSACHUSETTS

Following are the extracted sections from the 2004 Report on U.S. Citizen Expropriation Claims and Certain Other Investment Disputes dealing with Peru, Ecuador and Venezuela. Section (a) provides an alphabetical designation instead of the claimant's name, to avoid privacy concerns. Section (b) states the year that the claim arose, as well as it can be determined. In general the date provided by the Department represents the earliest date that the foreign government denied the claimant beneficial use of, or control over, the property, or formally expropriated the property under its domestic laws. Section (c) contains basic information on the claim, including its status and recent efforts with respect to the claim made by the U.S. Government. Section (c) also describes action by the relevant country to attempt to resolve the claim.

Please note that the information below is not intended for public dissemination, as its release to the public could have consequences related to the Privacy Act.

For more information related to the information below, including the Report's introduction, please refer to the complete Section 527 Report, which was delivered to the U.S. Congress in October 2004.

ECUADOR

The United States Government is aware of ten (10) claims of United States persons that may be outstanding against the Government of Ecuador (GOE). One of the six claims is reportedly resolved and another claim is in international arbitration.

1. a. Claimants A and B

   b. 1978

   c. The Claimants are investors in Tababuela Industrial Azucarera, C.A. (TAINA), a sugar mill and cane farm project originally covering 5,280 hectares near Ibarra in Imbabura province. The Embassy is not aware of a recent appraisal of the property, but in 1978 the Ecuadorian Social Security Special Court appraised the project at $6.39 million.

   The Claimants and their Canadian partners bought the sugar project from the Instituto Ecuatoriano de Seguridad Social (LESS) in 1966. LESS issued a $5 million mortgage on the property. By 1973, production costs were exceeding revenues and TAINA fell behind on its mortgage payments to LESS. By 1974, the debt amounted to $12.5 million. In 1978, LESS sued to collect back mortgage payments and unpaid pension premiums.

   Claimants A and B assert that the GOE's actions in response to TAINA's situation amount to expropriation without compensation. The GOE claims the case is one of a complicated bankruptcy and that TAINA had no assets to expropriate.

   The Superior Court of Ibarra has subsequently ruled against the Claimants.

   TAINA is now being sued by IANCEM (Ingenio Azucarero del Norte), a sugar company whose property holdings encompass the disputed land. LESS is 40% owner of IANCEM, as a result of the fact that LESS contributed 40% of IANCEM's property, of which 100% is the disputed land. Claimants allege that the lead counsel representing IANCEM has ties within the court system and that he is using his ties to try to win favor in the current proceedings.

   Department and Embassy officials have met with representatives of the Claimants several times. Department and Embassy officials (including the U.S. Ambassador) have also urged resolution of the case in letters to and meetings with GOE officials. In a communication with the Embassy in June 2003, TAINA's attorney expressed concern about the elevated levels of political pressure surrounding the current case against the Claimants.

   Embassy spoke with the Claimants lawyer in June 2004. According to the lawyer, the Supreme Court sent the case to the City of Ibarra Court where the sugar cane operation is located. The Ibarra Court has asked the LESS for additional information, which has not been provided, further delaying resolution of the case.

2. a. Claimant C, (Resolved).

   b. 1989

c. In 1989, the Quito municipality declared that an area of privately owned woodland near the city would be set aside as a city park. This area included 11 hectares of Claimant C's land. Estimates of the value of the land range from $66,000 to over $1 million. Claimant C had intended to build a hotel on this land and argues that compensation below the land's potential commercial value would constitute government expropriation. The municipality has offered to swap city land in the expensive "El Bosque" section of Quito for Claimant C's land in the proposed park.

U.S. Embassy representatives discussed Claimant C's claim with the Mayor of Quito, and State Department officials urged the Government to consider ways to resolve the claim. Negotiations between the owner and the municipality produced a partial solution. Claimant C settled the case with the municipality for $100,000 in 1994. Claimant C considers the case closed and remains concerned only with the TAINA dispute.

3. a. Claimant D

b. 1974

c. This dispute arose out of the 1974 sale of a portion of Claimant D's property (approximately 281.9 hectares) to a private Ecuadorian citizen. The purchaser's checks did not clear, but the Ecuadorian citizen occupied and, eventually, sold the land. To avoid repossession of the land, the occupants turned to the Ecuadorian Agrarian Reform and Colonization Institute (IERAC). In 1985, IERAC recognized the occupation, but maintained the immunity of Claimant D's property from expropriation. Then in 1990, IERAC revoked the immunity and transferred the disputed portion of land to the state without compensation to Claimant D.

In December 1991, Claimant D asked the Ecuadorian civil court to evict the occupants from the land. In October 2002, the court decided in Claimant D's favor, but the judgment was not enforced. In February 1992, the occupants requested that IERAC grant them title to the land. Despite the fact that the pending civil suit legally took the case out of IERAC's jurisdiction, IERAC awarded the title based on the Ecuadorian principle of abandonment, under which Claimant D was not entitled to compensation.

In March 1993, the National Administrative Development Secretariat ruled Claimant D as the legal owner and declared that IERAC had no jurisdiction to rule on the case. Nevertheless, in July 1993, IERAC's Regional Appeals Committee No. 2 upheld IERAC's prior award granting title to the occupants. Thus, by July 1993 there were inconsistent civil and administrative rulings concerning the title to the disputed 281.9 hectares.

As of the mid-1990s, there were no other layers of review available within IERAC. Additionally, there is some question whether Ecuadorian law will allow a reversal of the title granted by IERAC. Claimant D estimates the value of the property to be approximately $845,000; Ecuadorian government records suggest a value of about $17,000.

This case was first brought to the attention of the State Department in 1993. In 1994, the United States sent a diplomatic note suggesting that the GOE consider special legislation to compensate Claimant D. In August 1995, U.S. Embassy officials visited Claimant D's farm and discussed possible solutions to the claim. Embassy and State Department officials continued to raise the case with GOE officials in 1996 and 1997.

The Embassy continues to monitor this claim and has spoken with Claimant D on several occasions over the past few years. However, the case has not been raised with the GOE since late 1997.

The Claimant has contacted the Department of State and Embassy on a number of occasions. In December 2003, the Department of State requested that the Claimant provide additional information and further clarify her claim. In June 2004, the Ministry of Agriculture sent a letter to the Claimant seeking additional information to resolve the case. The Department recently received from Claimant D more information on her claim, but that information further confuses, rather than clarifying, the claim. The Department is working to understand the facts as alleged by Claimant D.

4. a. Claimant D (separate but related to the previous claim).

b. 1994

c. The CEDEGE, a state water management agency, determined that a portion of land (approximately 100 hectares) held by Claimant D would be condemned as part of a World Bank flood control project. CEDEGE and Claimant D disagreed over the number of hectares that would be affected by the project and

the value of the land per hectare. Claimant D alleges that CEDEGE workers have caused extensive damage to her property and that she is receiving less favorable treatment than Ecuadorian landowners affected by the CEDEGE project.

In 1997, the Embassy's Economic Officer spoke with CEDEGE's Executive Director, who indicated that Claimant D was actually receiving more (not less) compensation than her Ecuadorian neighbors did.

In 1995 and December 1997, Embassy officials visited Claimant D's farm, inspected the water damage done to the farm, and discussed possible solutions to her claim. With Embassy mediation, an apparent solution was reached in December 1997, but there is indication that Claimant D never collected the compensation check from CEDEGE.

The Embassy has spoken with Claimant D on several occasions over the past few years and continues to monitor the situation. State Department lawyers have also continued to correspond with Claimant D, most recently in December 2003. In April 2004, the claimant wrote that her "property continues to be invaded." One police report, dated April 2, 2003, concluded that there was no evidence of an armed group threatening the claimant's family or property. The Department is working to better understand this claim.

5. a. Claimant E (Resolved)

b. 1996

c. In 1995, Claimant E, a U.S. corporation, signed a contract to supply electric generating capacity to the GOE through INECEL, the Ecuadorian national power company. Claimant E invested nearly $40 million to install two power generation plants under the contract. The plants were inaugurated in 1996. Shortly thereafter, a dispute arose under the contract, including non-payment by INECEL of $20 million due to Claimant E. Due to an inability to renegotiate a contract acceptable to the GOE, Claimant E sold the power plants in 1997 at a large loss.

In July 1996, Claimant E initiated civil litigation in Ecuador against INECEL. Claimant E sought the GOE's agreement to arbitrate the claims, and in multiple meetings and letters, the Embassy has urged the GOE to resolve this case either through direct negotiations or international arbitration. Ecuador's Attorney General refused to arbitrate on the basis that the company no longer has legal status in the country and had removed all relevant legal papers from Ecuador. The Ecuadorian courts have also declared Claimant E's initial civil court case as "null and void."

The two corporations that own Claimant E are now pursuing international arbitration. In April 2003, they filed for arbitration under the rules of the International Center for the Settlement of Investment Disputes (ICSID), pursuant to the US-Ecuadorian Bilateral Investment Treaty.

Embassy staff spoke with the Ecuadorian lawyers representing Claimant E in April 2004. At that time, the international arbitration case was still pending before ICSID.

6. a. Claimants F and G

b. 2000

c. In April 2000, Claimant F, the U.S. citizen trustee of a Bahamian trust requested U.S. Government assistance in the Trust's dispute with the GOE over ownership and management of a U.S.-registered electric company located in Guayaquil, Ecuador. In February 2000, the Ecuadorian owner of the company transferred 100% of the company's shares into Claimant F's trust. In March 2000, the GOE " took over the company as part of a larger liquidation. Claimant F claimed that the seizure was tantamount to an expropriation of US-owned property.

Claimant F has been replaced by Claimant G as trustee of the trust in question. In June 2003, the former Ecuadorian owner of the company created a rival Bahamian trust in an effort to seize control of the utility from the original trust. The rival Bahamian trust intends to contest the 2000 trust transfer, claiming it led to the expropriation of the company.

Lawyers for the rival Bahamian trust told Embassy officials in July 2004 that they would seek relief through arbitration in the United States or through Ecuadorian or Bahamian courts. In a meeting with Embassy officials in June 2004, Claimant G said that Claimant F no longer has any legal interest in the trust and that Claimant G is trying to remove himself from the trust. He claims the only assets left in the trust are the claims and counterclaims against the GOE. According to Claimant G, all other assets and liabilities of the Bahamian

trust have been transferred to a private Ecuadorian trust to conduct the day-today operations of the electric company. Claimant G has not solicited USG intervention in the case and told Embassy officials.

The U.S. government has not taken a position on the merits of Claimant F's (now G's) expropriation charge. However, high-level Department of State and Embassy officials have raised this case numerous times with high-level GOE officials, including the President. U.S. government representatives have urged the GOE to work with all the parties to this dispute to reach a resolution of the ownership dispute.

7. a. Claimant H

b. 1993

c. In 1993 private parties filed a lawsuit against Claimant H in U.S. Federal Court alleging that one of its subsidiaries was responsible for environmental damage in Ecuador. As a condition of the dismissal of a suit in the United States, Claimant H agreed to appear in Ecuadorian Courts. In 2003, a private lawsuit was filed against Claimant H in Ecuador. The plaintiffs seek over a billion dollars in compensation for alleged environmental damages. Claimant H is defending the case on several grounds, including that it remediated any environmental damage it caused and that it received a release from the GOE from any further liability for environmental damage. State-owned oil company Petroecuador, the majority shareholder in those operations, has failed to meet its environmental remediation obligations. Claimant H has asked the GOE to honor the release provisions of the remediation agreement signed by Claimant H's subsidiary and Petroecuador. In addition, Claimant H has requested arbitration in New York under the terms of the operation agreement its subsidiary had with the then-existing state-owned oil company. The GOE has not acknowledged in the Ecuadorian court the release given in the remediation agreement with Claimant H and has resisted the New York arbitration claim.

8. a. Claimant I

b. 2004

c. Claimant I has had a number of investment disputes with GOE entities. One of the most serious disputes concerns GOE regulator attempts to collect a fee for each cellular telephone antennae. Claimant I and other cellular phone companies in Ecuador contest the fee. The regulator sought permission from the Procuraduria General (Solicitor or Attorney General equivalent) to take Claimant I to arbitration on the matter. The Procuraduria issued an opinion stating that the regulator could take Claimant I to arbitration, but added that the regulator would lose the arbitration. The regulator proceeded with the arbitration against Claimant I and lost. The current Procurador General claims he was obligated under Ecuadorian law to appeal the arbitration on procedural grounds, despite his predecessor's previous legal opinion that the GOE should have lost the case on legal grounds. The amount in dispute exceeds $ 8 million. Over six months ago, both the Procurador General and Ecuador's Minister of Trade promised the USTR verbally that the matter would be resolved within thirty days.

9. a. Claimant J

b. 2004

c. In July 2004, Claimant J won an international arbitration award against the GOE for value-added-tax (VAT) rebates amounting to $75 million through December 2003. At the time of the announcement of the award, Ecuador's Procurador General Jose Maria Borja announced he would review all foreign oil company contracts with the GOE, beginning with Claimant J and followed by a Canadian oil company that has its own VAT international arbitration case against the GOE. Several weeks later, the GOE announced to the press that Claimant J had violated Ecuador's hydrocarbon law in 34 instances. The most serious allegation is that Claimant J transferred 40% of its interests in oil block 15 to the Canadian company without the statutorily required prior authorization of the Minister of Energy. As a result of those alleged violations, the Procurador claims Claimant J's contract with the GOE should be declared void and all of Claimant J's Block 15 operations and assets should be transferred to state-owned oil company Petroecuador without compensation. Claimant J vehemently denies that the transfer to the Canadian company has been completed and notes that the contract between it and the Canadian company expressly states that the transfer cannot be made until authorization is given by the Minister of Energy. Claimant J asserts that it has either paid fines or legally chal-

lenged the other alleged violations and that, in any event, the Procurador's demand to cancel the contract and give its assets to Petroecuador is disproportionate to the alleged offenses and tantamount to GOE expropriation of its assets.

10. a. Claimant K

b. 2004

c. In 2004, the GOE, in an effort to reduce electrical costs to end users, subsidized diesel fuel for thermoelectric producers. As a result of this subsidy, inefficient thermoelectric producers have leap-frogged more efficient gas turbine electric producers like Claimants K in supplying power to the electrical grid. Thus, Claimants K has not provided the amount of electricity it would have normally provided to the grid had the subsidy not been in effect. The contract between Claimant K and the GOE states that if the economic conditions of the contract change, the contract must be accordingly adjusted. Despite requests from Claimant K, the contract has not been adjusted. In August 2004, Claimant K gave the GOE the six-month notice under the US-Ecuador Bilateral Investment Treaty (BIT), indicating its intention to seek international arbitration under the BIT. Claimant K has also claimed that is has been discriminated against in the payments owed by various GOE entities.

11. a. Claimant L

b. 1990s

c. Claimant L has had ongoing investment disputes with the GOE for several years. A number of those disputes were resolved as a result of the added attention of the ATPDEA review process. Negotiations have failed to resolve the one remaining dispute and Claimant L has commenced arbitration proceedings in that case.

PERU

The U.S. Government is aware of thirteen (13) claims which may be outstanding against the Government of Peru (GOP).

1. a. Claimant A

b. 1999

c. Claimant's Peruvian subsidiary was a major purchaser of Peruvian gold in the late 1990's. In 1999, the GOP issued a decree that made the final purchaser of gold responsible for verifying the legality of the supply chain from mine to export in order to receive the refunds of value-added tax (VAT) allowed under law. On the basis of this decree, applied retroactively, and in the context of a broader investigation into the loss of up to $150 million, the GOP tax authority, SUNAT, charged that claimant's subsidiary had participated in a scheme to defraud the GOP by falsifying gold purchases. SUNAT failed to refund VAT payments and, in December 1999, executed letters of guarantee worth a combined US $28 million put up by Claimant to secure early payment of the refunds. Claimant denied the accusations and filed an administrative appeal, which was later appealed to Peru's tax court. Subsequently, the GOP filed criminal charges against executives of claimant's Peruvian subsidiary.

On February 4, 2003, the tax court ruled against claimant, upholding SUNAT's resolution to withhold the US $28 million amount. The tax court ruling did not cite any direct evidence of specific misdeeds by claimant. However, the GOP contends that transactions within claimant's gold supply chain were simulated and that the company was in a position to know of the irregularities and wrongdoings of suppliers.

Claimant asserts that GOP corruption caused the execution of the letters of credit and the filing of criminal charges. Claimant argues that it should not be liable for any possible wrongdoing by its gold suppliers.

The judge in claimant's tax case issued a decision in May 2004 that threw out previous SUNAT and Tax Court rulings against the company. The court found that claimant cannot be held responsible for the irregular actions of third parties and that the GOP improperly seized the company's letters of credit in 1999. The GOP has appealed this decision. The Superior Court, which will hear the appeal, will have 20 working days to rule after receiving the case (however, this deadline will likely slip per common practice in Peru's courts). In the criminal case involving claimant's executives (lumped together with more than 200 other defendants), the government prosecutor requested that the judge extend

the period to investigate the case (adding 60 more days on to an investigative stage that has lingered for 3.5 years).

At Claimant's request, Embassy has engaged repeatedly with senior GOP officials since 1999 regarding this case. In exchange for trade benefits under the Andean Trade Preferences and Drug Eradication Act (ATPDEA), the GOP committed in September 2002 to promote prompt and effective due process and transparency under the law in Claimant's case.

2. a. Claimant B

b. 1999

c. Similar to Claimant A, Claimant B is involved in a dispute with the GOP regarding the refund of value-added tax on gold exported from Peru between May 1997 and February 1999. SUNAT, the tax agency, has withheld roughly US $600,000 that claimant contends it is entitled to receive as a tax refund. The Tax Court issued a decision in Claimant's case to wait until a parallel criminal case against Claimant's local general manager is resolved. The company has appealed this decision, arguing that the Tax Court had all the necessary information to make a ruling and that such a position creates undue delay. Claimant's criminal case is the same one that involves Claimant A's executives, which has not advanced in 3.5 years.

In the September 2002 ATPDEA commitment letter, the GOP pledged to resolve this case promptly, ensuring due process and transparency. In communications with GOP officials, USTR has set progress in the resolution of this dispute as a key factor that will determine whether Peru is included in the potential free trade agreement (FTA) that is sent to Congress.

3. a. Claimant C

b. 1989

c. Peru's Supreme Court ruled in December 1989 that ships belonging to Claimant had been illegally seized by Peruvian Customs in 1985, and that Claimant is due financial compensation. However, the amount of that compensation is now the subject of a series of court actions involving the Ministry of Economy and Finance (MEF). MEF contested the legality of Claimant's claim, stating that the statute of limitations had expired. The court ruled on March 12, 2004, against the company on the statute of limitations issue. Claimant has appealed this decision to the Superior Court, which was scheduled to start hearing the case by August 2004. An independent legal analysis requested by the Embassy suggested that the lower court ruling was within the bounds of Peruvian law.

4. a. Claimant D

b. 2001

c. Peru's telecommunications agency, OSIPTEL, sponsored competitive bidding for a subsidized, rural telephone network contract in September 2000. Foreign bidders were required to form a consortium with a Peruvian partner. On September 28, 2000, OSIPTEL announced that Claimant and its Peruvian partner had submitted the lowest bid (about US $27.8 million) for a subsidy. The bid submitted by Claimant D and its partner was approximately US $10 million less than the second-place bid. OSIPTEL issued an official resolution (a "Buena Pro") declaring Claimant D's consortium to be the winner.

To finalize the contract, Claimant D's partner was required to obtain a concession from the GOP, which the Claimant alleges should have been automatic. The GOP refused to do so, citing indictments against the owners of the Peruvian partner firm. The GOP awarded the concession to the second-place bidder in 2001, allowing the second-place firm to reduce its bid by US $10 million to match claimant's bid. Claimant D alleged that the decision to award the concession to the second-place bidder was prompted by that bidder's close contacts with former senior GOP officials. Claimant alleged that the GOP violated several of Peru's own laws and regulations.

Working on the basis of guidance from the Department, Embassy officers engaged actively with GOP officials to encourage the GOP to investigate the claimant's allegations and to consider an out-of-court settlement. However, no settlement was reached and the loss of the concessionary award still stands. Claimant D informed the Embassy that it has decided not to pursue further action. The GOP maintains that claimant does not have any impediment to participate in future international tenders to supply rural telephony.

5. a. Claimant E

b. 1996

c. This case was resolved in 2004. Claimant E constructed a $2.8 million facility in the municipality of Lima in 1996. Although the company complied with all municipal regulations and received all necessary permits, the city of Lima refused for several years to finalize the permitting and registration process for the facility.

As one of its ATPDEA commitments to the USG, the GOP pledged in September 2002 to "ensure that a final operating permit will be issued to (Claimant) not later than December 31, 2002." Senior USG officials, in Washington and during visits to Peru, repeatedly urged the GOP to push for resolution in this case. The Municipality of Lima issued final land-use approvals in 2004.

6. a. Claimant F

b. 2002

c. In 1997, the Ministry of Transportation procured a radar system from claimant under a turnkey contract. The system became operational in 1998 and, in July 2002, claimant sought to close out the contract based upon a satisfactory evaluation of the radar, as mandated by the agreement. The GOP refused to close the contract, arguing that the system did not function properly and that Claimant had not fulfilled its obligations. In a possible breach of contract, the GOP ordered its bank to collect from a US $6 million performance bond posted by Claimant before negotiations to settle this dispute could begin. That bond drawdown order was stopped by a temporary injunction granted by a New York court in August 2002.

Claimant and the GOP reached agreement in April 2004 on rules for submitting this dispute to local arbitration in Peru. The parties initiated the arbitration procedures on June 1, 2004. This process must be complete within 120 working days (in November 2004). Embassy and Washington officials have continuously urged the GOP at the highest levels to resolve this case.

7. a. Claimant G

b. 1999

c. In October 1999, the GOP's environmental authority, INRENA, obtained an emergency decree halting the movement of logging equipment and lumber in several of Peru's jungle provinces. INRENA shut down a logging operation in which claimant had invested $2 million and seized lumber intended for export to Claimant. The GOP alleged that the Peruvian company was engaged in illegal logging. Claimant denied the charges, asserting that the GOP's actions were intended to put Claimant's partner out of business. Claimant and its Peruvian partner have waged a legal battle in Peru against INRENA since then. Claimant has not sought Embassy assistance since 2002.

8. a. Claimant H

b. 1970

c. Claimant signed an agreement with the GOP in 1953 to build roads in rural Peru in exchange for one million acres of land. Claimant began developing a first installment of 60,000 hectares, but a military government expropriated the land in the 1960s. Claimant filed suit. In 1971, the Peruvian Supreme Court ruled that the GOP had to pay the Claimant for the roads he had built.

In its September 2002 ATPDEA commitment letter, the GOP noted that the judiciary had recognized Claimant's right to indemnity for the road construction, the value of which needed to be determined through further proceedings. The GOP further pledged to "ensure a transparent and prompt resolution."

The GOP issued in March 2004 a supreme decree establishing a special commission to negotiate a settlement with Claimant. The commission and Claimant's attorneys have met three times in Lima. The two sides reached agreement on most of the costs associated with construction of the highway in 1968 Peruvian currency. Substantial differences exist in each side's proposals for updating these costs to 2004. Claimant submitted a proposal that accounted for inflation and interest between 1971 and 2004. Applying this methodology and factoring in some discounts, Claimant came up with a substantial figure of around $200 million. In contrast, the GOP's initial offer totaled $6 million. The talks between the commission and Claimant have stalled and the GOP is seeking to extend a previously agreed upon deadline for ending the commission's work.

9. a. Claimant I

b. 2001

c. Peruvian tax agency SUNAT served Claimant in November 2001 with a $49 million tax assessment. SUNAT claimed that Claimant's local power company

under previous ownership underpaid taxes from 1996–1999 due to improper use of depreciation after the privatization of the power company. Claimant purchased the privatized company in 1999. The power company was privately audited from 1996–1999, and its financial statements for those years were approved by GOP representatives on the company's board and by the GOP privatization agency. In December 2001, Claimant filed an administrative claim against the tax assessment. In September 2002, SUNAT upheld its assessment but reduced the amount to $43 million. In late September 2002, Claimant appealed this decision to the Tax Court. The pending assessment against claimant now totals more than $50 million with interest. The Tax Court issued in May 2004 a decision disagreeing with the method of depreciation employed by the company and asking for SUNAT to recalculate its assessment. Parallel to the legal proceedings, Claimant and the GOP submitted this case to international arbitration in 2004. Claimant argues that SUNAT's reassessment violates a Legal and Tax Stability Agreement between the Company and the GOP.

10. a. Claimant J

b. 2003

c. In December 2003, tax agency SUNAT assessed claimant $9 million in fines and reduced the income tax credit for 1998 from 32 million Soles (Peruvian currency) to 9 million Soles. The assessment was based on SUNAT's claim that claimant's 1997 merger with a local metal refining company had no economic substance. Claimant believes the merger was done correctly and that its receipt of applicable tax benefits was in strict compliance with existing Peruvian law. Claimant contends that the economic substance of the merger has been clearly demonstrated.

Claimant has appealed the tax assessment before SUNAT. Claimant is concerned that SUNAT will pursue similar assessments for the 1999–2001 tax years.

11. a. Claimant K

b. 2001

c. Claimant is a local power company majority-owned by two U.S. energy companies. Claimant signed a ten-year legal and tax stability agreement with the GOP in 1994. Tax agency SUNAT disputed the company's continued use after 1999 of accelerated depreciation, which was permitted under Peruvian law for companies that underwent reorganizations. The issue initially went to arbitration and a parallel Tax Court proceeding. Claimant won in both instances, but SUNAT was permitted to revisit the case. In July 2003, SUNAT assessed claimant with $56 million in back taxes due since 1999. Claimant again appealed the SUNAT assessment to the Tax Court, which ruled in February 2004 that claimant had a right to revalue assets and that there should be no assessments for the years 19961998. The Tax Court, however, asked SUNAT to review the 1999 assessment again. Claimant awaits a final assessment by SUNAT.

12. a. Claimant L

b. 1970

c. Following receipt of a letter from Congressman Silvestre Reyes (TX) concerning Claimant's case in December 1999, Embassy received a letter from Claimant in February 2000 and met with claimant at his request while he was visiting Peru in May 2000. According to Claimant, in about 1970, Peru's military government expropriated his farm as part of a general land reform act that expropriated farms over 250 hectares. Claimant's farm, however, is just under 200 hectares. Claimant was issued compensation bonds, which have since become worthless as the result of hyperinflation. Claimant asserts that, because he believed the expropriation to be illegal and because he was living in the United States at the time, he made no attempt to redeem the bonds. Claimant has provided no estimate of the land's current value, maintaining that his goal is to have it returned.

Claimant began efforts to recover his farm in 1999. At Embassy's suggestion, he joined an association composed of others whose land was expropriated. Claimant has also contracted legal counsel in Peru, but has not separately pursued remedies through the Peruvian courts.

Embassy Officers met with Claimant in 2000, and were in contact with Claimant on one occasion in 2001. Embassy officers have requested details on the expropriated property, a timeline of events related to the expropriation, and any legal analysis supporting the Claimant's assertion that the expropriation

did not comply with Peruvian law. To date, Embassy has not received this information. Post has had no contact with claimant since July 2001.

13. a. Claimant M

b. 1976

c. According to claimant, pursuant to the Agrarian Reform law, the Peruvian Agriculture Ministry (MinAg) in 1976 transferred about 60 hectares of land he had purchased in 1964 to the Comunidad Campesina de Oyon (CCO), located in the district and province of Oyon in the department of Lima. MinAg allegedly did so without his knowledge and without notifying him of the action.

Claimant hired a lawyer to undertake administrative procedures for recovering his land in 1976, but the claim was lost, and in May 2000 MinAg found that his claim had no merit. He appealed administratively and also received a letter in November 2000 from the Huaura Superior Court indicating that the GOP's General Office of Agrarian Reform had mistaken him for another landholder with a similar name. Simultaneously, Claimant filed suit against local mining firm Buenaventura, which Claimant asserts took advantage of the title dispute to cut all of the trees on what was wooded land. Claimant also says that the dispute led to threats against him from the CCO, and that terrorist activity in the area prevented him from returning to his land until 1990.

Claimant sent Embassy documents in November 2000 related to the alleged expropriation of his land, and Econoff met with Claimant in February 2001 at his request. At Embassy's request Claimant provided a brief letter laying out the facts of the case in March 2001. Embassy forwarded this letter to MinAg, with a request that it be given appropriate attention. The Ambassador received a letter dated May 6, 2002 from MinAg, confirming that the land had been transferred under the agrarian reform program to the CCO on June 19, 1976, and that title had been confirmed to the CCO on November 8, 1982. MinAg asserts that, as a result, Claimant only has a right to claim the fair market value of the land, and must pursue this through the courts.

VENEZUELA

The United States Government is aware of six (6) unresolved claims of United States persons against the Government of Venezuela (GOV).

1. a. Claimant A

b. 2003

c. Since 1982, Claimant, an international consortium of investors with a majority U.S. share, has invested approximately $60 million in developing a diamond concession in Venezuela's Bolivar state. After extensive exploration and evaluation of the asset, Claimant planned to begin mine development in 2003–2004. However, in September 2003, the Venezuelan Ministry of Energy and Mines withdrew part of Claimant's concession, alleging non-payment of taxes and failure to comply with other obligations. Claimant disputes these allegations. The Embassy and U.S. congressional representatives have raised the case with senior GOV officials. Thus far there has been no return of the concession, although no more land has been seized to date.

2. a. Claimant B

b. 2002

c. Claimant was awarded a contract to perform the GOV's 2001 census. The contract included a clause mandating that the GOV compensate Claimant in the event of devaluation and interest accrual. The contract work product was delivered to the GOV on July 4, 2002, and GOV authorities signed off on the bid, performance and advance bonds as evidence of their complete satisfaction with Claimant's performance. After making initial payments, however, the National Statistics Institute ("Instituto Nacional de Estadistica") (INE), the statistical branch of the GOV stopped issuing payments, alleging a lack of funds. INE subsequently also questioned the validity of the contract devaluation clause. The U.S. Commercial Service began advocacy efforts on behalf of Claimant in May 2002 but the GOV has yet to pay the pending portion of the principal or the devaluation differential, a sum that now totals approximately $5.5 million.

3. a. Claimant C

b. 1994

c. Case History: Claimant, an airline, accrued $23 million in foreign exchange losses due to actions taken by the Central Bank of Venezuela (BCV) before and

after a devaluation of the currency in 1995. BCV imposed currency controls in 1994, which compelled Claimant to purchase all U.S. dollars through the Central Bank. The official exchange rate at that time was 290 bolivars to one dollar. Additionally, a 1994 presidential decree obligated the Claimant to sell all airline tickets in Venezuela in bolivars, at the official rate. In early 1995, BCV stopped exchanging bolivars for dollars for several months immediately prior to a significant devaluation of the currency from 290 to 470 bolivars/$ 1. The Claimant maintains that the devaluation resulted in a $23 million loss to the amount held in escrow. The Claimant brought suit against the GOV in July 1996, but the Supreme Court of Venezuela dismissed the suit in May 1998. Claimant resubmitted the case in 1999, and a chamber of the Court made a decision against it on March 25, 2003. Claimant is considering filing a further appeal for reconsideration by another chamber of the Court or taking some other action.

4. a. Claimant D

   b. 2003

   c. In 2001, Claimant, an international consortium with a 55 percent U.S. share, entered into a ten-year contract to operate a key petroleum export terminal for Venezuela's state-owned oil company, Petroleos de Venezuela (PDVSA). On December 6, 2002, as a result of Venezuela's petroleum strike, Claimant declared force majeure. Claimant's employees continued to perform the necessary maintenance so that the terminal could be brought back into operation quickly once the conditions that necessitated the force majeure were resolved. The terminal, however, was seized by the GOV on December 15 and Claimant's employees were forbidden access. Claimant's representatives informed the GOV that it would be willing to be bought out of the contract for a payment of approximately $24 million. Claimant filed for international arbitration with the ICC on May 7, 2003, and the case is now scheduled for hearings before an arbitral panel in September 2004.

5. a. Claimant E

   b. 2001

   c. In 1996, Claimant and Venezuela's state-owned oil company Petroleos de Venezuela (PDVSA) entered into a joint venture agreement. The joint venture company would take over all information technology services for PDVSA under a service agreement that would be renegotiated every five years. In December 2001, as the two were finishing negotiations on the second five-year agreement, PDVSA informed Claimant that it would not be ready to implement a renewed contract. The agreement was subsequently extended for an additional six-month term. Upon expiration of the agreement, Claimant and PDVSA started negotiations to dissolve the joint venture and to transfer Claimant's shares to PDVSA. This situation was exacerbated by the December 2003–February 2003 general strike, during which the joint venture company ceased to provide services to PDVSA.

   Although a tentative agreement was reached in February 2003, the Venezuelan authorities pulled out before it could be finalized and subsequently filed suit against the joint venture company in the Venezuelan courts. In September 2003, Claimant filed a claim under OPIC political risk insurance, stating its investment had been expropriated. On February 24, 2004, OPIC made a final determination in support of this claim and made a final payment to the insured on May 12, 2004. In the meantime, on May 6, 2004, the Venezuelan Supreme Court issued a ruling in the case brought against the joint venture company by PDVSA. In that ruling, the Court ordered the joint venture company to restore the services it had previously supplied to PDVSA.

6. a. Claimant F

   b. 2002

   c. In 1993, Claimant entered into a long-term relationship with Venezuela's state-owned oil company Petroleos de Venezuela (PDVSA) and with PDVSA-affiliate CITGO, in which: (1) Claimant agreed to invest over $1.1 billion to upgrade its refinery to process Venezuelan extra-heavy crude, (2) CITGO agreed to contribute to the upgrading and purchase the bulk of the refined products, and (3) PDVSA committed to supply 230,000 barrels/day for 25 years. Two contracts, one signed under Venezuelan law and one signed under U.S. law, established this relationship. Claimant asserts that between April 1998 and September 2000, PDVSA, citing GOV commitment to OPEC quota cuts, wrongfully declared force majeure and reduced its deliveries by as much as 100,000 barrels/

day. This force majeure was lifted in October 2000, but in January 2002 PDVSA once again informed Claimant that deliveries would be cut because of OPEC quota cuts. Claimant attempted to resolve the dispute but ultimately filed suit against PDVSA on February 1, 2002 before the United States District Court for the Southern District of New York, seeking damages and specific compliance. On May 31, 2002, PDVSA filed a motion to dismiss Claimant's suit arguing protection under the "Act of State doctrine." PDVSA's motion was dismissed in 2003 and the case is proceeding.

Mr. BALLENGER. Mr. Faleomavaega.

Mr. FALEOMAVAEGA. Thank you, Mr. Chairman. And, again, I want to express my appreciation to Secretary Vargo and all the help she has given with my tuna. I don't mean Coach Parcells the "Tuna," Mr. Chairman, I mean tuna that is considered the most pricey fish there is in the consumer market here in the United States.

I do have a couple of questions, and I am a little somewhat puzzled by some of the dialogue that has taken place in terms of the expectations and the standards. And I look at the fact that our corporate interests—these are big boys. These are multi-billion dollar companies that are doing business in Ecuador and Peru. These are not small businesses. What I mean by this is that, as my good friend from Massachusetts said, justice delayed, justice denied. Another saying could also be, what you see is what you get. And I am not being protective of Peruvian or Ecuadorian court systems, but I would think that before these companies wanted to make investments in these countries, they would kind of study carefully the landscape—what kind of a legal system it has, corporate incentives, of course the language in Spanish, I mean the contractual relationships between entities involved here.

I am wondering if you are suggesting here that the legal system with these two countries are not up to our standards, or is it because our corporate interests are not satisfied with the court rulings of some of these things now taking place in court? I am a little fuzzy here. Are you suggesting here that if the companies don't like what they got, they then come to the U.S. Embassy and file a formal complaint because this is not what they wanted? Secretary Wayne, or maybe Ms. Vargo, could you help me with this?

Ms. VARGO. I would say that most of these cases involve instances where the U.S. companies feel that the Governments have changed the rules of the game after a substantial investment has been made, and so many of them involve either allegations of breach of contract or possible expropriation. And the difficulty is how one resolves those issues in an emerging economy, a developing democracy where some of the institutions are weak, where the judicial system does take longer, and where there are some of the complications that have been put forward by Deputy Assistant Secretary Shapiro.

So I don't think it is a matter of double standards or did they not do due diligence in most of these instances; this is a question of how businesses and governments resolve differences.

Mr. FALEOMAVAEGA. Would it be fair for me to say that these companies have taken their legal grievances to the highest level of the courts of both countries, and passing that level are now coming to a Government-to-Government type of situation where we are trying to find a remedy on their behalf? Or are you saying that these

things are still bogged down in lower courts—whether it be negotiations with different agencies or different offices like it is in even our own country? I am saying that, you know, you go to court and you lose a case and you are finished. And I just wanted to know where exactly is the framework of how our corporate interests in these countries are, you might say, not being satisfactory in terms of how the legal system of that country does its operations. Or the way it renders its decisions may be different because it is in Spanish? Does it mean that interpretations may also be taken differently? I don't know. I am just trying to see if there is equity and fairness in the process. What I am hearing here is that it is not being fair, it has not been fair. And I just wanted to know if the legal remedies of our corporate interests have been taken to the highest level and it is now before the Congress and us to take remedial measures like: No FTA, no free trade agreement, if you don't come up to par with what these companies want or expect. That to me is somewhat unfair if, you know, you question the integrity of that country's whole legal system.

Mr. WAYNE. Well, we are of course focusing, Mr. Congressman, here on the countries, I think, in areas where there is a dispute. And some of these disputes are in different stages, and there are some disputes that come on and are resolved after several months and go away. A number of these are disputes that have been out there for a long time and so there has been a problem in resolving them. In the case of Ecuador, where we have a bilateral investment treaty, there is a provision to go to international arbitration, and that is what Occidental Petroleum did when they had a difference with the Government. The Government accepted that, it is in the treaty, and that is a fully accepted process. In other cases, there is treatment in the Peruvian or the Ecuadorian legal system.

But just to put this in context, remember in Peru there are about 150 United States investors. The Commerce Department said that our total investment in Peru in 2002 was about $3.2 billion. The American Chamber of Commerce in Peru says that total investment now they estimate from American companies is about $6 billion. So there is a lot of business going on. Some of it is going on without problem, there is new investment going on. But there are particular cases that we just seem to run into delays in due process.

Mr. FALEOMAVAEGA. And just as some of the cases in our own country have also taken years to adjudicate.

Mr. WAYNE. This happens in many countries, yes.

Mr. FALEOMAVAEGA. So this is what I am trying to get a sense of a better understanding of. Is this our standard procedure now? If an American company does business in a foreign country and is not satisfied due to undue delays and all, it now comes to the Congress and the Administration to put political pressure on these countries to decide otherwise? Is this our procedure now on how we are going to resolve some of these cases?

My problem is that these companies knew as a whole what to expect and they invested, and I am sure they have received a very profitable return for their investments in the process. And I just wanted to get a sense. Is it now a question that we are going to

threaten Peru and Ecuador with free trade agreement restraints or even not participate in the process?

Mr. WAYNE. Congressman, what I would say is certainly from the point of view of the State Department and our Embassies overseas, we have a commitment to support U.S. companies in their exports, in their investment process, when they face an unfair playing field. When they face a lack of due process, then we are available to be supportive of them, but we certainly do have severe limits as to what we do. We do not interfere in judicial processes when there is a judicial process going forward or when it is inappropriate in other countries' institutions. But there is certainly a role when companies face an unfair playing field.

Mr. FALEOMAVAEGA. Just one more question, Mr. Secretary. Just in your best judgment, overall, U.S. companies are being treated in the same way as other companies are? I mean, is there some sense of tainted response; just because it is a U.S. company there is a different line of standard that is applicable? Because certainly we are not in agreement to that kind of a process. But I just want to ask your best judgment, Are our companies being treated any more or any less than any other foreign companies doing business in Peru or Ecuador in getting the same treatment of delayed decisions or, you know, just lack of it or being adjudicated?

Mr. WAYNE. Mr. Congressman, my impression is not that our companies are being discriminated against. But I would say, if I step back, I would say that in both countries it is in the interest of those countries to make their treatment of investors as fair, as respectful of due process, as balanced as possible, because both of those countries are interested in raising their level of prosperity and of raising the incomes of their people. They both have significant portions of their population living below the poverty level. They need trade, they need economic activity, they need job creation, and foreign investment is an important part of that process. And so it is very much in their interest not to discriminate against companies from one country or another, but to treat everybody in a just, fair, and in a quick due process or fair due process way.

Mr. FALEOMAVAEGA. Thank you.

Mr. MENENDEZ. Would my colleague yield?

Mr. FALEOMAVAEGA. I would gladly yield to my good friend.

Mr. MENENDEZ. I appreciate the gentleman yielding. And I want to assure my colleague that to get to this point is an exceptional set of circumstances that nobody wants. But I am sure my colleague would agree with me that when you follow the judicial process of a country, when the constitutional court rules in your favor, then the time frame for appeal from the constitutional court has expired by months, that it is not fair nor in the interests of the United States nor Peru in terms of attracting investments. Because your question might imply that an American company is seeking a benefit that it does not deserve because it has not followed the exhausting of the rule of law in that country. But when an American company follows the exhausting of the rule of law in that country and still is circumvented in achieving the enforcement of that court's decisions, and whose time frames have expired—that is arbitrary, abusive, capricious, and ultimately will create a consequence for investment in that country.

And I hope the gentleman will have the time to stay for the next panel because I think you would hear firsthand that that is the nature of what happens.

And, secondly, I want my dear friend to know that our concern here is that if we are going to just allow our companies to go ahead and—having followed the rule of law, having exhausted their remedies, having had judgments in their favor—still get no redress, then what is the use of trade agreements that don't ultimately ensure their benefit? None of us would want that. And I appreciate the gentleman for yielding.

Mr. FALEOMAVAEGA. And I want to say to my good friend from New Jersey, that is the very question I was trying to raise with the members of the panel and they just haven't been forthcoming in saying this. That is all I was trying to say. It was not clear in my mind in the dialogue that had been taking all this time, is have our companies been treated fairly? And my good friend from New Jersey said they have not been. All I wanted from the panel was, yes, they have not been treated fairly. And I am totally satisfied if that has been the case. But at the same time, I also want to say to my good friend from New Jersey that, you know, in fairness to the host countries, making sure that they have always exhausted their remedies, their processes, their system, so that we don't question the integrity of that country's ability to enforce its laws. If they have been doing it, by golly, they should be recognized for doing so. That is all I was trying to say. And I thank the gentleman for his comment.

Mr. DELAHUNT. Would my colleague yield?

Mr. FALEOMAVAEGA. If I have enough time, I would be happy to.

Mr. DELAHUNT. I thank the Chairman for indulging me. But my point is, too, what I would suggest is that what we have read and what we hear here today not only calls into question the infrastructure, if you will, in terms of arbitrating or resolving commercial disputes, but the integrity of the entire system as it applies to the citizens both of Peru and Ecuador. And let us not forget that this Andean region, I think, can be fairly characterized as a region that is unstable at best at this particular point in time.

So I think it goes far beyond just simply the commercial relationships between American businesses and the executive and judicial branches of these countries that has far more implications. Just imagine workers in Ecuador and Peru who seek enforcement of their rights under any agreement, any provision that might be reached between FTAA. They do not have the resources of large American corporations, and I think that is something that really bothers me and something that we have to consider as we proceed here. And I thank my friend for yielding.

Mr. FALEOMAVAEGA. I thank the gentleman from Massachusetts. Mr. Chairman, thank you. You have been so kind.

Mr. BALLENGER. Ms. Vargo had raised her hand.

Ms. VARGO. I wonder if I might just make a comment on that, Mr. Chairman and Congressman Delahunt, which is that a lot of people, when they think about free trade agreements, primarily think about market access, and they have concerns as our good Representative here from American Samoa does. But it really is about establishing a good set of rules and the conditions for doing

business in the country. So whether those rules are intellectual property rights or services regulation or labor and environment, you are trying to lay that groundwork. And the FTAs, when we do them, strengthen some areas, particularly the relationship between Government and the private sector, in the transparency and advance notice and comment, and in anti-corruption rules. And they are more willing to do that for us sometimes than they are willing to do initially for their own citizens. But when they put it in place for us, you can't wall it off, and that is part of why the kind of agreement and effort we are making here can be broadly beneficial for an emerging democracy. It also helps them in a whole package take on some reforms that individually could never get through their congresses.

So I think we are all about the same thing, and what we are talking about here is what we are troubled about—the need for an indication of the ability and the will to move forward in a constructive way on these particular issues, and we are working hard with the Governments and we have given them a very strong and clear message about their need to be able to demonstrate that they are ready and able to work with us to build and strengthen the system. And these cases present an opportunity for them to demonstrate that, within their political processes, within their judicial processes, that they can bring the right forces to bear.

The only comment I want to emphasize is that we don't ask for a particular outcome. We are looking here for a process; in many of these instances it is already hard to say it is timely, it has been very delayed, but we are looking for a fair and transparent process that gets a resolution for the companies.

Mr. BALLENGER. Well, I think that covers it pretty well, and I would like to thank the panel for being here.

Mr. PAYNE. Mr. Chairman, I won't make a statement. But I just want to simply say that I am glad that you called this very important hearing. And, as you know, the company PSEG in Newark, and Congressman Menendez and I share the city, we are certainly concerned about what is happening as relates to that particular case, and I just wanted to have that put on the record. I won't take up any more time since I am here so late, but I am glad that we are dealing with some of these issues that have been around for quite a while.

Thank you.

Mr. BALLENGER. Again, let me thank you all. We appreciate it. I think it was educational for us, and I hope the news media got the education that we were trying to give them. So thank you for coming, and we will welcome the next panel.

We would like to go on to the next panel, if we may.

We understand we have a vote coming up in about 45 minutes, so we are guaranteed not to keep you too long.

Let me introduce, if I may, first of all, Mr. John G. Murphy. Mr. Murphy serves as Vice President of the Western Hemisphere Affairs of the U.S. Chamber of Commerce. He is also Executive Vice President of the Association of American Chambers of Commerce in Latin America, based in Washington, DC. John Murphy directs all advocacy activities related to trade and investment in the Americas on behalf of the U.S. Chamber of Commerce. He also manages the

staff of Association of American Chambers of Commerce in Latin America. And I think at one time or another I must have met every one of your members.

Second, we have Mr. Farnsworth, Eric P. Farnsworth, as Vice President of the Washington Operations of the Council of the Americas. Mr. Farnsworth leads the Washington-based efforts of the Council, including policy development and advocacy programming and public affairs. The Council includes over 170 corporate members, and has been a leading voice for over 40 years in the effort to promote free markets and free people throughout the Hemisphere.

And, finally, Mr. Mark Dresner. Mr. Dresner is Engelhard Corporation's Vice President of Corporate Communications and an elected officer of the corporation. He is responsible for all public relations and public affairs activities, including corporate positioning, financial communications, media relations, government affairs, marketing communications, and internal communications.

And, with that, we will switch to Mr. Murphy, and you may give your opening statement.

STATEMENT OF JOHN MURPHY, VICE PRESIDENT FOR WESTERN HEMISPHERE AFFAIRS, U.S. CHAMBER OF COMMERCE

Mr. MURPHY. Thank you very much.

I would like to open by thanking the Committee, in particular Chairman Ballenger and Congressman Menendez, for your leadership on a range of important hemispheric issues. This hearing is an excellent example on how this Committee is focused on timely issues that matter to U.S. business.

The U.S. Chamber of Commerce is the largest business federation in the United States and in the world, representing 3 million businesses of every size, sector, and region. At the urging of our broad membership, the Chamber has advocated closer trade relations between the United States and Latin America for nearly a century. In principle, we strongly support the efforts to negotiate a free trade agreement with Columbia, Peru, and Ecuador.

As you have heard, the 100 million citizens of these countries generate a collective GDP near half a trillion dollars when measured on a purchasing power basis. To get a sense of the potential of this combined market, I would simply point to the new United States-Chile free trade agreement which, since January 1st, when it was first implemented, is helping generate new exports to that country at an increased rate of over 20 percent this year alone.

There is no denying the tremendous commercial advantages afforded by this next generation of free trade agreements, and the Chamber strongly supports Ambassador Zoellick and his team, including Ms. Vargo, in this. However, we believe that a number of commercial disputes related to United States companies' investments in Peru and Ecuador must be resolved before concluding the negotiations. And, sadly, progress toward this goal has been disappointing.

It is noteworthy that the Government of Colombia, under the leadership of President Alvaro Uribe, has moved to resolve a number of the most difficult disputes in that country and to improve

the business climate generally. His leadership should serve as an example to other Governments.

The situation in Peru is more difficult. The total value of current disputes of United States companies with the Government of Peru is over $300 million. Notable common threads have already been noted here today, including uncertainty regarding which agency or branch of government has authority to resolve a dispute and lack of respect for legal and tax stability agreements entered into by the Government.

The Chamber is particularly worried about a number of disputes involving the tax agency SUNAT which has already been discussed here today. Too often SUNAT's dealings with companies are inconsistent with Peru's own laws, and the agency has ignored procedural timelines again and again on some cases.

We do note the positive developments of the creation of a taxpayer advocate which has helped to limit some of SUNAT's abilities to prolong unnecessarily some procedures. However, the fact remains that none of the SUNAT-related disputes cited earlier this year have been resolved.

The investment climate is also difficult in Ecuador, where several major United States investors are involved in disputes with the Government. The Chamber was particularly alarmed at a recent comment by a senior Ecuadorian official suggesting the country would not comply with the terms of the existing United States-Ecuador investment treaty.

U.S. trade negotiators will rightly insist on including in the United States-Andean FTA an investment chapter that will strengthen the provisions in the existing BIT. By threatening to overturn the BIT, the Government of Ecuador raises serious questions about whether the Government should be expected to—whether or not they could be expected to respect the terms of the FTA.

In my written statement I provide details on some particularly worrying cases. Occidental Petroleum, BellSouth and Bechtel are among the companies whose cases are detailed. We are concerned about instances in which the Ecuadorian Government has refused to enforce rulings by binding arbitration panels and failed to comply with domestic law and the terms of contracts with foreign companies.

In another case, a group of Ecuadorian citizens filed an action last year against the predecessor fourth tier subsidiary of ChevronTexaco that was part of a now defunct consortium of companies that included the State-owned oil company, Petroecuador. This legal claim is contrary to a settlement and release agreement reached 9 years ago by ChevronTexaco and the Government of Ecuador. In fact, the Ecuadorian Government certified in 1998 that ChevronTexaco had fulfilled all terms of the agreement. Unfairly and inexplicably, Petroecuador is not mentioned in this legal action.

Now, one major reason the Chamber supports free trade agreements is that they represent strong medicine to prevent certain kinds of disputes from arriving in the future. This is accomplished through the creation of a more transparent rules-based business environment which in turn will strengthen democratic institutions.

For example, the FTA will guarantee transparency in Government procurement with competitive bidding for contracts and extensive information made available over the Internet, not just to well-connected insiders, and it will strengthen legal protections for intellectual property rights in the region as well as the actual enforcement of those rights. In this sense, the FTA is a significant part of the solution to the problems that beset the investment climate in these countries.

The Chamber has shown its commitment to these FTAs by organizing business roundtables at each of the negotiating rounds to date as well as activities in several U.S. cities. However, the Chamber's support for the inclusion of Peru and Ecuador in the United States-Andean FTA is tempered by the urgent need to secure the rapid resolution of these disputes. While we understand each case is different, and some cases may require additional time due to arbitral processes, the time to act on most of them is now. We need action, not words; accion, no palabras.

If the opportunity to conclude a free trade agreement with the United States should fall by the wayside, Peru and Ecuador may have to wait years for another chance to enter into such an economic relationship with the United States. It is incumbent upon those two Governments to demonstrate their resolve.

Thank you.

[The prepared statement of Mr. Murphy follows:]

PREPARED STATEMENT OF JOHN MURPHY, VICE PRESIDENT FOR WESTERN HEMISPHERE AFFAIRS, U.S. CHAMBER OF COMMERCE

In May 2004, the United States launched negotiations for a free trade agreement with Colombia, Peru, and Ecuador, dubbed the U.S.-Andean Free Trade Agreement (FTA). Several negotiating rounds have been held since May, and officials with the Office of the U.S. Trade Representative have outlined a negotiating schedule aiming to conclude the agreement in January 2005. Bolivia is participating in the negotiations as an observer.

The U.S. Chamber of Commerce is the world's largest business federation, representing three million businesses of every size, sector, and region. The U.S. Chamber has long advocated closer trade relations between the United States and the countries of Latin America and the Caribbean through the Free Trade Area of the Americas (FTAA) negotiations as well as bilateral and sub-regional agreements such as the North American Free Trade Agreement (NAFTA), which has brought remarkable benefits to U.S. businesses, workers, and consumers. The U.S.-Chile FTA, which was implemented on January 1, is already delivering significant benefits for the U.S. economy as well. The U.S. Chamber also expects excellent results from the landmark U.S.-Dominican Republic-Central America Free Trade Agreement (DR–CAFTA), which is pending Congressional approval.

In similar fashion, many of our member companies and their employees stand to benefit directly from the proposed U.S.-Andean FTA. The agreement stands to boost trade and investment between the United States and several of our closest neighbors. Colombia, Peru, and Ecuador represent a significant potential market, with a population of 93 million and a collective GDP near $500 billion when measured on a purchasing power parity basis. Bilateral trade was near $17 billion in 2002.

The U.S. Chamber of Commerce supports the proposed FTA in principle. We believe the FTA will help promote the economic development of the Andean countries while providing new business opportunities for U.S. agriculture, industry, and service providers. However, we believe that a number of commercial disputes related to U.S. companies' investments in Peru and Ecuador must be resolved before concluding negotiations. Sadly, progress toward this goal has been disappointing.

RESOLVING ONGOING INVESTMENT DISPUTES

A number of persistent disputes between U.S. companies that have invested in Peru and Ecuador and the respective national governments stand as a substantial obstacle that could block the participation of these countries in a free trade agree-

ment with the United States. The few remaining months of the negotiations represent a critical opportunity for governments to resolve these disputes.

It is noteworthy that the government of Colombia, under the leadership of President Alvaro Uribe, has moved to resolve a number of the most difficult disputes in that country and to improve the business climate generally. His leadership and the diligence of other members of the Colombian government to resolve a number of thorny problems serve as an example to other governments.

The situation in Peru is more difficult, and details relating to investment disputes in that country are well known to a variety of U.S. officials, obviating the need for a detailed account in this document. The total value of current disputes of U.S. companies with the government of Peru is over $300 million. Notable common threads in the disputes include aggressive tax assessment strategies targeting foreign firms; uncertainty regarding which agency or branch of government has authority to resolve a dispute; and a lack of respect for legal and tax stability agreements entered into by the government.

The U.S. Chamber is particularly worried about a number of disputes revolving around the Peruvian tax agency, known by its Spanish-language acronym, SUNAT. Too often, SUNAT's dealings with companies are inconsistent with Peruvian law, and the agency has ignored procedural timelines repeatedly in some particular cases. On a positive note, the newly created position of Taxpayer Advocate, sometimes referred to as an ombudsman, represents a step forward. The Taxpayer Advocate has helped to limit some of SUNAT's ability to prolong unnecessary procedural argumentation indefinitely, though the fact remains that none of the SUNAT-related disputes have been resolved.

The investment climate is also difficult in Ecuador, where several major U.S. investors are involved in disputes with the government. Among the difficulties that have kept foreign investors away are the government's failure to pay its bills to private companies and its willingness to see spurious lawsuits against multinationals pursued in domestic courts.

The U.S. Chamber was particularly alarmed at a recent comment by a senior official of the Ecuadorian government suggesting the country would not comply with the terms of the existing U.S.-Ecuador investment treaty. U.S. trade negotiators will rightly insist on including in the U.S.-Andean FTA an investment chapter that will strengthen the protections in the existing bilateral investment treaty. By threatening to overturn the existing BIT, the government of Ecuador is raising serious questions about its readiness for a free trade agreement. The comment also raises doubts about whether the government of Ecuador could be expected to respect the terms of the free trade agreement itself.

In one specific case, Ecuador's attorney general in August submitted a petition to the energy ministry seeking termination of a 19-year-old contract with Occidental Petroleum Corporation, Ecuador's largest foreign investor. This action comes hard on the heels of a July decision by an international arbitration tribunal, which ordered the government of Ecuador to pay Occidental a $75 million tax rebate. It is difficult to conclude that the government of Ecuador's move to terminate Occidental's contract is anything but retaliation for the unfavorable arbitral ruling. These actions send an alarming signal to foreign investors, but the true losers in this dispute are the people of Ecuador, who stand to benefit from development of the energy sector.

In another instance, BellSouth, a company that has invested over half a billion dollars primarily in Ecuador's cellular market, faces a variety of issues related primarily to the Ecuadorian government's failure to enforce binding arbitral agreements, a lack of fairness and transparency in negotiations with government entities, and a lack of transparency and consistency in the regulatory process. To illustrate, after a two-year binding arbitration process in which BellSouth was determined to be entitled to over $18 million because of the improper imposition of a tariff on handsets, the Ecuadorian government then requested nullification of the award through the local court system, where it remains pending. During the renegotiation of interconnection contracts with the state-owned companies, BellSouth continued to provide services and so far over $10 million is owed, but not paid, for services provided. Just this week, one of the state-owned companies announced that it intends to unilaterally impose, not negotiate, new rates, which further calls into question whether the state-owned companies are negotiating in good faith. And, almost a year ago, BellSouth filed a notification of intent to provide a supplemental service allowed under the company's concession contract, but the regulator has not acted on the notification, and the inaction has provided an advantage to domestic interests that provide competing services.

In another case, the Ecuadorian government has failed to comply with its own law in a dispute involving Interagua, an affiliate of the Bechtel Corporation, which is

a concessionaire for the supply of water services in Guayaquil. The government has not complied with provisions in the original telephony and radio communications law, 175, and its successors, which directed that two-thirds of the revenue generated by a 15% surcharge on telephony bills be automatically deposited in a trust mechanism for Interagua. Provisions of the concession contract have effectively prevented Interagua from obtaining the necessary long-term debt financing to complete the expansion of the potable water and sewage connections stipulated in the contract. Continued non-compliance by the Ecuadorian government could lead to large financial losses by Interagua and failure of the utility to provide adequate water and sewage services to the people of Guayaquil.

The U.S. Chamber is also very concerned about the lawsuit faced by ChevronTexaco Corporation in Ecuador, which potentially represents an instance of "global forum shopping." Last year, a group of Ecuadorian citizens filed an action against a predecessor, fourth-tier subsidiary that was part of a now-defunct consortium of companies that included elements of the Ecuadorian government. The consortium had been licensed by the Ecuadorian government between the years of 1964 and 1992 to explore and produce oil. This legal claim is contrary to a standing 1995 Settlement and Release Agreement between ChevronTexaco and the government of Ecuador, including its state-owned oil company, Petroecuador, which was a member of the former consortium. In fact, the Ecuadorian government certified in 1998 that ChevronTexaco fulfilled all terms of the Agreement, pouring nearly $50 million into the Oriente region in the form of environmental remediation programs and social projects to directly benefit the local communities. To resolve the dispute, the Ecuadorian government must admit its responsibility for the situation involving ChevronTexaco in the Oriente and define a plan of action to resolve these concerns, thereby eliminating the basis for naming ChevronTexaco as the sole defendant in the lawsuit.

PREVENTING FUTURE INVESTMENT DISPUTES

One major reason the U.S. Chamber supports the proposed FTA is that it represents strong medicine to prevent certain kinds of disputes from arising in the future. This is accomplished through the creation of a more transparent rules-based business environment which in turn will help enhance democratic institutions, business transparency, and economic reform. For example, the FTA will guarantee transparency in government procurement, with competitive bidding for contracts and extensive information made available on the Internet—not just to well-connected insiders. It will also create a level playing field in the regulatory environment for services, including telecoms, insurance, and express shipments.

Another instance where we expect the FTA to improve the business climate in the Andean countries relates to dealer protection laws. Such laws represent a significant trade and investment barrier for U.S. companies seeking to do business in the region. In some cases, these laws provide local dealers and distributors of products, services, and trademarks owned by foreign principals with exaggerated protections, locking manufacturers into exclusive dealership arrangements. In some cases, U.S. companies have no way to discipline a nonperforming dealer. The recently negotiated DR–CAFTA dealt with this matter effectively, and the U.S.-Andean FTA should use that agreement as a model in this regard.

In addition, the proposed FTA also represents an important opportunity to strengthen legal protections for intellectual property rights in the region, as well as the actual enforcement of these rights. For the pharmaceutical patent-based industries, ongoing violations of the WTO's Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) as well as provisions of the Andean Trade Preference Act (as amended in 2002) in some of the Andean countries are a source of serious concern. This is particularly true with regard to the failure to protect confidential and exclusive test data in the research-based pharmaceutical sector. The U.S. Chamber submitted more detailed comments on negotiating priorities to the inter-agency Trade Policy Staff Committee on March 17, 2004.

The government of Colombia took a positive first step last year with the promulgation of Decree 2085, which protects confidential test data provided to the authorities upon registering a patent. Peru and Ecuador should take the necessary administrative steps to ensure that no new or additional unauthorized copies of innovative drugs are given a sanitary registration and/or marketing approval inconsistent with data exclusivity. This provisional protection should remain in place until such time that Peru and Ecuador complete implementation of meaningful and effective data exclusivity language.

RESOLVING FUTURE INVESTMENT DISPUTES

A final reason the U.S. Chamber in principle supports the FTA is the promise it holds to establish dispute settlement mechanisms designed to provide timely recourse to an impartial tribunal. Such "Investor to State Dispute Settlement Procedures" (ISDPs) are included in over 40 bilateral investment treaties (BITs) between the United States and other countries, many of which have been in force for decades, as well as in FTAs.

ISDPs provide for dispute settlement panels operating under international legal standards that mirror U.S. Constitutional protections against arbitrary government actions and against taking of property without compensation. In developing countries where local judiciaries are at times slow, ineffective, or corrupt, U.S. companies have benefited from recourse to ISDPs. The existence of such procedures in a BIT or FTA represents a boon to the investment climate, even though the number of cases tried is typically very small (e.g., a total of just over 30 cases have been brought under NAFTA's Chapter 11 in all three countries over the past ten years). The value of the investments involved in these cases is small compared to the hundreds of billions of dollars that U.S. companies have invested in countries with which the United States has BITs or FTAs that feature ISDPs.

In this vein, the FTA should include a requirement that the signatory countries take the necessary steps to accede to arbitral conventions, including New York Convention and the Convention on the Settlement of Investment Disputes between States and Nationals of Other States (ICSID Convention).

CONCLUSION

The U.S. Chamber believes that a free trade agreement with the Andean countries has the potential to improve the region's investment climate and economic development prospects. Above all, the rules included in such an agreement promise to level the playing field for U.S. and local businesses in important ways, including measures to ensure transparency in government procurement, stronger protections for intellectual property, and access to international arbitration for investment disputes. In this sense, the FTA is a significant part of the solution to the problems that beset the investment climate in some countries.

However, the U.S. Chamber's support for the inclusion of Peru and Ecuador in the U.S.-Andean Free Trade Agreement is tempered by the urgent need to secure the rapid resolution of the disputes cited above. While we understand that each case is different in nature, and some cases may require additional time to resolve, concluding the negotiations with Peru and Ecuador should be conditioned on the resolution of a great majority of these disputes. While some cases pending before international arbitral panels are subject to fixed timetables, it is certainly reasonable to require the final resolution of many of these cases, including those involving Peru's SUNAT. We have had enough of roadmaps. We need action, not words—hechos, no palabras. If the opportunity to conclude a free trade agreement with the United States should fall by the wayside, Peru and Ecuador may have to wait years for another chance to enter into such an economic relationship with the United States. In this sense, Peru and Ecuador are at a critical juncture in their economic development. It is incumbent upon those two governments to demonstrate their resolve.

Mr. BALLENGER. Mr. Farnsworth.

STATEMENT OF ERIC FARNSWORTH, VICE PRESIDENT, COUNCIL OF THE AMERICAS

Mr. FARNSWORTH. Mr. Chairman, Members of the Committee, as you mentioned, my name is Eric Farnsworth, with the Washington office of the Council of the Americas. And as you have said, our members are over 170 corporations and businesses who have been active in Latin America and the Caribbean for many, many years. We really do appreciate the invitation to speak before you today, and I would simply echo my colleague's comments, John Murphy from the Chamber, to thank you both for the specific hearing but also, frankly, for your leadership on these issues for many years. So thank you very much.

Before I address the specific issues at hand with regard to Peru and Ecuador, I would like to put some of these issues in context.

As you know, Mr. Chairman, the Council strongly believes that it is in the economic and national security interests of the United States to pursue open trade and investment relationships in the Western Hemisphere. We have been strong supporters of virtually every agreement that has been negotiated in the region starting with NAFTA, the United States-Chile FTA, Trade Promotion Authority, and obviously the agreement that has been negotiated with Central America. We are strongly supportive of these initiatives, and we congratulate the U.S. Trade Representative for moving forward.

Similarly, we have supported, in principle, ongoing negotiations toward the free trade agreements with the Andean countries of Colombia, Ecuador, Peru, and prospectively Bolivia. Such agreements are in the U.S. interest, we believe, for a number of reasons. They facilitate commerce to our largest export market, the Western Hemisphere, they catalyze economic growth in the United States, which leads to the creation of jobs. As has been mentioned in the previous panel, they set world class standards in areas like services, trade, and intellectual property where the United States has comparative advantages in the global market, and they foster closer, more cooperative relationships with strategic allies on a number of foreign policy fronts.

We also believe that these agreements are in the interests of our trading partners in the Hemisphere. Trade with the United States is a key component of virtually all hemispheric economies. Trade agreements provide an incentive to implement important economic and political reforms that support democracy and development. And, frankly, global investors take a favorable view of these types of issues as a sign of increased stability and potential. And for all of these reasons, as I mentioned, the Council has supported trade negotiations with the Andean nations from the moment they were first announced by Ambassador Zoellick, actually, at our Washington conference in May just this year.

Mr. Chairman, I am going into this level of background and detail in order to express to you and to Members of the Committee our recognition of the importance of trade and investment not just for the United States but also for the countries of the Andean region. At the same time, however, I must also express the deep concern that we, as longstanding friends of Latin America and certainly of the Andean region, have about ongoing investment disputes in certain Andean nations, that have the potential, frankly, to threaten the vision that I have just laid out in terms of hemispheric trade and the mutual benefits that we believe that it brings.

It is safe to say, I believe, that wherever investments are made, investment disputes will inevitably arise. The issue is not whether such disputes exist, the issue rather is whether—when they do arise—investment disputes are promptly, adequately, and effectively resolved. And whether the established patterns of foreign government behavior build momentum and goodwill for their ultimate resolution or, frankly, obstruct and impede this goal. This has direct implications for the decisions of future investors while speaking to the issue of whether nations will be able to meet prospective commitments that they may make in trade agreements with the

United States, and I believe those issues were fairly well aired out in the last panel.

As a positive example, one need look no further than Colombia, a nation that seeks to resolve investment disputes while honoring international trade obligations, including the ATPDEA. Colombia has also been hailed as a leader and a partner in the discussions for FTAA. Even with ongoing political difficulties, investors have responded in a positive way. This is not to say there are no obstacles to trade with Colombia, but rather that Colombia has shown itself to be a strong candidate for expanded trade and an impetus for the regional agreement.

Now, with regard to the two countries at hand—and I thank you for your indulgence to allow me to set the background for that. We also believe that expanded trade would have salutary benefits over time for Ecuador and Peru. But one of the main benefits of the trade agreement is to draw increased foreign direct investment from abroad. Trade and investment are really two sides of the same coin. And in that regard, in a global economy where capital is a coward, investors will look first to the investment climate as to whether they will increase or, frankly, reduce their exposure to the countries in question.

Last March at a hearing before the Administration I noted the vexing nature of investment disputes in Peru and Ecuador, urging the sequential definitive resolution of disputes—and I must say definitive is a key word in that context—at a minimum, as a gesture of goodwill we asked that no new cases be allowed to develop as negotiations were moving forward and as discussions for resolution of existing cases were ongoing. I noted that with specific reference to Peru, and contrary to Peru's own policies concerning foreign investments, the Peruvian internal revenue service, SUNAT, which has been previously mentioned, has seemingly embarked on a campaign retroactively to assess foreign direct investors. Indeed, the day after trade negotiations were publicly announced, one of our member companies received a new unfounded multi-million dollar tax assessment—the day after. To date, disputed tax assessments against Council member companies total over $200 million, another one of which occurred as recently as December 2003. Others have been ongoing for several years, of course, but all revolve around the tax agency SUNAT. Rather than shrinking, the universe of disputes that we have been involved with has actually expanded since the idea of a free trade agreement was first put on the table.

Equally serious problems exist, of course, with regard to member companies in Ecuador, several of which have been mentioned by, again, John previously, where senior officials have recently disavowed international arbitral judgments concerning international investors. They have sought to litigate or reopen cases that have long been closed, and they have suggested that Ecuador should unilaterally abrogate its bilateral investment treaty with the United States, the one document that actually guarantees redress for international investors should the local remedies not prove effective.

Even where companies have gone all the way to international arbitration, generally the end of a long road of local remedies and legal battles—frankly, it is a true last recourse for aggrieved par-

ties—and even where they have won favorable judgments, the Government has refused to recognize the result.

Collectively, these circumstances I must say portray a pattern of behavior that casts doubt on the ability of long-term direct foreign investors to obtain redress, and they are disturbing, as has been mentioned previously, because they are occurring even as trade negotiations are progressing.

Mr. Chairman, let me please be perfectly clear. We strongly support expanded trade and investment with the Andean region, and it is our fervent hope—and I really mean that—our fervent hope that these disputes are resolved quickly and judiciously so that an agreement, once it is negotiated, can gain the support it will need to be implemented promptly with maximum economic impact. And that is why we are working so hard with key officials in Peru and Ecuador who understand the problem—and they are there, and we are trying to work closely with them. And, frankly, we thank representatives of the Government of Peru and Ecuador for their openness to do that.

We are also working closely with members of the U.S. Government. And I would say that both United States Ambassadors in Peru and Ecuador, Curt Struble and Kristie Kenney, I think have done a remarkable job. Speaking personally, I think they have done a very good job, and we appreciate their efforts. Obviously, as Members of the Committee, you all have been quick to respond to these issues, too, and we very much appreciate that.

In conclusion, let me simply say that we are in a process. Free trade negotiations with the Andean countries are ongoing, and we remain hopeful that our partners in Peru and Ecuador will be successful in their efforts to resolve these disputes. We would of course like to see them resolved immediately or as soon as practical. And for the longer term, it is critical that a mechanism be put in place in each of these countries that ensures fair, transparent, definitive, and consistent treatment of disputes in a timely manner. Indeed, we believe that trade agreements can and should be supportive of these efforts. And, again, the previous panel discussed those issues. However, now, as trade negotiations proceed to an end game, the time of action really is at hand.

Mr. Chairman, I thank you again for the opportunity to be with you and your colleagues again today, and I look forward to your questions.

[The prepared statement of Mr. Farnsworth follows:]

PREPARED STATEMENT OF ERIC FARNSWORTH, VICE PRESIDENT, COUNCIL OF THE AMERICAS

Good afternoon, Mr. Chairman, members of the Committee. My name is Eric Farnsworth, Washington Vice President of the Council of the Americas. As you know, the Council of the Americas ("Council") is a leading voice for U.S. business in Latin America and the Caribbean. Our members include over 170 prominent companies invested and doing business in the Western Hemisphere. For almost 40 years, the mandate of the Council has been to promote open markets, democracy, and the rule of law throughout the Americas. Thank you for the invitation to speak before you today.

Before I address the specific topic at hand, let me provide a little background to put these issues in context.

The Council strongly believes that it is in the economic and national security interests of the United States to pursue open trade and investment relationships in the Western Hemisphere. For that reason, we were strong supporters of the North

American Free Trade Agreement; we were leading advocates for Trade Promotion Authority; and we were strong proponents of the bilateral trade agreement with Chile that just went into force earlier this year on January 1. Our ultimate goal in the hemisphere, as agreed on a bipartisan basis with democratic leaders at Summits of the Americas in Miami, Santiago, Quebec City, and Monterrey, is a hemispheric free trade area that links regional economies in a high standards, commercially meaningful agreement. In the interim, we have given our support to the negotiation of sub-regional trade agreements that can contribute to the overall goal of a Free Trade Area of the Americas, including the pending agreement with Central America. Similarly, we have supported in principle ongoing negotiations toward a free trade agreement with the Andean countries of Colombia, Ecuador, Peru, and prospectively Bolivia.

Such agreements are in the U.S. interest for a number of reasons: they facilitate commerce with our largest export market (44% of all U.S. exports go to the Western Hemisphere); they catalyze economic growth in the United States, which leads to the creation of jobs; they set world-class standards in areas like services trade and intellectual property, where the United States has comparative advantages in the global market; and, they foster closer, more cooperative, relationships with strategic allies on a number of foreign policy fronts.

We also believe that these agreements are in the interests of our trading partners in the hemisphere: trade with the United States is a key component of virtually all hemispheric economies; trade agreements provide an incentive to implement important economic and political reforms that support democracy and development; and, global investors view a trade agreement with the United States as a sign of increased stability and potential.

For all of these reasons, the Council has supported trade negotiations with the Andean nations from the moment they were first announced by Ambassador Bob Zoellick at the Council's Washington Conference in May. And we put forward a vision—as we did with respect to Central America—that the ultimate U.S. goal with regard to the region should not be a series of two-way agreements, but rather open trade existing among as well as between countries. For U.S. companies this would mean a consistent set of rules on a regional basis. For our trading partners it would mean strengthened intra-regional ties and increased economies of scale. In trade terms, the more parties to a final agreement, the better.

Mr. Chairman, I am going into this level of background and detail in order to express to you and to members of the Committee our recognition of the importance of trade and investment, not just for the United States, but also for countries in the Andean region. At the same time, I must also express the deep concern that we—as long standing friends of the region—have about ongoing investment disputes in certain Andean nations that have the potential to threaten this vision.

It is safe to say that, wherever investments are made, investment disputes will inevitably arise. The issue is not whether such disputes exist. The issue, rather, is whether, when they do arise, investment disputes are promptly, adequately and effectively resolved, and whether the established patterns of foreign government behavior build momentum and goodwill toward their ultimate resolution, or obstruct this goal. This has direct implications for the decisions of future investors, while speaking to the issue of whether nations will be able to meet prospective commitments they may make in trade agreements with the United States.

As a positive example, one need look no further than Colombia, a nation that seeks to resolve investment disputes while honoring international trade obligations including the ATPDEA. Colombia has also been hailed for its constructive leadership on FTAA. Even with ongoing political difficulties, investors have responded in a positive way. This is not to say that there are no obstacles to free trade and investment with Colombia, but rather that Colombia has shown itself to be a strong candidate for expanded trade and an impetus for the regional agreement.

With regard to Ecuador and Peru, we also believe that expanded trade would have salutary benefits over time. But one of the main benefits of a trade agreement is to draw increased direct foreign investment from abroad; trade and investment are really two sides of the same coin. And in that regard, in a global economy where capital is a coward, investors will look first to the investment climate as to whether they will increase or reduce their exposure to the countries in question.

Mr. Chairman, last March at a hearing of the inter-agency Trade Policy Staff Committee, I noted the vexing nature of investment disputes in Peru and Ecuador, urging the sequential, definitive resolution of disputes. At a minimum, as a gesture of goodwill, I suggested that no new cases should be allowed to develop.

I noted that contrary to Peru's own policies concerning foreign investment, the internal revenue service, SUNAT, has seemingly embarked on a campaign retroactively to assess foreign direct investors. Indeed, the day after trade negotiations

were publicly announced, one of our member companies received a new, unfounded multi-million dollar tax assessment. To date, disputed tax assessments against Council member companies total over $200 million, another one of which occurred as recently as December 2003. Others have been ongoing for several years, but all revolve around the tax agency-SUNAT. Rather than shrinking, the universe of disputes has actually expanded since the idea of a trade agreement was first proposed.

Equally serious problems exist with member companies in Ecuador, where senior officials have recently disavowed international arbitral judgments concerning international investors, sought to litigate cases long closed, and suggested that Ecuador should unilaterally abrogate its bilateral investment treaty with the United States. Even where companies have gone all the way to international arbitration, generally the end of a long road of local remedies and legal battles—a true last recourse for aggrieved parties—and have won favorable judgments, the government has refused to recognize the result.

Collectively, these circumstances portray a pattern of behavior that casts doubt on the ability of long-term, direct foreign investors to obtain redress, and are disturbing because they are occurring even as trade negotiations are progressing.

Mr. Chairman, let me be perfectly clear. We strongly support expanded trade with the Andean region, and it is our fervent hope that these disputes are quickly resolved so that an agreement, once negotiated, can gain the support it will need to be implemented promptly with maximum economic impact. That's why we are working so hard with key officials in Ecuador and Peru who understand the complications these disputes are creating. We thank representatives of the Governments of Ecuador and Peru for their willingness to engage in this dialogue. By talking frankly about the ramifications of these disputes, we hope to foster a clearer understanding of their importance while supporting the efforts of those officials who are working for their resolution.

The Council has also been in close contact with U.S. government representatives, including U.S. ambassadors Curt Struble in Peru and Kristie Kenney in Ecuador, who have been attuned and responsive, as have a number of officials in Peru and Ecuador, as I noted earlier. Members of this Committee, as well, have been quick to respond to these serious issues.

We are in a process. Free trade negotiations with the Andean countries are ongoing, and we remain hopeful that our partners in Ecuador and Peru will be successful in their efforts to resolve these disputes. We would of course like to see all outstanding disputes resolved immediately. And for the longer term, it is critical that a mechanism be put in place in each of these countries that ensures fair, transparent, definitive and consistent treatment of disputes in a timely manner. Indeed, we believe that trade agreements can and should be supportive of such efforts. Now, as trade negotiations proceed to an endgame, the time for action is at hand.

Mr. Chairman, thank you again for the opportunity to be with you today. I look forward to your questions.

Mr. BALLENGER. Mr. Dresner.

STATEMENT OF MARK DRESNER, VICE PRESIDENT FOR CORPORATE COMMUNICATIONS, ENGLEHARD CORPORATION

Mr. DRESNER. Thank you. Mr. Chairman, Mr. Menendez, Members of the Subcommittee, I certainly appreciate the opportunity to appear before you today to discuss my company's more than 5-year long struggle with the Government of Peru.

For a quick background, Engelhard is a Fortune 500 company headquartered in Iselin, New Jersey, with facilities in 18 States and worldwide operations employing more than 6,600 people. I am here today to strongly request that the United States Congress stand firm in denying the Government of Peru the benefits of a free trade agreement until such time that Peru returns the nearly $30 million it expropriated from our company in 1999, together with accrued interest in accordance with Peruvian law.

The basics of the case are actually very simple. Engelhard purchased real gold at fair market prices, paid all the VAT required under Peruvian law, exported the gold to its United States refinery, thereby becoming eligible for a VAT refund. For more than 5 years

now, the Government of Peru has produced no evidence, either documentary or testimonial, of any wrongdoing on the part of the company or its officials, nor has it ever even offered a motive or explanation of how the company may have profited from any alleged scheme.

On the other hand, each of Engelhard's transactions were found to be legal and appropriate by three independent audits, including one performed by Peruvian court-appointed auditors.

The Government of Peru's position has been to hold Engelhard accountable for the actions of others, time and again claiming that the ultimate exporter should be denied refunds if any VAT shortfalls were discovered or any irregularities occurred regardless of who was responsible.

For example, Peru speaks of sham transactions and false invoices, yet for more than 5 years not one shred of evidence has ever been produced that links Engelhard to any sham transaction or any false invoice.

Another example, which goes to the question of treatment in Peruvian courts, Peruvian officials repeatedly told United States officials that Engelhard people were caught smuggling gold-painted lead bars in an attempt to defraud the Government of VAT. It is true that an individual was in fact caught doing just that, but that person never worked for Engelhard nor had any connection or business dealings with the company whatsoever. That individual pled guilty to defrauding the Peruvian Government of approximately $20 million, he was sent to prison, he served time, he was released. He is a free man today. Yet our case remains unresolved, and two of our own employees remain in legal jeopardy.

In order to secure its ATPDEA benefits in September 2002, former Peruvian Ambassador Roberto Danino promised the United States Government, and I quote:

> "The Government of Peru will promote prompt and effective due process and transparency under the law in connection with processes that companies such as Engelhard may seek to pursue in Peru."

Over the 2 years since that promise, the Government of Peru has done absolutely nothing to promote prompt and effective due process in the Engelhard matter. In fact, quite the opposite is true.

Consider the following: SUNAT repeatedly blocked our attorneys access to the Engelhard file. That is a clear violation of Peruvian law. Only after the attorneys filed formal notarized documents did SUNAT relent and allow our attorneys to see our own file. A thorough review of that file revealed that an engineering report cited by the tax court in its ruling against Engelhard was not in the file, which is another violation of Peruvian law. As a result, Engelhard was denied the opportunity to argue or even see the report before the tax court used it as the basis to rule against the company. An eventual review of that engineering report further revealed it to be a preliminary report, not a final report, which was based solely on information and unverified assumptions provided by SUNAT. Engelhard filed criminal charges against both SUNAT and the Ministry of Economy and Finance for its actions. A subsequent police investigation concluded that members of SUNAT, a number of

SUNAT employees, were alleged perpetrators of four crimes against Engelhard: Abuse of authority and omission of governmental duties, false declarations in administrative proceedings and inducement of government error, general falsehood and illicit associations. The case was forwarded to a special anti-corruption court where a second investigation supported the findings of the police probe.

There still has been no significant progress in the penal case against two officials of Engelhard Peru, a case brought in October of the year 2000 using falsified testimony. Judge Nicolas Trujillo, who initiated that case, faces criminal charges in connection with his actions in bringing that case against Engelhard, as well as many, many others in Peru.

On May 9, 2003, Engelhard filed an action in Peru's constitutional court, claiming SUNAT and the Ministry of Economy and Finance had violated the company's rights. Normally, Peruvian process calls for that decision to be made in 3 days. The case was brought on May 9th, 2003. On April 28, 2004, the constitutional court ruled that Engelhard's rights had indeed been violated. The ruling implicitly and repeatedly states that Engelhard cannot be held responsible for the actions of third parties. The ruling further states that the documentary evidence filed by SUNAT does not demonstrate any irregularities in the purchase of gold by Engelhard. And the court also ruled that SUNAT and the MEF violated due process rules by exercising Engelhard's letters of guarantee totaling approximately $20 million, and by withholding additional refunds from the company, amounting to an additional $10 million.

SUNAT and the MEF appealed the constitutional court ruling. On May 28, 2004, the 5th Civil Chamber of the Superior Court was assigned to decide on the appeal. Now, according to Peruvian law, the Superior Court has 20 business days to render a decision in such an appeal, thereby establishing June 25th, 2004 as the deadline, which, by the way, was well in advance of the recent judiciary strike mentioned in the earlier panel. To date, not only has the Superior Court failed to rule, it has not even scheduled oral arguments in the case.

One of the truly tragic elements of our matter is that Engelhard did what Peru wanted: We invested in their country. Nearly a decade ago, Engelhard saw a business opportunity to purchase and export gold from Peru. We also built a state-of-the-art refinery there. That refinery, which would have provided jobs so desperately needed by Peruvian citizens never opened. Why? Because just before it was scheduled to open in February 1999, the Government of Peru issued Supreme Decree 14, which held Engelhard responsible retroactively for the actions of others with whom we never did business. Though Supreme Decree 14 was later declared unconstitutional, the aim of stealing the company's $30 million had been achieved.

It is clear that Engelhard was the victim of corruption that ultimately lead to the downfall of former President Alberto Fujimori and his infamous spy chief, Vladmir Montesinos. But I want to be very clear that the actions of subsequent Peruvian administrations have seemingly been designed to cover up the illegal actions and provide false justifications for not returning the money rightfully

owed the company. That is in spite of the findings of a bipartisan commission of the Peruvian Congress which concluded that Engelhard was a victim of corrupt elements within SUNAT and the Fujimori Government. That is in spite of the police report I referenced earlier which supports the company's position and was further corroborated by the findings of a probe performed by the anti-corruption court. That is in spite of two separate rulings in the penal case in which a judge granted the equivalent of bail to the Engelhard Peru employees, specifically citing the lack of evidence to support SUNAT's charges. And that is in spite of an overwhelming ruling from the constitutional court which declared that Engelhard's rights were violated, that it had been denied due process, and its money should never have been seized.

At the beginning I said this was an easy case made complex by those in Peru determined to deny the company justice. Throughout these more than 5 years there are two questions Peru has never answered because it simply cannot: If Engelhard bought gold at fair market prices, exported that gold to the United States, paid all the VAT required under Peruvian law and can document each transaction, why is it not entitled to its money back? And, second, if Engelhard paid $1 in VAT and sought $1 in VAT refund, how did the company profit? And what proof do you have that the company did anything wrong?

By its actions, the Government of Peru has demonstrated that it will do only what it is forced to do in order to get what it wants from the United States Government, and now they seek the benefits of a free trade agreement in spite of the fact that Peru has failed to live up to the promise it made to secure its ATPDEA benefits 2 years ago.

Peru argues that it cannot interfere with the Engelhard matter because it is in the courts. This case should never have been put in the courts. Furthermore, these past 5 years have clearly shown us that officials in Peru regularly interfere with the courts when it suits their purposes.

There is no evidence against the company or its employees. Criminal acts have subsequently been committed in order to keep the case hopelessly gridlocked, and that is not simply Engelhard's view, that view is supported by judges' decisions in bail hearings, the findings of a bipartisan commission of the Peruvian Congress, the findings of a Lima police investigation, the findings of a probe by the anti-corruption court, and a ruling by Peru's constitutional court.

We continue to oppose Peru's request for a free trade agreement until such time that Peru demonstrates its ability to offer an environment that will attract and hold foreign investment. Furthermore, to grant Peru these benefits knowing how they continue to mistreat United States companies and mislead U.S. Government officials would be to reward and enable the continuation of such corrupt practices.

I thank you.

[The prepared statement of Mr. Dresner follows:]

PREPARED STATEMENT OF MARK DRESNER, VICE PRESIDENT FOR CORPORATE COMMUNICATIONS, ENGLEHARD CORPORATION

Mr. Chairman, Mr. Menendez and Members of the Subcommittee, I appreciate the opportunity to appear before you today to discuss my company's more than five-year struggle with the Government of Peru.

I am Mark Dresner, Vice President of Corporate Communications for Engelhard Corporation. Engelhard is a *FORTUNE 500* company headquartered in Iselin, New Jersey with facilities in 18 states and worldwide operations employing more than 6,600 people.

I am here today to strongly request that the United States Congress stand firm in denying the Government of Peru the benefits of a Free Trade Agreement—and consider withholding some of the more than $600 million Peru annually receives from the U.S. Government—until such time that Peru returns the nearly $30 million it expropriated from our company in 1999, together with accrued interest in accordance with Peruvian law.

The basics of the case are simple. Engelhard purchased real gold at fair market prices, paid all the VAT required under Peruvian law and exported the gold to its U.S. refinery, thereby becoming eligible for a VAT refund.

For more than five years now, the Government of Peru has produced no evidence—either documentary or testimonial—of any wrongdoing on the part of the company or its officials, nor has it ever even offered a motive or explanation of how the company may have profited from any alleged scheme.

On the other hand, all of Engelhard's transactions were found to be legal and appropriate by three independent audits, including one performed by Peruvian court-appointed auditors.

The Government of Peru's position has been to hold Engelhard accountable for the actions of others—time and again claiming that the ultimate exporter should be denied refunds if any VAT shortfalls were discovered or any irregularities occurred—regardless of who was truly responsible.

For example, Peru speaks of sham transactions and false invoices. Yet, for more than five years, not one shred of evidence has been produced that links Engelhard to any sham transaction or false invoice.

Another example: Peruvian officials repeatedly told U.S. officials that Engelhard people were caught smuggling gold-painted lead bars in an attempt to defraud the government of VAT. It is true that an individual was caught doing just that, but that person never worked for Engelhard nor had any connection or business dealings with the company. That individual plead guilty to defrauding the Peruvian government of approximately $20 million. He was sent to prison, served time and was released. He is a free man today. Yet our case remains unresolved, and two of our employees remain in legal jeopardy.

In order to secure its ATPDEA benefits in September 2002, Peru's former Ambassador Roberto Danino promised the U.S. Government:

> *"The Government of Peru will promote prompt and effective due process and transparency under the law in connection with processes that companies such as Engelhard and Princeton Dover may seek to pursue in Peru."*

Over the two years since that promise, the Government of Peru has done absolutely nothing *"to promote prompt and effective due process"* in the Engelhard matter. In fact, quite the opposite is true. Consider the following:

- SUNAT (Peru's taxing authority) repeatedly blocked our attorneys access to the Engelhard file—a clear violation of Peruvian law. Only after the attorneys filed formal, notarized documents did SUNAT relent and allow access.
- A thorough review of that file revealed that an engineering report cited by the Tax Court in its ruling against Engelhard was not in the file, another clear violation of Peruvian law. As a result, Engelhard was denied the opportunity to argue—or even see—the report before the Tax Court used it as the basis to rule against the company.
- An eventual review of that engineering report revealed it to be a preliminary document—not a final report—which was based solely on information and unverified assumptions provided by SUNAT.
- Engelhard filed criminal charges against both SUNAT and the Ministry of Economy and Finance (MEF) for its actions. A subsequent police investigation concluded that a number of SUNAT employees were "alleged perpetrators" of:
  1. *"Offense against public administration—abuse of authority and omission of governmental duties;"*

2. *"Offense against judicial administration—false declarations in administrative proceedings—inducement of government error;"*
3. *"Offense against public good faith—general falsehood;" and*
4. *"Offense against public peace—illicit association."*

- The case was forwarded to a special Anti-Corruption Court, where a second investigation supported the findings of the police probe.
- There still has been no significant progress in the penal case against two officials of Engelhard Peru; a case brought in October 2000 using falsified testimony. Judge Nicolas Trujillo, who initiated that case, faces criminal charges in connection with his actions in the Engelhard case and many others.

On May 9, 2003, Engelhard filed an action in Peru's Constitutional Court, claiming SUNAT and the MEF had violated the company's rights. On April 28, 2004, the Constitutional Court ruled that Engelhard's rights had, indeed, been violated. The ruling implicitly and repeatedly states that *Engelhard* cannot be held responsible for the actions of third parties.

The ruling further states that the documentary evidence filed by SUNAT does not demonstrate any irregularities in the purchase of gold by Engelhard. The Court also ruled that SUNAT and the MEF violated due process rules by exercising Engelhard's letters of guaranty totaling approximately $20 million and withholding additional refunds from the company amounting to an additional $10 million.

SUNAT and the MEF appealed the Constitutional Court ruling. On May 28, 2004, the Fifth Civil Chamber of the Superior Court was assigned to decide the appeal. According to Peruvian law, Superior Court has 20 business days to render its decision, thereby establishing June 25, 2004 as the deadline. To date, not only has the Superior Court failed to rule, it has not even scheduled oral arguments in the case.

One of the truly tragic elements of our matter is that Engelhard did what Peru wanted: We invested in their country. Nearly a decade ago, Engelhard saw a business opportunity to purchase and export gold from Peru. We also built a state-of-the-art refinery there.

That refinery, which would have provided jobs so desperately needed by Peruvian citizens never opened. Why? Because just before its scheduled opening in February 1999, the Government of Peru issued Supreme Decree 14—which held Engelhard responsible, *retroactively*, for the actions of others with whom we never did business. Though Supreme Decree 14 was later declared unconstitutional, the aim of stealing the company's $30 million was achieved.

It is clear that Engelhard was the victim of the corruption that ultimately led to the downfall of former President Alberto Fujimori and his infamous spy chief Vladmir Montesinos. However, I want to be very clear that the actions of subsequent Peruvian administrations has seemingly been designed to cover-up the illegal actions and provide false justification for not returning the money rightfully owed the company.

- That is in spite of the findings of a bi-partisan commission of the Peruvian congress, which concluded that Engelhard was a "victim" of corrupt elements within SUNAT and the Fujimori government.
- That is in spite of the police report I referenced earlier, which supports the company's position and was further corroborated by the findings of a probe performed by Peru's Anti-Corruption Court.
- That is in spite of two separate rulings in the penal case in which a judge granted the equivalent of bail to the Engelhard Peru employees, specifically citing the lack of evidence to support SUNAT's charges.
- And that is in spite of an overwhelming ruling from the Constitutional Court, which declared that Engelhard's rights were violated, that it had been denied due process and that its money should never have been seized.

At the beginning, I said this was an easy case made complex by those in Peru determined to deny the company justice. Throughout these more than five years, there are two questions Peru has never answered—because it cannot:

1. If Engelhard bought gold at fair market prices, exported that gold to the United States, paid all the VAT required under Peruvian law, and can document each transaction, why is it not entitled to its money back?
2. If Engelhard paid $1 in VAT and sought $1 in VAT refund, how did they profit, and what proof do you have that the company did anything wrong?

By its actions, the Government of Peru has demonstrated that it will do only what it is forced to do in order to get what it seeks from the U.S. Government. Now, they seek the benefits of a Free Trade Agreement and ongoing U.S. aid in spite of the

fact that Peru has failed to live up to the promises it made to secure ATPDEA benefits two years ago.

Peru argues that it cannot interfere in the Engelhard matter because the case is "in the courts." This case should never have been put in the courts. Furthermore, these past five years have clearly shown us that officials in Peru regularly interfere with the courts when it suits their purposes.

There is no evidence against the company or its employees, and criminal acts have been committed in order to keep the case hopelessly gridlocked. That is not simply Engelhard's view. That view is supported by:

- A judge's decisions in bail hearings;
- The findings of a bi-partisan Commission of the Peruvian Congress;
- The findings of a Lima police investigation;
- The findings of a probe by the Anti-Corruption Court; and
- A ruling by Peru's Constitutional Court.

We continue to oppose Peru's request for a Free Trade Agreement—and continuation of additional U.S. aid—until such time that Peru demonstrates its ability to offer an environment that will attract and hold foreign investment.

Furthermore, to grant Peru these benefits knowing how they continue to mistreat U.S. companies and mislead U.S. Government officials would be to reward and enable the continuation of corrupt practices.

Thank you.

Mr. BALLENGER. Thank you, sir.

Let me ask, Mr. Farnsworth and Mr. Murphy, both of you know of the history of this situation, and obviously there are people that are willing to invest throughout the world and so forth. Do you find anybody now that is willing to invest money in your group—you have got a large number—in either Peru or Ecuador? Has it stopped it?

Mr. FARNSWORTH. Well, it has certainly reduced it, there is no question about that. There are companies that, where they see opportunities where they think they can really do well, they move forward. But it has put a chill on investment, there is no question about it.

And one thing I might add, too, and it relates to the previous panel, is that the comment was made that some of these companies are large companies and they need to do due diligence and things like that. And I believe that is the case. But I think it is the case that the companies do the due diligence, and they go into the countries in some cases having signed specific tax stability agreements, for example, with Peru. Or in the case of Ecuador, having agreements that they have signed to resolve issues that have been longstanding. And then years later, these issues are reopened.

So it is not a matter of companies not being aware of where they are going. In fact, they take every step that they possibly can to hedge their bets, if you will, legally, financially, they do all the right things. But then when Governments change or regulators change or economic circumstances change or something else changes, then it is not uncommon for companies who have made large investments oftentimes in fixed assets that can't easily be removed to then become targets of some of these activities.

But the short answer to your question, Mr. Chairman, is, yes, we have seen continued investment but we have also seen a chill. It is definitely not as high as it otherwise would have been.

Mr. BALLENGER. Does OPIC apply in any of this situation? I mean, they ensure investments overseas. Is that only for earthquake damage or fire? What?

Mr. MURPHY. OPIC's political risk insurance is available in these countries, and some of that insurance does extend to cases like expropriation. Now, it would be very alarming if that became necessary, but that is certainly a word that has been bandied about in some of these recent cases, is that some of these Government actions that have been contemplated seem to resemble expropriation.

Mr. BALLENGER. In my many years of traveling through Central and South America, one of the greatest stumbling blocks I have found in just the development of the economy and the Government itself was the Napoleonic Code. Does that still participate as far—as you mentioned oral arguments. That has been a disaster as far as general law enforcement is concerned. But does it apply also as far as this economic situation?

Mr. MURPHY. I don't know about the Napoleonic Code per se, although it seems as if the way the law is being implemented in some cases seems to resemble from that era. I think it is interesting, as I said earlier, to look at the contrast with Colombia. It is remarkable what President Uribe has been able to accomplish there, and to show how a President who is really committed to creating a transparent business climate can really accomplish a great deal. And there was a backlog of investment disputes in that country, and they have pretty much all been resolved at this point.

Mr. Farnsworth and I both have the experience that companies call us largely when they have difficulties. I have had the unusual experience of having companies call me to talk about how good things are in Colombia lately, and it is a real contrast, and I think it is something that is useful to point out to countries like Ecuador and Peru, which are anxious to have additional foreign investment. Well, the ball is in their court if they wish to attract that.

Mr. BALLENGER. Mr. Menendez.

Mr. MENENDEZ. Thank you, Mr. Chairman.

I want to thank you for your testimony. And before I go to Mr. Dresner, I want to say I appreciate what you had to say. I found that eye opening, Mr. Murphy, because I have been asking this question; I am glad I had the U.S. Chamber of Commerce instead of the U.S. Government quantify for me what is the size of the disputes. Three hundred million dollars. Three hundred million dollars.

And, Mr. Farnsworth, when you say that the scope of the number of cases with SUNAT has expanded since we started negotiations versus contracted, that is just mind boggling to me. It speaks volumes of what I have been trying to get here, Mr. Chairman.

Mr. Dresner, let me ask you a couple of questions. Have you followed the rule of law?

Mr. DRESNER. Absolutely.

Mr. MENENDEZ. In Peru?

Mr. DRESNER. Absolutely.

Mr. MENENDEZ. Have you pursued the legal system?

Mr. DRESNER. Absolutely. Every step of the way.

Mr. MENENDEZ. Has the—well, you had the opportunity to hear the previous panel, and I would like to give you the opportunity to see if you have any—to be kind, to suggest whether you have any different perspectives than maybe the previous panel for the pur-

poses of enlightening the Committee since your company has been involved for years now.

Mr. DRESNER. Yes. I would certainly say that there are differences in the way certain companies are treated in the Peruvian judiciary system, certainly also with SUNAT. In our particular case, one of the largest buyers and sellers of gold in Peru was an operation called Banco Wiese, and Vladmir Montesinos in the infamous videotapes was caught on tape ordering Banco Wiese out of the investigation. His personal banker was with Banco Wiese, his personal accounts were with Banco Wiese. Banco Wiese did manage to slip through on one minor administrative case and one minor penal case. Both of those cases have been resolved.

So the Peruvian system can move when it needs to move, as the example I gave with the gentleman who was found guilty of defrauding the Government. Banco Wiese was let out of the penal case on a technicality. A statement from the banking superintendent that is required before you can go after a bank was not gotten, so they threw the case out of court. And on the administrative side, the tax court ruled in favor of Banco Wiese, which we find particularly interesting because the arguments used in the Banco Wiese case, it was also a VAT refund case, were exactly the same arguments we used, and we lost in front of the same tribunal, the same tax court. So I think there is evidence right there that there is not equal treatment of companies in Peru.

Our case is somewhat unique of all of the ones that I am aware of in Peru. In ours, it is not a dispute, it is clearly thievery, and it is clearly a case where everything has been done to hang up the case so that it is almost unsolvable in a judiciary system that is questionable at best.

On the penal side, they lumped all of the gold cases together. So we are talking dozens and dozens and dozens of defendants with thousands and thousands and thousands of pages of testimony, with no commonality from one case to another. Thrust that on a judiciary system that has no resources with which to handle that. For the first time, 5 years later, they are actually taking statements. There has been no investigative work done. So all of this criminal work that has been sitting in there for 3-, 4 years now, the criminal case actually began a year after the administrative case, has all been based on statements from SUNAT. Not any investigation by anyone else. That work is being done now. They are trying to get statements from over 150 witnesses. At the pace they are going, I would consider that we would probably be looking at close to another 5 years at best.

Now, we have introduced a number of vehicles which we have communicated to the Peruvian Government through State and USTR of ways this case could be resolved quickly, but they have demonstrated that there is not an interest to resolve it quickly.

The appeal, that came up in the first panel. The ombudsman was put in place to prevent appeals in tax cases, but ours was a constitutional court case. So, therefore, there was no—they did not have to go through the ombudsman in order to appeal the constitutional court ruling. We tried to incent the Peruvian Government not appeal the constitutional court ruling. Through Ambassador Struble we sent the message that we would be willing to forego the

interest payments that we would be owed if they did not appeal to enable a more rapid solution and resolution of the case, even knowing that ultimately the resolution may be against us, and yet they chose to appeal it anyway.

Mr. MENENDEZ. How much money would that have been?

Mr. DRESNER. $8 million in interest payments.

Mr. MENENDEZ. You were willing to forego $8 million without knowing the result, and yet the Peruvian Government said no?

Mr. DRESNER. Correct. One of the things that I have mentioned before is there are two actions against Engelhard here. There is an administrative action for the $30 million in the tax case; there are criminal charges against the father and son that ran our office in Peru. I wish I could bring them before you, and you could see how their lives have been ruined by this. The father is extremely ill now, suffering from a number of stress-related ailments. They have been threatened. His wife, the mother of the son, has been threatened on telephones, in mailgrams, and things and such to stop interfering with the United States Government. Many people in the business community have asked us, Why don't you just walk away from the money? We might if it wasn't for the fact that we have two innocent employees who face some serious consequences. And that is why we have always said satisfaction to us is threefold: It is, drop all the criminal charges. There is no evidence there against those people. Clear the company's name—we have done nothing wrong—and then return the money. We have offered to negotiate a settlement with them on many occasions. They have not been willing to come to the table. We have offered to enter into a long-term repayment plan if they couldn't write a check for $30 million had we been found innocent. Guaranteed as our refunds were by instruments such as letters of guaranty to ensure, if there was an unstable government, that we would still be entitled to repayment. They have not been willing to come to the table to talk about those things.

Mr. MENENDEZ. It seems to be an extreme set of reasonable circumstances to offer to forego interest without knowing the results, maybe get ruled against and still have a Government that says no. Let me ask a final question here. SUNAT, now, that is not a court. Right?

Mr. DRESNER. Correct.

Mr. MENENDEZ. It is a governmental agency?

Mr. DRESNER. Correct.

Mr. MENENDEZ. So when I hear about this alleged, you know, we are going to go ahead and yet you want us to interfere with our courts, this is a governmental agency that arbitrarily capriciously, and, as I said, I think it is a rogue agency, acts in a way in which it is not interfering with the court. It is a governmental agency who has by every mode and design sought to avoid the enforcement of what the Peruvian courts have done. Is that a fair assessment?

Mr. DRESNER. Yes.

Mr. MENENDEZ. Would the rest of you say that is a fair assessment?

Mr. MURPHY. I would say that we have had numerous reports in talking to companies over the past few weeks and indeed the past couple of years. What you see again and again is SUNAT's failure

to comply with its own timelines, times when the law lays out procedures which SUNAT has then not followed, so that they are not complying with the Peruvian law. And we hear that from company after company.

Mr. FARNSWORTH. And if I might, Mr. Menendez, add one additional comment to what has already been said. There is an institutional, let me use the word "bias," when a judgment comes down in favor frankly of a U.S. company and it is an opportunity to say, okay, this case is resolved, it is closed, it is done, it is finished, judgment is there. SUNAT has on numerous occasions then appealed that favorable decision to extend the case further, extend the legal fees further, extend the lack of judicial redress further. So that is simply one additional element. But there just seems to be no culture of concluding these cases and actually moving them toward resolution with goodwill.

Mr. DRESNER. Mr. Chairman, if I may. In our case, the Superior Court is waiting to decide on the appeal, SUNAT's appeal of our constitutional court action. It is within the Superior Court's power to order the settlement, but it is also in the Superior's Court's power to return it to square one, where it was in February 1999, which would put it right back at SUNAT.

Mr. BALLENGER. I go back to the judicial system there. Who invented SUNAT? Is that some legislative body put that together?

Mr. DRESNER. I think SUNAT was created by the Congress, but I can't be sure of that. It is the equivalent of our IRS.

Mr. MENENDEZ. Thank you, Mr. Chairman.

Mr. Ballenger. Mr. Weller.

Mr. WELLER. Thank you, Mr. Chairman. And this has been a useful hearing for me, and I want to thank you, Mr. Chairman and Mr. Menendez, for having the leadership to convene this hearing today. And you know, I look at our friends in Ecuador and Peru, they are both democratically-elected Governments. I have great respect for President Gutierrez, President Fallado, and their respective elected Congresses, and our countries have a lot of cooperative efforts, particularly in the area of narcotrafficking, which is a source of funding for terrorism not only in our own Hemisphere but elsewhere, and we appreciate that partnership. But this hearing here, I think, illustrates a real concern that those of us who are advocates of a free trade agreement with Peru and Ecuador feel must be resolved prior to the Congress considering any trade agreement with our two friends.

With regard to Ecuador, Mr. Murphy and Mr. Farnsworth, both of you mentioned that a senior Ecuadorian official suggested Ecuador might not comply with the terms of the United States-Ecuador investment treaty, and international arbitral judgments have been disavowed.

Further troubling is Ecuador's move to terminate a contract with Occidental, the largest foreign investor in Ecuador, for what appears to be baseless reasons.

Would you assess the situation in Ecuador as getting worse in terms of encouraging foreign investment?

Mr. FARNSWORTH. I would.

Mr. WELLER. Do you believe the Government of Ecuador is serious about maintaining its current trade commitments, moving forward in the free trade agreement process?

Mr. FARNSWORTH. I would say certain parts of the Government are and others are not. I think that was addressed a little bit in the previous panel with regard to—and I don't try to assign motivations to anybody in particular, but political processes and potential for higher office and things like this tend to perhaps weigh in in terms of some of these issues.

But there are certainly some very fine members of the Ecuadorian Government who are trying to do the right thing. But it is a country that has other people in the Government, and outside certainly, who have perhaps personal agendas or other agendas. We are trying to work with the people who are responsible, who understand the issues. I believe President Gutierrez and, in Peru, President Toledo have been outspoken in their desire to get these things resolved.

As Mr. Menendez has said, in Peru, it is a matter of the SUNAT issue and who is controlling it and who does it speak for; and you have a similar, although not exactly the same, situation in Ecuador where you have the Attorney General's Office essentially has been very active.

Mr. WELLER. Returning to the focus on Ecuador, Mr. Murphy, do you have something to add?

Mr. MURPHY. It is always very alarming when a senior Cabinet officer makes a comment such as that. It sends a chilling signal to the entire business community. And where you have other cases going on where a binding arbitration process has unfolded and has been given a ruling, and it is not complied with, again, it sends a chilling signal. We have seen a number of those instances now.

Mr. WELLER. From the sense of your members, the Council as well as the Chamber, the members who do business in Latin America, would you say their assessment would be to discourage their associates and colleagues in business from investing in Ecuador and Peru at this stage because of this issue of outstanding dispute resolutions?

Mr. FARNSWORTH. It certainly factors into their discussion; there is no question about it.

I would also put it in the context, a couple of countries in the region that are doing this right. Chile. Chile has a free trade agreement and has stayed true to its international commitments. Chile has proven to be a successful trade partner with the United States and, frankly, with other countries, and where, despite the size of the Chilean economy, investment is booming.

Colombia has been mentioned.

Absolutely, in the global economy with a fixed pool of capital, the countries that are trying to do the right thing to attract that capital are winning. The other ones are falling further and further behind.

Mr. WELLER. How do you feel—with the outstanding disputes waiting to be resolved and the need for a fair and transparent and timely resolution of this process, how do you feel it factors into the existing negotiations that we currently have?

Mr. FARNSWORTH. With regards specifically to Peru and Ecuador, I think this needs to be taken into account. I think we need to determine, once the negotiations have been concluded, where the countries are with respect to these other issues.

There is no question about it, the determination needs to be made whether the countries—having signed agreements with the United States—will be able to meet their obligations under these agreements. I think that is the political judgment that needs to be made.

It is premature to speculate on that because some of these things could be resolved very quickly. I think it is something that needs to be taken into account.

Mr. WELLER. We have used our negotiations with our friends to reach agreements, particularly in areas such as intellectual property rights, in the past, where we have come to terms and agreements have been honored.

Do you feel that the issue of dispute resolution and resolving these should be considered part of that process in a similar way.

Mr. MURPHY. I think back to the CAFTA negotiations in the final stage when the Government of Costa Rica was refusing to put telecommunications and insurance on the table. Consequently, USTR decided to close the deal with four countries. A month later, Costa Rica was back and was willing to make the necessary commitments.

I think that shows USTR's resolve.

As Eric says, I think it is too early to make a final determination about these countries' suitability to be included. The process that you all are engaging in here is what we applaud here today. The Congress and USTR, our very able Ambassadors, Kinney and Curt Struble in Lima, we need to keep the pressure on here because a number of these disputes can indeed be resolved in short order.

Mr. WELLER. Let me just close by asking this question of Mr. Murphy and Mr. Farnsworth, and I say this again as a Member of Congress who wants a trade agreement with our friends in Peru and Ecuador.

As you have noted, the Government of Colombia has worked to resolve this issue in a way that has been respected by all parties and is accepted by all parties, whereas obviously today we are discussing concerns about Ecuador and Peru and the lack of resolution, some have suggested detaching Peru and Ecuador from the trade agreement, moving forward with Colombia and setting aside Ecuador and Peru until this issue is resolved.

I am wondering what is the viewpoint of your two organizations on that suggestion?

Mr. MURPHY. I think it is too early to make that decision. But the fact that, for other reasons, that has been done before, I think sends a clear signal.

I think one of the ironies here that we see with our membership is that many of the companies involved in these disputes are the most natural supporters of a free trade agreement. A number of them have faced cases before SUNAT in Peru; they have privately said to me, described a free trade agreement would be good for Peru, would generate additional economic growth, it would create

more business for us; we are the natural champions of this free trade agreement.

It is a very difficult situation.

Mr. WELLER. Do you concur, Mr. Farnsworth?

Mr. FARNSWORTH. I do, and associate myself with those comments.

I would also echo the recent remarks of Deputy USTR Peter Allgeier, who said, There should not be things in a negotiation that would unfairly impinge on the ability of Colombia to move ahead. Colombia is trying to do the right things under some very difficult circumstances. President Uribe has already been mentioned, and I would concur with that.

If the other countries are able to enter into an agreement and meet their obligations within the international context, then fine. Our preference is to have a broader agreement. If that becomes problematic, there is no reason to negatively impact the Colombians for something, frankly, that somebody else has done.

Mr. BALLENGER. If I may just interrupt quickly, if all of the trade agreements that have come through, if any one of them had had this $300 million hanging over its head, it would never had gotten through this body.

I told the Foreign Minister this and the Trade Representative for Ecuador, as far as I could see, there was not a snowball's chance in hell of its getting through here unless they clean up their mess.

Talk about CAFTA, suppose somebody in that group, as backward legally as those two countries, we have enough problem, much less try to pass something where you are dealing with a bunch of crooks. That is a completely unbiased statement.

I would like to thank you gentlemen for appearing here. It might have been interesting to have a little bit of your statements before the first panel. You had some information that might have made it a little more difficult for the first panel to leave as peacefully as they did.

Mr. MENENDEZ. I tried not to allow it to be too peaceful.

Mr. BALLENGER. Let me thank you all for coming.

[Whereupon, at 4:50 p.m., the Subcommittee was adjourned.]

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