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Ecuador: Investment Climate Comparison Study

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1.0 INTRODUCTION

1.1 Background and Scope of Work

This study was conducted by Nathan Associates Inc. as part of the Latin American/Caribbean Trade and Investment Development Project (LAC/TI), under contract to the U.S. Agency for International Development (A.I.D.), in response to a request from the USAID Mission in Quito, Ecuador.

Conceptualized and supervised by the Office of Trade and Investment in A.I.D.'s Latin America/Caribbean Bureau (A.I.D./LAC/TI) in Washington, D.C., the LAC/TI project's overall goal is to foster economic integration in the Western Hemisphere and promote an open trade environment through stimulating and supporting market opening initiatives and enhancement of trade and investment regimes toward international standards through A.I.D.-assisted programs. The project staff and affiliated technical consultants provide technical expertise and assistance to identify and propose remedies to tariff and nontariff barriers to expanded trade and investment, focusing on legal and regulatory constraints that inhibit such trade and investment. The LAC/TI project makes available technical expertise and services to A.I.D./Washington and A.I.D. missions and representative offices abroad and to governments and their agencies in the region. It also provides recommendations to A.I.D./Washington on programs of bilateral assistance. Through the LAC/TI project, A.I.D. and Nathan Associates are playing an important technical support role in the liberalization of trade and investment in the Americas. The lessons learned will be useful for similar future efforts in other regions.

USAID/Ecuador, through A.I.D.-LAC/TI in Washington, requested an investigation and analysis of the climate for foreign direct investment—in particular, laws, regulations, policies, and practices—in Ecuador, Chile, Colombia, and Costa Rica. Specific elements of the study were to include (1) analyzing the legal framework or regime for foreign investment in Ecuador compared with that in the other countries, in order to identify deficiencies inhibiting such investment; (2) comparing investment incentives in Ecuador with those of the other countries (particularly tax inducements, labor assistance, and foreign exchange provisions); (3) assessing comparative political, economic, and other risks to investment in the countries studied; and (4) identifying areas in which Ecuador has had or could have a comparative advantage likely to attract foreign investment.

The study involved (1) marshalling, in the United States and in the field of documentary information, of facts and figures relevant to the study; (2) review and analysis of all relevant laws, regulations, policies, and governmental practices affecting foreign investment; and (3) personal contacts and extensive interviews with U.S. Government personnel in the region (specifically USAID mission staff and Foreign Commercial Service officers), local government officials, and individuals—local and expatriate—involved in business or professional services that support foreign investment. In all, some 94 individuals in four countries were interviewed for the study.

A thorough understanding of the basic concepts relating to FDI (definitions, legal framework, basic investment issues, types of FDI regimes, reasons for FDI, incentives and disincentives, investor concerns, and FDI standards) is essential to comparing FDI in the countries included in this study. A comprehensive background discussion of FDI concepts is given in Appendix A.

Basic comparative statistical information developed for this study for the four countries surveyed is set forth in detailed, aggregate form in Appendix B, Tables B-1 to B-4.

Table C-1 in Appendix C is a comprehensive comparison of the FDI regimes in Ecuador, Chile, Colombia, and Costa Rica. Table C-2 is a comparison of the international trade and investment arrangements to which the countries studied are parties.

Appendix D is the statement of work for the study. A list of individuals interviewed for this study is given in Appendix E. The documents reviewed in preparing this study are listed in Appendix F, and Appendix G gives brief biographies of the authors of the study.

1.2 Summary and Recommendations

This study was conceptualized to answer for the Ecuadoran government the question "Why are foreigners investing in Chile, Colombia, and Costa Rica, but not in Ecuador?" The study compares the foreign direct investment (FDI) regimes of the four countries and attempts to draw conclusions and make recommendations for Ecuador.

Chile, which currently has one of the most dynamic economies in South America, has the most complex FDI regime of the countries studied, as well as the highest level of FDI. Under its Foreign Investment Statute, investors are not legally required to seek approval for their investments, but, if they do so and enter into a formal "foreign investment contract" with the government's Foreign Investment Committee, the government guarantees them that

the "rules of the game" regarding admission/approval, national treatment, taxation, and repatriation of profits and capital will not change during the term of the investment. The agreement guarantees investors national treatment and free access to the formal (banking system) exchange markets and free remission of profits and capital after payment of applicable taxes. Moreover, the agreement permits investors to avail themselves of an "invariable" income tax rate for 10 years from commencement of operations instead of any otherwise applicable standard income tax, unless the investor opts (on a one-time-only basis) to be covered by the latter. Chilean corporate income is taxed at 15 percent and remitted profits are taxed at an additional 35 percent rate. Chile's constitution expressly forbids uncompensated expropriation and provides for judicial review of payment issues. Chile limits positive investment incentives for general industrial development to exemption from its value-added tax (VAT) on imports and fixed rate guarantees for import duties on imports of machinery and equipment. However, it grants more extensive incentives targeted in certain geographical areas or industrial sectors. These sectors include remote industrial areas that receive exemption from or reduced income taxes as well as from VAT and customs duties. Operations in two remote free trade zones (FTZ) are exempted from all income and value-added taxes. Chile's sectoral incentives are targeted at forestry and certain extractive industries. It grants a one-time-only "bonus" or subsidy of up to 75 percent of the costs of forestry planting, while 50 percent of related revenues are deemed tax exempt. Mining concessions are granted under contracts with the presidency that may provide concessionaires with a reduced income tax rate and waive payment of most other taxes or customs duties.

Historically, Colombia has tended to regulate FDI as an aspect of its foreign exchange regime. Like Ecuador, in addition to its own laws and regulations, as a member country of the Andean Pact, Colombia's FDI regime reflects basic principles of Decisions 291 and 292 of the Andean Pact. Colombia's International Exchange Statute and International Investment Statute require the advance approval of its National Planning Department only for investments related to public services, nontoxic waste disposal services, and all insured investments (Overseas Private Investment Corporation [OPIC], Multilateral Investment Guarantee Agency [MIGA]). FDI is prohibited in national security and defense areas and in industries dealing with toxic wastes. Colombia's National Social and Economic Policy Council (CONPES) may prohibit or restrict FDI in other sectors. All FDI must be registered with the Central Bank, and capital or profits arising from nonregistered investments may not be transferred from Colombia. The Colombian constitution and the Exchange and Investment Statutes operate to guarantee national treatment to FDI and foreign investors. Corporate income is taxed at a 37.5 percent effective rate, and remissions of regular income and capital gains from FDI are taxed at 12 percent, a rate that will

be gradually reduced to 7 percent by 1996. Colombia has no recent history of expropriation, and the constitution requires prior payment for any expropriation. However, a 1991 amendment to the constitution appears to permit uncompensated administrative expropriation without judicial recourse if acquiesced by one house of the Colombian Congress, a development that led Britain to refuse to sign a recently negotiated bilateral investment treaty with Colombia and to protests from the Japanese ambassador. Colombia provides few positive investment incentives but has incentives for FTZ operations and FTZ-like technology and tourist zones that exempt export-related (or technology- or tourism-related) income from taxation and provides reduced import duties on certain vehicles.

Costa Rica has no legislation dealing specifically with FDI. Its constitution guarantees foreigners national treatment. FDI registration requirements were eliminated in 1992 (except for incentives qualification), and there are no present restrictions on repatriation of capital or conversion of local currency for remission abroad. Investors wishing to receive positive investment incentives for tourism, export production, or FTZ activities must have their FDI approved in advance and register their investments with the authority that administers incentives. Foreigners are forbidden to own beaches or to own or operate medical services or radio and television stations. Costa Rica "reserves" certain banking, insurance, petroleum, and utilities operations to the state subject to concessions. Corporate income taxes range from 10 to 30 percent depending on level of income, and there is no tax on remissions of profits or repatriation of capital, although remittances for royalties, salaries, or services are subject to withholding rates of 5 to 50 percent. Costa Rica's constitution prohibits uncompensated expropriations, but in fact seven cases of expropriation remain unsettled between Costa Rica and the United States. Positive investment incentives were developed in 1984 and later to cover export production and tourism development. Export production incentives involve both FTZ and temporary importation for processing operations (maquilas). FTZ operators are exempt from import duties and foreign exchange controls and are exempt from all income taxes for 8 years and from 50 percent of income taxes for another 4 years. For export production, import duty exemptions are offered in proportion to the amount of final product exported. Tourism incentives offer duty-free importation of capital goods not otherwise available in Costa Rica as well as a 50 percent exemption for tourist-related income, but these incentives are being phased out.

Ecuador has made significant, even dramatic, progress in liberalizing its FDI regime, as part of the Durán-Ballen Administration's overall economic policies and modernization thrust and in response to advocacy and suggestions of private sector organizations such as the Fundación Ecuador. The govern-

ment initiated administrative and legislative action in 1993 that now makes Ecuador's FDI legal and regulatory regime the most open of the four countries included in this study, theoretically if not necessarily yet in practice. It has eliminated most requirements for prior government authorization of FDI, opened up previously restricted sectors to FDI, and eliminated discriminatory taxation on profits remissions and repatriation of capital in a completely free foreign exchange regime.

Ecuador's problem is that the country has a relatively small, stagnant economy and so many disincentives or contraindications for investment—local or foreign—that there is not yet a basis for investor confidence that Ecuador is an inviting place for FDI. This is because, although its new government has undertaken reform and restructuring initiatives and tried to enhance its business and investment climates, Ecuador has made little real progress in reducing or ameliorating the negative impacts of its structural and other disincentives for investment. Ecuador still lags well behind most of South America—and certainly its major rivals for new FDI—in macroeconomic reform, restructuring, and overall economic growth and stability.

Although considerable official and private sector rhetoric has been devoted to the need for incremental FDI, the Ecuadoran government still has no proactive, aggressive, effective overall policy or strategy for promoting and facilitating FDI. The policy initiatives it has undertaken or attempted are frustrated by political paralysis, a complex and relatively outdated legal and regulatory system, lack of coordination and cooperation among various sectors of government, and a continuing proclivity by its bureaucracy toward complication, confrontation, and delay—not to mention outright corruption—in nearly every interaction with the private sector.

Ecuador's many general disincentives to new investment—domestic or foreign—as revealed in interviews with more than 45 individuals in Ecuador, include exchange rate volatility, a bloated public sector and high public deficits, inflation, a massive external debt overhang, significant government control of or intervention in the economy, scarcity of private investment financing, persistent infrastructural inadequacies, an officious bureaucracy, and an essentially antientrepreneurial labor regime. Disincentives specifically affecting FDI include property rights problems, continuing sectoral exclusions or restrictions, bureaucratic violations of the principle of national treatment, and lack of adequate intellectual property rights protection.

Ecuadoran public officials, and some in the private sector, appear in their expectations and policy formation to have confused "openness" (on paper) of their FDI regime with "attractiveness" of their country for new FDI. In reality, Ecuador's FDI legal and regulatory regime reflects an attitude and policy of

total "neutrality" toward FDI under which foreign investors are (or are supposed to be) treated the same as domestic investors. Vastly more important, however, in FDI decision making is investor confidence in a nation's economy and in the governmental and political systems that manage it. In comparison, even though Chile and Colombia have more complex FDI admission/approval procedures and even some remaining restrictions or taxes on profits remissions, prospective foreign investors have confidence in their dynamic, growing economies and in their legal and regulatory and political systems, believing their government's assurances that the rules will not change after their investment.

Moreover, although it has substantially simplified its FDI legal and regulatory regime, Ecuador still does a minimally effective job of promoting FDI either internally or externally. It has many agencies and officials with responsibilities related to trade, investment, and tourism, but which apparently accomplish little and seem either unwilling in or incapable of productive coordination or cooperation.

It is important to recognize, however, that the liberalization of Ecuador's FDI legal and regulatory regime has had less than a year of implementation and little time to produce definitive results. In addition, the Durán-Ballen Administration appears to recognize why the general and specific disincentives described herein inhibit FDI and has acted or attempted to deal with a number of them. In both Decree 415 of January 8, 1993, and in the draft Modernization Law (principally for privatization) pending before the Ecuadoran Congress, Ecuador has taken aim at eliminating problems in the bureaucracy. The country just recently signed both a bilateral investment treaty and an agreement on intellectual property rights protection with the United States and is negotiating an Ecuador-U.S. double taxation treaty. It has attempted to rationalize government FDI promotion in Decree 459 of February 2, 1993, by establishing the National Coordinating Committee for the Promotion of Exports and Investments (CONAPEI).

Positive investment incentives explicitly favoring FDI are inconsistent with Ecuador's overall policy of investment neutrality and may even be unconstitutional. However, Ecuador has already experimented with positive investment incentives applicable to all investors, local and foreign, and has phased out or is phasing out most of them. Indications are that generic positive incentives designed to stimulate and support industrial development and employment have been ineffective. The government's elimination of such incentives appears warranted in that incentives that seek to create artificial, market-distorting (and essentially nonstructural) competitive advantages are not desirable in a free market economy and are resented by other nations in competition for new FDI. But Ecuador is not precluded from appropriate positive incentives in sectors specific to its resource endowments and that basically do not yet have a competi-

tive market to distort, for example, natural resources and tourism.

This study propounds certain recommendations for both the Government of Ecuador and the U.S. Agency for International Development. Its recommendations for the Government of Ecuador recognize that some may be feasible in the short-term (e.g., non-legislative initiatives that can be implemented within a year or less), whereas others are feasible, given economic and political realities, only over a longer period (medium-term actions). This report makes recommendations for the Government of Ecuador on the general FDI regime, macroeconomic policy reform, government bureaucracy, infrastructure and productivity, labor regime reform, intellectual property rights protection, trade-related measures, and tourism. Our recommendations to A.I.D. are intended to suggest areas or programs wherein A.I.D. (through USAID/ Ecuador) can provide encouragement and support to the Ecuadoran government to undertake and implement our recommendations.

Major study recommendations include

- Establishment of a "one-stop-shop" (or "Ventanilla Unica") to coordinate Government of Ecuador FDI policy and promotion programs and provide FDI-related services.

- Analysis of Ecuador's basic comparative advantages and development of an Ecuador FDI promotion strategy.

- Establishment of a mixed public-private FDI Promotion Commission addressing <u>only</u> FDI and establishment of bi-national private sector working groups with the private sectors of major investing nations.

- Enactment of a unified Foreign Investment Code.

- Granting to FDI of investment regime guarantees against changes in FDI "rules of the game."

- Abolition of remaining sectoral and geographic restrictions on FDI.

- Enactment of the government's Modernization Law initiative.

- Reform of the bureaucracy, including creation of a professional, career civil service and enactment of an anticorruption law.

- Infrastructure and productivity enhancement.

- Labor regime reform.

- Ecuador's accession to the General Agreement on Tariffs and Trade.
- Development of a national tourism development policy and strategy.
- Privatization of tourism promotion and development.

2.0 FOREIGN INVESTMENT: BASIC CONCEPTS

2.1 Definitions/Concepts

A full treatment of the basic concepts underlying foreign investment is given in Appendix A. Investment, whether originating domestically or from abroad, is divided into two basic types: "direct investment" and "portfolio investment." "Direct investment" describes an investment made to acquire and manage a continuing interest in the target entity. When the entity is located in one country and the investor is located in another country, the investment is referred to as "foreign direct investment." Ownership of less than 10 percent of an entity is referred to as "portfolio investment" and generally implies an essentially passive interest only in the earnings potential of stock in the firm.

The legal context or framework within which FDI is admitted and regulated in a country is known as the "FDI Regime" and includes the whole array within that country of constitutional provisions, laws, regulations, policies, and practices that, taken together, specifically establish and define the rights and obligations of both the foreign investor and the state with regard to FDI.

In many countries, an effort has been made to codify and encapsulate in a single body of legislation and implementing regulations the nation's basic provisions on the admission and treatment of FDI, known as "investment codes."

There are two main types of investment codes, open investment regimes and authorization/approval regimes. Within the latter type are two identifiable subtypes.

3.0 ECUADOR: THE LEGAL FRAMEWORK FOR FDI

3.1 Recent History of Ecuador's FDI Regime

Before the incorporation of Andean Pact Decision 24 into Ecuadoran law, FDI in Ecuador was governed only by certain foreign exchange provisions. The rules of Decree No. 239 and Resolution No. 555 of the Monetary Board in 1970 were the principal channels for regulation. Under these provisions, the entry of foreign capital into the country required registration with both the Monetary Board and the Central Bank that included a detailed description of the contemplated investment and documentation on the entity in which such investment was projected. The Exchange Department of the Central Bank evaluated the proposed investment, and authorization was issued by the General Manager's office. Incoming FDI was also subject to collateral regulation under the Companies and Banking Law with regard to specific aspects of oversight and control of corporations and foreign banks or local banks with FDI.

Under the foregoing norms, investments were accepted in exchange that had to be sold to the Central Bank as well as in machinery and equipment whose irrevocable importation into the country was manifested by customs receipts. FDI was permitted in both existing and new entities. Although there was a right to repatriate capital and remit earnings abroad, there were "temporary" limits on the export of capital abroad to the effect that such remissions abroad could not occur before 5 years after registration of the investment with the Central Bank.

In December 1970 the Commission for the Treaty of Cartagena approved Andean Pact Decision 24 entitled "The Common Regime for the Treatment of Foreign Capital and Trademarks, Patents, Licenses, and Royalties," which effected a substantial modification of Ecuador's FDI regime and which was implemented in Ecuador through Supreme Decree 974 of June 30, 1971. Ecuador's application of Decision 24 responded to its need and desire to achieve a degree of control and orientation for FDI toward certain priority sectors, in particular in its border areas. However, implementation of Decision 24 was not seen as an attempt to repel FDI. Rather, Decision 24 included an affirmative declaration that FDI was good for the Andean Region and contributed effectively to the development plans and goals of the nations of the region.

Decision 24 contained a number of norms that included (1) the requirement for prior authorization for both original FDI and the reinvestment of earnings; (2) a progressive national participation requirement of at least 51 percent local ownership of the capital of the enterprise; (3) regulations affecting industrial

property rights; (4) requirements affecting technology transfer; and (5) regulations governing transfers of capital abroad for loan repayments, interest, royalties, and repatriation of profits.

During the early 1980s, as a result of the debt crisis, Andean governments concluded that the interruption of capital flows from abroad and the consequent scarcity of foreign exchange required a change of attitude toward FDI. Decision 24 was, in effect, repealed and a new Common Regime was adopted for FDI. Ecuador implemented changes to the legal approval process in 1984. In May 1987 the member countries of the Andean Pact approved Decision 220 to succeed Decision 24. In March 1991, Decision 220 was substituted by Decision 291, which remains the pact's basic internal regime for regulation of FDI.

3.2 Ecuador's Current FDI Regime

The current complex of laws and regulations that form the specific legal and regulatory regime in Ecuador governing FDI and foreign investors consists of the following:

- Decisions 291 and 292 of the Commission of the Treaty of Cartagena, as they have been applied within Ecuador by an executive decree
- Ecuadoran Political Constitution of 1984
- Decree No. 415 of January 8, 1993, establishing regulations for the implementation of Andean Decisions 291 and 292
- Capital Markets Law of May 6, 1993
- The recently signed Bilateral Investment Treaty with the United States

3.2.1 Constitution of Ecuador

The Ecuadoran constitution establishes the organic basis for the Ecuadoran state and its system of law. Article 14 of the Constitution provides that "foreigners shall enjoy, in general, the same rights as Ecuadorans within the limits established in the Constitution and the law."

Article 18 of the constitution provides that foreigners may not directly or indirectly acquire real property in the frontier zones or in certain "reserved" areas except as specifically authorized by law. Article 46 provides that there are four basic sectors of the Ecuadoran economy: (1) the public sector, composed of state enterprises; (2) the mixed economy, composed of certain private entities "in an association" with public sector

enterprises; (3) the community sector, consisting of certain cooperative enterprises; and (4) the private sector, formed by all other nonenumerated entities. Article 46 also provides that certain areas of economic exploitation are reserved to the state, including natural resources; public utilities (water, electrical energy, and telecommunications); and certain "strategic enterprises" as defined by law, but that the State may, in exceptional cases, delegate the exercise of any such activities to "private initiative."

Article 47 provides that the public sector, "for purposes of social order" and subject to the procedures and forms of payment provided by law, may (upon prior just compensation) nationalize or expropriate property and activities that belong to other sectors. The articles also declares that "all confiscation is prohibited."

Finally, Article 48 of the constitution provides that private property, in any form, constitutes a right recognized and guaranteed by the state "as long as it complies with its social function."

3.2.2 Andean Investment Code

The Andean Investment Code consists of two decisions of the Commission for the Treaty of Cartagena, the organic structure for the Andean Pact: Decision 291, "On the Common Regime for Treatment of Foreign Capital and on Marks, Patents, Licenses, and Royalties," and Decision 292, "Uniform Regime for Andean Multinational Enterprises," both of March 21, 1991.

Article 1 of Decision 291 defines foreign direct investment as follows:

> [C]ontributions, proceeding from the exterior, of property of foreign natural or juridical persons, to the capital of an enterprise, in freely convertible cash or real or tangible property such as industrial plants, new and reconditioned machinery, new and reconditioned equipment, parts and spare parts, raw materials, and intermediate products.

Also considered FDI are investments made in local currency derived from resources entitled to remission abroad and reinvestment of earnings made in conformity with the Decision 291 regime. Article 1 defines a "foreign investor" as the "owner of a foreign direct investment."

Article 2 of Decision 291, entitled "Rights and Obligations of Foreign Investors," provides that "foreign investors shall

have the same rights and obligations to which national investors are subject except as provided in the legislation of each member country." Article 3 requires all FDI to be registered in freely convertible currency, by the appropriate national agency of each Andean Pact member country.

Article 4 provides that "owners of a foreign direct investment . . . shall have the right to transfer abroad in freely convertible exchange, under terms provided for in the legislation of each member country, the net documented profits arising from their foreign direct investment." Article 5 states that foreign investors "shall have the right to re-export amounts obtained from the sale within the country of their shares, participation, or rights or upon the reduction of capital of or liquidation of the enterprise, upon prior payment of the corresponding taxes."

Article 6 provides that "registered capital" shall constitute the amount of the initial foreign direct investment plus subsequent increases therein and reinvestments actually realized and registered less net losses, if any. Article 7 provides that reinvestments shall also be considered FDI, subject to the same norms established therefor in Article 3. Finally, Article 10 states that disputes arising out of any FDI shall be resolved by member countries by applying the provisions of their internal legislation.

3.2.3 Decree 415

Decree 415, of January 8, 1993 (R.O. No. 106, Jan. 13, 1993) was issued by Ecuador's new Durán Ballen administration ". . . to promote foreign investment in the country, with the same rights of and equal treatment to national investment, in accordance with that prescribed in the State's Political Constitution." The new decree supersedes and substantially liberalizes earlier Decree 2501, of June 17, 1991, of the Borja administration, which incorporated Andean Pact Decisions 291 and 292 into Ecuador's FDI regime. Decree 415 institutionalizes the principle of national treatment for FDI, eliminates (arguably) a number of sectoral restrictions on FDI, and eliminates (at least in part) requirements for prior Government approval for FDI.

3.2.4 Stock Market Law

Although principally constituting an organic law and framework of regulation for financial markets, the Ley de Mercado de Valores (Stock Market Law) of May 6, 1993 (Supplement to R.O. 199, May 28, 1993, p. 3 et seq.)contains certain provisions that

eliminate further restrictions on FDI--in particular, the prior approval requirement and taxation of remitted profits.

Admission/Approval. Article 5, Decree 415, January 8, 1993, provides that "foreign direct, subregional [e.g., Andean Pact], or neutral investment may be made in all economic sectors without prior authorization of MICIP, under the same conditions in which it may be made by Ecuadoran natural or juridical persons."

Ecuadoran authorities assert that Article 5, when read with Article 6 of the decree, effectively eliminates the requirement of prior approval by MICIP. But Article 6 can be read as actually retaining legal authority to require approval while removing the exercise of administrative discretion with respect thereto and eliminating delays therein. Article 6 provides that

> The Ministry of Industries, Commerce, Integration and Fisheries (MICIP), shall authorize, at the time of presentation, every application for the transfer of shares or participation within the terms of Article 22 of the Companies Law, without necessity of any requirements whatsoever.

Article 22 of the Companies Law required MICIP authorization for acquiring stock in Ecuadoran investors by foreign investors; that is, "the cession or transfer of common stock and shares in companies from nationals to foreigners or between foreigners, may not be effected without authorization of MICIP." Decree 415 also lifts prior inhibitions or conditions to investments in Ecuador by Ecuadoran subsidiaries of foreign companies. Paragraph 3 of Article 13 provides that "foreign companies according to the definition found in Decision 291 require no prior authorization to invest in Ecuador."

Although none of the foregoing provisions of Decree 415 refers specifically to unincorporated branches of foreign companies, Article 5 appears to include branches within its context such that FDI through branches may also be effected without prior authorization of MICIP. Any remaining concerns about the prior approval requirement, however, were removed by Article 74 of the Stock Market Law of May 6, 1993, which amended Article 22 of the Companies Law to read "Foreign investment that occurs in corporations and other entities subject to the control and oversight of the Superintendent of Companies shall not require any prior authorization of any agency of the State."

When Decree 415 was published in Ecuador's Official Register, local press accounts reported enthusiastically that it opened up the Ecuadoran economy "without any prohibitions on foreign capital" and that "foreign investments could be made freely in all economic sectors." According to El Universo,

> As reported, among the most essential rules contained therein, the new regulation . . . includes elimination of every type of restrictions on foreign investments.
>
> Prior legislation said that foreign direct investment . . . could not be realized in the following sectors: defense and national security; radio, television, press, and other sectors provided for in special [e.g., sector-specific] laws, such as commercial banking, insurance, reinsurance, and financial companies.

The then-minister of MICIP was quoted in El Comercio as saying, "From today on, Ecuador eliminates all restrictions that existed for the contribution of foreign investment in sectors like public services, commercial banking, insurance, and finance companies."

Nevertheless, there apparently is a legal issue as to the scope of the decree and whether it does—or could—eliminate such sectoral restrictions on FDI. Whereas Decree 415, as an executive decree, deals with FDI admission generally, it is presumably inferior in status, in a constitutional sense, to "laws" or "statutes" (enactments of the Congress) that deal with FDI on a sector-specific basis. Therefore, there is a question of whether the decree can effect changes in statutory law or amend or repeal inconsistent existing laws. In this regard, some Ecuadoran laws prohibit or otherwise restrict or regulate FDI—and in some cases all private investment—in certain strategic or economic sectors.

Article 46 of the constitution specifies that water, mining, electricity, and telecommunications are "reserved to the State" but that the state may delegate any of these areas to private initiative "when the law so provides" (emphasis added). Article 18 of the constitution provides that foreigners may not acquire or use property in frontier areas or "reserved areas" unless they obtain "authorization contemplated by law." The Aliens Law (R.O. 473, July 7, 1986) defines "frontiers" as areas within 50 km of any national boundary or sea coast. This overall ban is also found in Article 10 of the Mining Law (Supp. R.O. 695, May 31, 1991). Authorization may be granted only by the president, with the approval of the Joint Council of the Armed Forces. The Mining Law also opens the mining sector to foreign participation via individual concession arrangements negotiated with domestic and foreign companies by the Ministry of Energy and Mines. Under the Civil Aviation Law (R.O. 32, Aug. 5, 1970), domestic air transportation may be owned and operated only by Ecuadoran nationals or companies (defined as having no less than 60 percent Ecuadoran share ownership). Radio and television licenses may be granted only to Ecuadorans by birth under the Law of Radio and Television (R.O. 785, April 2, 1975). Exploitation of fisheries is permitted only to Ecuadoran or mixed (public and private) capital companies under the Fisheries Law (R.O. 497, Feb. 12, 1974), although the Fisheries Council established thereunder may

except fishing activities by a foreign company in certain nontraditional products.

Article 7 of Decree 415 continues the requirement for registration of every foreign direct investment (or reinvestment) with the Ecuadoran Central Bank. It clearly withdraws any exercise of discretion by bank staff by specifically enumerating the documentation required to support the registration and providing, in Paragraph 4, that "the Ecuadoran Central Bank is prohibited from asking for any other documentation apart from that expressly mentioned in this rule." Moreover, Article 19 of the decree verbalizes a particularly explicit injunction against any bureaucratic obfuscation with the FDI approval process:

> "[Neither] The Superintendent of Banks, the Superintendent of Companies, the Ecuadoran Central Bank, nor other public institutions shall demand compliance with more requirements than those contemplated in the law and this regulation for purposes of approval of the acts of companies receiving investments, or [of] their investors."

National Treatment As indicated previously, Article 14 of Ecuador's constitution provides that "foreigners shall enjoy, in general, the same rights as Ecuadorans within the limits established in the Constitution and the law." Article 2 of Decision 291 of the Andean Pact provides that "foreign investors shall have the same rights and obligations to which national investors are subject except as provided in the legislation of each member country."

The premises clause of Decree 415 specifically describes that the goal of the government in issuing that decree is " . . . to promote foreign investment in the nation with the same rights and similar treatment [accorded] to national investment." Article 5 of the decree provides that FDI may be made ". . . under the same conditions under which it can be made by Ecuadoran natural or juridical persons." Still, it is interesting to note that certain Ecuadoran citizens may be deprived, in effect, of certain civil rights by reason of their association with foreign investors. Under Article 58 of the Ecuadoran constitution, no one may be a member of the National Congress who is a legal representative or holds a power of attorney for a foreign company, nor, under Article 79, may such a person be elected president of Ecuador.

Taxation and Remission of Profits Every entity doing business in Ecuador is subject to income tax. A company is considered resident in Ecuador and, therefore, subject to taxation of worldwide income when it has been established under Ecuadoran law and has its principal base in Ecuador. Corporate entities are liable for corporate income tax on their taxable

income after deducting usual expenditures and, from profits, the 15 percent mandatory employee profit sharing. The current corporate income tax is 25 percent of taxable income, subject to full withholding.

Until May 1993 and passage of the Ley de Mercado de Valores, an additional 11 percent was imposed on profits remitted abroad, for an overall effective tax rate of 36 percent (previously 49 percent) thereon. Branches of foreign companies were taxed at the 36 percent rate with an 11 percent deduction for earnings reinvested in share capital. However, the Ley de Mercado de Valores further implemented the government's drive toward nondiscriminatory treatment for foreign investors by repealing the tax and withholding thereof on profits remitted abroad so that all companies, foreign and domestic, are taxed only at the 25 percent rate.

As a result of Decree 415 and the new Ley de Mercado de Valores, Ecuador now has one of the most liberal profits repatriation regimes in Latin America. Article 9 of Decree 415 provides that "owners of a foreign direct investment . . . shall have the right to transfer abroad, in freely convertible exchange, the net profits earned on their registered [e.g., with the Central Bank] investment."

Therefore, foreign investors are free to remit up to 100 percent of net profits (as well as the proceeds from the liquidation of their investment) without payment of any special remissions tax and without foreign exchange restrictions through commercial banks at freely determined exchange rates. Neither are there limitations imposed on outflows of funds for debt service, royalties, or payments for importations, although licensing contracts for the importation of technology and technical know-how and services must be registered in advance with MICIP. Ecuador and the United States are negotiating a bilateral agreement, expected to be signed by the end of 1993, on avoidance of double taxation.

Expropriation and Dispute Settlement Article 48 of the Ecuadoran constitution provides that "property, in whichever of its forms, constitutes a right recognized and guaranteed by the State for the organization of its economy, as long as it fulfills its social function." However, the constitution explicitly provides for expropriation under certain conditions. Article 47 provides

> For purposes of social order, the public sector, pursuant to procedures and forms of compensation prescribed by law, may nationalize or expropriate, in any case, upon just indemnization, the goods, rights, and assets belonging to the other sectors, for itself or another of the sectors mentioned.

All confiscation is prohibited.

Public entities may be authorized to expropriate property within the constraints of Article 47 by their specific sectoral laws. The Ecuadoran Civil Code recognizes a specialized legal right to litigate compensation issues, and the Code of Civil Procedure establishes a specialized procedure for a judicial determination of property value and level of compensation. Apart from this procedure, any citizen or resident of Ecuador, individual or juridical, may attack the legitimacy of any action of an agency of the Ecuadoran government in special administrative procedure courts established for that purpose and appeal decisions thereof to the Ecuadoran Supreme Court.

Article 96 of the Ecuadoran constitution provides, in pertinent part:

> [E]very administrative act engendered by the central administration, provincial or municipal [government] or whatever autonomous entity recognized by the Constitution and the law, may be impugned before the Fiscal or Administrative Litigation Courts in the form determined by law.

Article 141 of the constitution establishes the Court of Constitutional Guarantees, a tribunal with specific competency to safeguard compliance with and interpret the provisions of the Ecuadoran constitution through advisory opinions or litigation alleging constitutional violations. The court has the power to annul governmental actions that violate constitutional guarantees and suspend laws or regulations inconsistent with it; however, its actions are subject to legislative veto.

Although the U.S. Department of Commerce's Investment Climate Assessment for Ecuador (March 1993) states that " . . . there have been no recent cases of <u>expropriation</u> of foreign holdings," the report also notes that

> A major U.S. investor in the Electricity sector [Emelec case] in Guayaquil had his investment '<u>intervened</u>' by the Ecuadoran Government over a four-year period, while a process was under way to purchase the company from the investor. This 'intervention'—which impeded the remittance of profits—was not provided for in the terms of the Company's valid concession contract, and the decisions of an arbitral panel convened by the two parties were not implemented. The Durán-Ballen Government committed itself to resolving the issue promptly in a way that respected the rights of the investor. The Government's stated intention was to keep the Company in private hands rather than have it nationalized. Indeed, on January 25, 1993, the U.S. investor sold his shares in the Electric Company to a group of Ecuadoran investors, thus putting an end to a ten-year controversy.

Nonetheless, a number of business interviewees raised the issue of Emelec, concerned about the kind of signal that prior Ecuadoran governments transmitted with the pressures they were willing to apply to achieve their goal of this form of "private sector nationalization." Some of the interviewees noted that because of the "informality" of the government's pressure, it was difficult to impugn their action directly at law, raising the possibility that another government could undertake the same kind of "intervention" for the same or different motives. They were particularly concerned for the image projected by the Government's refusing to enforce adverse rulings of an arbitral panel freely chosen by the parties to the dispute.

Article 18 of Decree 415 addresses the issue of settlement of investment disputes. It provides that

> the State may submit controversies that arise in the application of the [Andean Pact Decision 291] Common Regime for the Treatment of Foreign Capital . . . to Arbitral Tribunals established by reason of international treaties to which Ecuador is a party.

Ecuador is a member of the International Center for the Settlement of Investment Disputes (ICSID), a specialized international arbitration entity established under the 1966 Convention on the Settlement of Investment Disputes Between States and Nationals of Other States (Washington Convention). The convention established rules under which investment disputes between governments or governmental entities and foreign nationals may be resolved through arbitration or conciliation. Ecuador also is a signatory to the 1958 United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York Convention) and the 1975 Inter-American Convention on International Commercial Arbitration (Panama Convention).

Bilateral Investment Treaty On August 27, 1993, Ecuador signed its first bilateral investment treaty with the United States. Ecuador has also entered into BIT discussions with France, Italy, Switzerland, and the United Kingdom. The Ecuador-U.S. BIT is the first BIT that the United States has signed with an Andean Pact member country and the second with a South American country (the first was Argentina).

The Ecuador-U.S. BIT provides a stronger legal basis than before the treaty was signed for the admission and treatment of U.S. FDI in Ecuador. The treaty's basic provisions are that

- Investments shall receive, upon establishment and thereafter, either national treatment or most-favored-nation treatment (MFN), whichever is better (subject to certain exceptions);

- Investments are guaranteed freedom from performance requirements, such as domestic content or export quotas;
- Expropriation may occur only in accordance with international law standards, for a public purpose, in a nondiscriminatory matter, under due process of the law, and upon payment of prompt, adequate, and effective compensation;
- Investments are guaranteed the unrestricted transfer of funds in a freely usable currency; and
- U.S. nationals and companies in investment disputes with Ecuador shall have access to binding international arbitration without first resorting to local courts.

The treaty guarantees investors the right to hire top management personnel regardless of nationality and guarantees that investments shall be granted "fair and equitable" treatment, prohibiting thereby the parties from impairing, through arbitrary or discriminatory means, the management, operation, maintenance, use, enjoyment, acquisition, or disposal of investment. Ecuador (like the United States) has made certain reservations to the requirement for national treatment. The reserved areas include traditional fishing (but not fish processing or aquaculture) and ownership of broadcast radio and television stations. It should be noted, relevant to the discussion of admission (see Appendix A), that Ecuador did not reserve any sectoral reservations to MFN treatment. In addition, Ecuador's membership and requirements of the Andean Pact are recognized by a provision that its MFN obligation does not extend to advantages accord to third countries by virtue of Ecuador's membership in a free trade area or customs union. (This applies similarly to the United States in the case of the North American Free Trade Agreement.)

The BIT between Ecuador and the United States is meant only to establish a floor for standards in the treatment of U.S. FDI. An investor may actually be entitled to even more favorable treatment through domestic legislation, other international legal obligations, or a specific obligation assumed by Ecuador relative to that investor. The treaty enters into force 30 days after the exchange of the instruments of ratification by the two governments and continues in force for 10 years from the date thereof. On September 10, 1993, President Clinton submitted the treaty to the U.S. Senate for ratification.

Investment Incentives Ecuador does not offer positive investment incentives limited to or directly targeted at attracting FDI, which reflects its overall policy of impartiality between and equal treatment of foreign and domestic investors. It does, however, provide certain positive investment incentives to encourage economic and industrial development.

Under the Free Trade Zones Law (Decree Law No. 1, R.O. 625, Feb. 19, 1991) and its implementation regulation (No. 2710, R.O. 769, Sept. 13, 1991), companies using the FTZ are exempted from payment of customs duties on imports of raw materials and machinery and equipment, as well as from value-added tax (VAT) transaction taxes; are permitted to export products finished or partially assembled without restriction; and are entitled to use and remit profits in freely convertible foreign exchange. Ecuador also has a recently enacted temporary importation or maquila law (Law 90, R.O. 493, Aug. 3, 1990) and regulation (No. 1921, R.O. 553, Oct. 31, 1990) to promote manufacturing, assembly, conversion, or repair of temporarily imported goods that are exported immediately after processing. The law provides that goods imported for processing are exempt from customs duties and importations for processing do not require Central Bank approval. The law also authorizes unlimited and free remission of profits to foreign investors and, like the FTZ law, permits a high degree of "flexibility" in the terms of labor contracts. Although Ecuadoran officials frequently tout the benefits and attractiveness for foreign investors of these two laws, so far the industrial FTZ has only one operating company (other than certain tourism projects described in Section 10.1), and the few companies taking advantage of the maquila law are local.

The Industrial Development Law of September 1971 (R.O. 251) provides significant tax incentives to industrial companies to encourage establishment or modernization of industries that assist in the development of Ecuador. Investments are classified under the law in various categories: Special, Class A, Class B, and the List of Directed Investments; the type of incentive depends on the category into which the investment falls. Incentives may include (1) certain exemptions, for example, from restrictions on industrial goods exported, customs duties on imported inputs, certain stamp or transaction taxes, and customs duties on imported machinery and equipment; (2) deduction from income for tax purposes of investments in buildings, machinery, or equipment for a minimum of 3 years; and (3) additional 10 years of tax incentives for investments outside Quito and Guayaquil in "listed investments" such as agro-industry, shipbuilding, and cement.

The Mining Law (R.O. 695 Supp., May 31, 1991) provides a special income tax regime, reduced taxes on capital and profits remission, and reduced customs duties and fees for imports of machinery, equipment, work vehicles, parts and spares; mineral exports are exempted from most export taxes.

Certain tourism incentives are discussed in Section 10.1. The Agricultural Development Law (R.O. 792, March 15, 1979), designed to increase production and productivity in that sector, provides exoneration from exports of nontraditional agricultural products financed in the medium to long term, as well as exoner-

ations or reductions, or both, from customs duties on imports of machinery and equipment, raw materials, and other inputs. The Fisheries Development Law (R.O. 497, Feb. 19, 1974) provides exoneration from incorporation taxes and fees, taxes on financing contracts, export taxes, and provincial and municipal taxes. Most of these sectoral investment incentives are due to expire in 1994.

4.0 COUNTRY PROFILE: COLOMBIA

4.1 Basic Comparative Indicators

Colombia, with a geographical area of 1,141,748 km^2 (440,000 mi^2) is the largest of the countries being compared, both in area (about the size of Texas, New Mexico, and Arkansas combined) and in population (33.4 million, with four cities of more than 1 million inhabitants). Approximately 70 percent of its population is urban, and its capital, Santa Fé de Bogota, has more than 5 million people.

Colombia's 1990 GDP of US$46,989 million was 3.5 times larger than that of Ecuador, which had a 1990-1991 GDP growth rate of 3.9 percent. Colombia's 1990 GNP was US$41,922 million, almost four times larger than that of Ecuador. In 1992 Colombia had the lowest external debt of all the countries studied as well as the lowest debt to GDP percentage.

Gross domestic investment in Colombia amounted to US$8,450 million in 1991. The average annual growth rate in domestic investment fell during 1981-1990 to 0.9 percent, compared with 5.1 percent for 1971-1980. In 1991, Colombia's total private investment as a share of GDP was approximately 10.9 percent, second smallest in the comparison group of countries.

In 1991, Colombia received approximately US$468 million in overall new FDI constituting some 7.2 percent of gross domestic investment that year, making it the third largest receiver of new FDI among the countries studied and second smallest in the percentage of new FDI to total gross direct investment.

In 1991, Colombia was host to total U.S. FDI of US$1,744 million, nearly six times as much as Ecuador. Like Ecuador, U.S. FDI was heavily concentrated in manufacturing and petroleum. The average annual rate of growth of U.S. FDI slowed dramatically from 23 percent during 1980-1984 to 1.2 percent during 1984-1989, the latter figure comparable to Ecuador's 1.7 percent for the same period.

Colombia is highly diversified as an economy, with significant comparative advantages in leather and leather manufacturing, apparel, and nonmetallic mineral manufacturing, and with noticeable comparative advantages in iron and steel, footwear, plastics, and textiles.

Colombia is a member country of the Andean Pact, as well as a member of the Latin American Economic System (SELA), Latin American Integration Association (LAIA), the Río Group, Latin American Energy Organization (OLADE), and the Andean Parliament. It is one of three countries (with Mexico and Venezuela) that form the G-3 Group of economically advanced Latin American nations.

4.2 Basic Investment Regime

Colombia has no single, comprehensive FDI code. Its revised Constitución Política (Political Constitution) of July 1991 does not specifically address either FDI or the rights and obligations of foreign investors. However, Article 100 provides that "foreigners shall enjoy in Colombia the same civil rights accorded Colombians." Nevertheless, for reasons of public order the law may subordinate or deny the exercise of certain civil rights to foreigners. Historically, Colombia hastened to regulate FDI as an aspect or constituent of its foreign exchange laws and regulations. Although recently liberalized, its overall FDI regime is more restrictive (certainly on paper) than that of Ecuador with its recent changes.

Basic elements of Colombia's current FDI regime include (1) Andean Pact Decisions 291 and 292 of March 1991 (described earlier); (2) Article 58 of the constitution, relating to expropriation; (3) Law 9 of 1991; and (4) Resolutions 51/91 and 52/91 of the National Social and Economic Policy Council (CONPES). Collateral laws and regulations specifically addressing or affecting FDI include Colombia's exchange laws, tax laws, a decision governing technology transfer, the Company Law, and the Labor Code.

As a member country of the Andean Pact, Colombia has incorporated into and applied to its FDI regime Decisions 291 and 292. Article 15 of Law 9 (also called the International Exchange Statute) provides that "the general regime on the investment of foreign capital in Colombia . . . shall be established by the national Government." The law also established CONPES and authorized it to issue specific directives regulating FDI.

Under authority of Law 9, CONPES issued Resolutions 51 and 52 of 1991, referred to together as the International Investment Statute (IIS). Article 8 of the IIS provides that FDI may be made

in all sectors of the Colombian economy except in (1) national security and defense; and (2) processing, disposal, and elimination of toxic, dangerous, or radioactive wastes not produced in Colombia. Article 8 also says, however, that CONPES "may reserve sectors of economic activity and determine whether the participation of investment of capital from abroad will be permitted therein."

Article 9 of the IIS requires that a number of otherwise permissible investments "shall require the prior authorization of the National Planning Department." These include projected investments related to (1) public services and (2) disposal and elimination of nontoxic wastes (upon approval of the competent agency), as well as (3) investments that "rely on their being covered by protection, guarantee or insurance mechanisms, derived from international agreements in force, ratified by Colombia"—essentially, U.S. OPIC insurance or MIGA coverage. Article 11 provides that foreign investors may also undertake FDI through purchase of shares, participation, or rights from investors in Colombia, subject to the same approval requirements. The IIS qualifies, at least for the investment areas enumerated above, as an "authorization or approval" type of FDI regime that provides a degree of discretion to the National Planning Department (NPD).

The department is qualified as the competent agency to issue approvals, except in certain special sectoral areas such as financial (Superintendency of Banks), mining (Ministry of Mines and Energy), and institutional funds (Superintendency of Securities). Article 12 prescribes certain evaluative criteria, however, to guide the discretion of the NPD in deciding whether to approve or reject an investment. These criteria include (1) for investments in public services, the positive effects on the costs and efficiency in rendering the service and the promotion of public welfare; (2) for waste enterprises, the origin and nature of the waste and the nature of its transformation process; and (3) for insured or guaranteed investments, "whether the investment is desirable for the country." Article 13 of the IIS authorizes the NPD to attach certain conditions subsequent to its approval of an investment but specifies no criteria therefor. Article 14 imposes a time requirement on the NPD to the effect that it must rule on any application for authorization within 45 business days following the filing date, "provided no supplementary documentation has been requested within 15 days" thereof. Although Article 14 provides that "applications not decided within the period established in this article are considered approved," it also authorizes suspension of the tolling of the 45-day period to enable it to request and receive the opinions of other "agencies or entities, public or private" on the application for up to 1 month.

Whether or not an FDI requires approval of the NPD or other competent agency, Article 15 of the IIS requires that <u>all</u> FDI

(including reinvestments) must be registered at the Central Bank within 3 months of the investment or of the approval of the investment, whichever applies; an extension of up to 6 additional months may be granted when requested of the Central Bank and found to be justified. Capital or profits from FDI that is not properly registered with the Central Bank is not authorized to be remitted from Colombia. Article 15 also requires that if the investment is in a new company or involves opening of a branch, an operating license must be obtained from the Superintendency of Companies or Banks, as required by law. Paragraph 4 of Article 15 of the IIS provides that the Central Bank will not register investments ". . . if the interested party has not first informed the Bank . . . that funds arriving from abroad will be used to make the foreign capital investment."

Special regimes for FDI in the financial sector and in mining and hydrocarbons are set forth in Articles 27-29 and 30-38 of the IIS, respectively.

4.3 Treatment

As indicated earlier, Article 100 of the Constitución Política of Colombia provides that

> foreigners shall enjoy in Colombia the same civil rights accorded Colombians. Nevertheless, the law may, for reasons of public order, subordinate the civil rights of foreigners to special conditions or cancel them [altogether].

With specific reference to FDI, Law 9 of 1991 in the paragraph to Article 15, provides that "the rules issued pursuant to this article may not establish conditions and grant treatment to foreign investors that are discriminatory vis-à-vis those of Colombian private investors."

The resolutions of CONPES that constitute the International Investment Statute provide more explicit statements of the standard for treatment of foreign investors and FDI. Article 3 of the IIS states that

> [e]xcept for matters relating to the transfer of funds abroad, the investment in Colombia of capital from abroad will be treated for all effects, in the same way as are investments by Colombian residents.
>
> Without prejudice to the provisions set forth in special regimes, no discriminatory conditions or treatment may be imposed on investors of capital from abroad vis-à-vis Colombian private resident investors, nor may investors of

capital from abroad be given more favorable treatment than that granted Colombian private resident investors.

4.4 Taxation

4.4.1 Income Taxation

Colombian law defines taxable income as the sum of all regular and nonrecurring income forming earnings and producing an increase in next assets not otherwise expressly excluded, less returns, rebates, discounts, costs attributable to such income, and deductions. Foreign companies and Colombian branches of foreign companies are taxed on all regular and windfall income originating in Colombia. The law establishes a presumption that net assets of a taxpayer at end of year have generated income of at least a set percentage of their value per year. For 1993 the percentage is 5 percent, for 1994 and subsequent years it is 4 percent.

The higher of presumptive and ordinary income is the base for calculating the flat rate of income tax applicable to incorporated entities, partnerships, and Colombian branches of foreign corporations. The applicable rate of income tax is 30 percent but that is supplemented by a special 25 percent surcharge on net tax payable imposed for fiscal year 1993 through fiscal year 1997, so that the effective tax rate for these years is 37.5 percent. Certain industrial sectors have their own applicable income tax rates, for example, oil, coal, and nickel.

There are certain exemptions from income tax, for example, payments and royalties paid by Colombian publishers and income from certain export operations. Income obtained by foreign nationals enjoys the exemptions specified in certain international treaties and agreements to which Colombia is a party.

4.4.2 Profits/Capital Repatriation

Transfer abroad of regular income and capital gains are subject to a remittance tax withheld at the time of payment. The remittance tax rate depends on the type of income remitted. Dividends and partnership profits payable to a foreign investor as shareholder or partner are not subject to a remittance tax, but dividends or partnership profits obtained by foreign companies or other entities not domiciled in Colombia, or by nonresident foreign nationals, are subject to income tax that is withheld at the time of payment according to a decreasing

schedule: 12 percent in 1993, 10 percent in 1994, 8 percent in 1995, and 7 percent in 1996 onward.

If the dividends or partnership profits are the product of profits not previously taxed in the company distributing them, a flat rate of 30 percent income tax will be imposed in lieu of the remittance tax. If dividend or partnerships profits are paid in shares or participation units to capitalize the company generating the income, the tax rate is zero if the company has already paid income tax and the net amount thereof is reinvested or retained in Colombia for 5 years or more. If the profits distributed in the firm of shares or partnership interests have not paid tax in the company generating them, income tax is payable at the 30 percent rate but deferred while the investment is retained in Colombia.

Royalties are exempt from a remittance tax up to a limit of 3 percent of gross sales or production in the year paid or credited. Payments of interest, commissions, royalties (beyond the 3 percent limit), leases, know-how, and technical services and assistance to foreign companies or nonresident foreign nationals are subject to an income/remittance tax of 12 percent and 30 percent withholding. However, beginning in 1994, such payments are subject to a scheduled reduction as follows: 10 percent in 1994, 8 percent in 1995, and 7 percent in 1996 onward.

Colombia also has a VAT with a general rate of 14 percent and special, higher rates for imported vehicles and spirits, as well as stamp, import, and municipal taxes.

4.5 Expropriation

Colombia has been in the world news recently because of concerns raised by the British and Japanese regarding recently enacted legal authorities dealing with expropriation. These concerns have to do with a recent amendment to Colombia's constitution that appears to permit uncompensated, administrative expropriation without judicial recourse if one house of the Colombian Congress approves.

Article 58, Paragraph 1, of the Constitución Política de Colombia provides that

> private property and other rights acquired in accord with civil laws are guaranteed and may not be withdrawn or impaired by subsequent laws. When the application of a law enacted for public utility or social interest results in a conflict between the owner's rights and the necessity recognized [in such law], the private interest shall accede to the public or social interest.

Article 58 then provides that

> for reasons of public utility or social interest defined by the legislature, expropriation may occur by means of a judicial order and previous indemnization. In cases determined by the legislature, such expropriation may proceed administratively, subject to subsequent adversarial administrative proceedings, including with regard to price.
>
> Withal, the legislature may, for reasons of equity, determine those cases in which there is no cause for the payment of indemnization, by means of an affirmative vote of an absolute majority of members of one or the other of the houses [of Congress].

However, an amendment to the Colombian constitution promulgated (among various adopted by a recent Constituent Assembly) July 7, 1991, added language to the above-quoted portion of Article 58 that provides that "the reasons of equity, as well as those of public utility or social interest, invoked by the legislature, shall not be controverted judicially." [Emphasis added.]

The foregoing sentence effectively removes any avenue of judicial recourse for property owners whose property has been expropriated by administrative action endorsed by one or both houses of the Colombian Congress. In July, Colombian President César Gaviria journeyed to London for a state visit, the centerpiece of which was to have been the formal signing of a recently negotiated bilateral investment treaty between Colombia and the United Kingdom. However, since discovery of the above-quoted amendment to Article 58 of the Colombian Constitution, the British have asserted that any protection to the contrary provided for in the treaty could be voided as unconstitutional by a Colombian court. The Japanese government has expressed its concern about the effect of such a provision, and U.S. authorities are only now beginning to address the consequences on upcoming negotiations for a Colombian-U.S. bilateral investment treaty.

The issue is downplayed by Colombians who assert that, notwithstanding previously existing authority for expropriation (even without compensation), Colombia has no history in modern times of such action and is unlikely to undertake any in the future.

Colombia is a signatory to international agreements providing for protection against political risks through both the OPIC and the MIGA. It is considering adhering to the agreement establishing the International Council for the Settlement of Investment Disputes (ICSID) in order to gain access to international settlement and arbitration forums.

4.6 Investment Incentives

Colombia has few positive foreign direct investment incentives. The principal incentives, available to Colombian and foreign investors alike, are found in its free zones.

The government has authorized the establishment of free zones based on industry, trade, tourism, and technologies, preferably designed for exports. Free zones enjoy special customs, exchange, trade, and tax privileges and may be established anywhere in Colombia. The zones are classified as industrial and commercial zones, science parks, and tourist zones. Industrial and commercial zones promote the production of goods and provision of services for export. Science parks require at least 10 technology-based businesses producing for export primarily and only secondarily for the domestic market. Tourist zones are designed to develop tourist areas and tourist services. No minimum levels of exports are demanded, and free zone user contracts can be signed for up to 30 years and are renewable. If a free zone user cannot sell the free zone's production abroad, it may do so in Colombia, but subject to import duties and taxes like any other company operating outside the zone in Colombia.

The major incentives provided free zone users are related to exchange and taxes. Foreign currency earned from exports may be held freely and negotiated. Exporters are not required to sell their currency through the Colombian banking system. The only requirement is that foreign users must register any foreign investment with the Central Bank. Industrial users are exempt from (1) income and asset taxes on the proceeds of goods and services exported; (2) VAT sales taxes on imported materials; (3) withholdings for income and remittance taxes on remittance of profits or payments of interest or technical services related to export sales; and (4) import duties on passenger vehicles, yachts, and other vessels for the tourist zones. Licensing contracts for technology, technical assistance, technical services, basic engineering, trademarks, patents and other industrial property may be registered automatically with INCOMEX; as a result, the contracts receive automatic access to foreign currency required to pay for them.

Apart from free zones, certain investments in new reforestation projects, coconut palm, palm oil, rubber, olives, cacao, fruit trees, irrigation, and activities primarily benefiting agricultural production enjoy annual deduction from income of the investment made, up to 10 percent of taxable income.

5.0 COUNTRY PROFILE: CHILE

5.1 Basic Comparative Indicators

Chile, with a geographical area of 271,000 km^2 (about 109,000 mi^2) is roughly twice the size of California. It has a population of 13,360,000, approximately 86 percent of which is urban.

Chile's 1990 GDP amounted to US$33,289 million, nearly three times that of Ecuador, with a real GDP growth rate of 6.5 percent in 1992, twice that of Ecuador. At US$2,527, Chile's 1990 GDP per capita is twice that of Ecuador, and its 1992 GDP per capita growth rate of 4.8 percent was more than three times that of Ecuador. Chile's 1991 inflation rate of 19 percent was the lowest of the countries studied and 40 percent that of Ecuador.

Chile's overall 1991 private investment amounted to US$576 million, six times that of Ecuador. U.S. FDI in Chile increased some 93 percent between 1984 and 1989, compared with 1.7 percent in Ecuador.

Chile stands as the early leader in Latin America in macroeconomic reforms, privatization, and restructuring, and now includes a dynamic private sector that attracts FDI from around the world. It has a broadly diversified economy with little government intervention and, as evidence of the success of its market-oriented policy initiatives and economic growth, has been cited by the U.S. Government as second in line after Mexico for negotiation of a free trade agreement.

5.2 Basic Investment Regime

Like Colombia, Chile has no single, comprehensive foreign direct investment code. Its constitution contains no provisions specifically directed toward the concept of foreign investment in the country or defining the rights, obligations, or treatment of foreign direct investors. The constitution does set forth certain general principles, which, taken together, provide a basis in constitutional law for both private entrepreneurial activities and the exercise of public authorities. Article 19, Paragraph 21, provides that the constitution guarantees every person "the right to develop whatever economic activity which is not contrary to morals, public order, or national security, respecting the legal norms regulating it."

Paragraph 2 of Article 19 guarantees every person equality before the law, and provides that "in Chile, there are no

privileged groups or persons. . . . Neither the law nor any authority may establish arbitrary differences."

Nevertheless, Chile has a coherent, albeit rather complex, FDI regime, the basic elements of which include (1) Decree Law 600 of July 13, 1974 (from time to time amended, most recently by Law No. 19,207, published March 31, 1993), which is referred to as the Foreign Investment Statute; (2) Chapter XIV of the Compendium of International [Foreign] Exchange Rules of the Central Bank (relating to "Investments, Contributions of Capital, or Credits Provided from Abroad"); and (3) Chapter XIX of the compendium (relating to investments realized as a result of Chilean debt-equity swaps).

5.3 Admission/Approval

Essentially, FDI can occur in Chile either formally through the procedures specified by Law 600, less formally and without the guarantees contained in Law 600 by simple registration with the Central Bank (Compendium Chapter XIV), more formally through the debt-equity swap device (Compendium Chapter XIX), or completely informally without any of the guarantees or protections provided FDI by the government through the informal exchange market.

Law 600 is the principal channel for introducing new FDI into Chile. Article 1 of the law provides that foreign natural and legal persons who transfer foreign capital to Chile and formalize a foreign investment contract with the state are governed under the rules established in the law. Under the law, FDI can occur in any of the following forms: (1) freely convertible foreign exchange, (2) contributions of physical property, (3) transfer of technology, (4) credits extended incident to a foreign investment, (5) capitalization of credits and foreign debts denominated in freely convertible foreign exchange, or (6) capitalization of profits entitled to remission abroad.

Approval of FDI by the Chilean government is evidenced by the formalization of a foreign investment contract between the foreign investor and the Foreign Investment Committee, the agency established by Article 12 of Law 600 as the "only organism authorized to represent the Chilean State, with regard to the acceptance of foreign capital. . . and to establish the terms and conditions of the respective [foreign investment] contracts." The Foreign Investment Committee includes the Minister of Economy, Development, and Reconstruction, who serves as chairman; the Minister of Finance; the Minister of Foreign Relations; the Director of the Office of National Planning; the President of the Central Bank of Chile; and ministers of agencies with specialized

regulatory authorities over specific sectoral areas when the investment involves such areas. The committee is managed daily by its Executive Vice-President.

The foreign investment contract, in effect, establishes the rules under which the investment will be undertaken and guarantees the investors that the rules thus established will not be changed regardless of subsequent changes in laws and regulations that otherwise change the FDI legal regime. The contract (1) describes the parties to the contract, (2) authorizes the investment, (3) defines the goals for the investment, (4) specifies the time limits within which the actual investment shall occur (3 years except for certain mining investments), (5) applies current legislation to the investment, (6) prescribes the forms for making the investment, (7) specifies the rights of the foreign investor, (8) provides for changes in the nature or forms of the investment, (9) "grandfathers" investment effected before approval or formalization of the contract, and (9) ensures that the agreement carries with it the full faith and credit of the Chilean state.

Of primary importance to foreign investors are the "rights" recognized and guaranteed by the Chilean state to the foreign investor. The rights explicitly specified include (1) the right to contract with the state about the rules and regulations that will affect the investment, (2) free access to the formal exchange market to buy or sell exchange and to remit such exchange abroad, (3) free remission of capital and profits abroad (after payment of applicable taxes), (4) the right to opt to be covered by invariable income tax rates, (5) the right to non-discrimination compared with domestic investors, and (6) the special privileges granted to so-called "megaprojects."

For investments involving less than US$5 million, the contract may be negotiated and signed on behalf of the Chilean government by the Foreign Investment Committee's Executive Vice-President. Investment contracts involving more than US$5 million must be considered by all members of the committee and signed by the Chairman (the Minister of Economy). Certain other investment contracts must also be considered by the whole committee, including those involving sectors normally developed by the state, those relating to the provision of public services, those involving communications media, and those investments made by a foreign government or agency.

5.4 Treatment

As previously indicated, the Chilean Constitution does not explicitly provide specific norms relating to the treatment of foreign investors and their investments other than a vague

guarantee of "equality before the law" contained in Article 19, Section 2. However, Article 57 of the Chilean Civil Code does address the issue, providing that "the law recognizes no differences between a Chilean and a foreigner with respect to the acquisition and enjoyment of the civil rights regulated by this Code."

Law 600, the Foreign Investment Statute (FIS), also addresses concerns of treatment of FDI. The first paragraph of Article 9 provides that

> foreign investment and the enterprises in which it participates are also subject to the common juridical regime applicable to national investment, without discrimination thereto, direct or indirect, with the sole exception provided for in Article 11.

Article 11 provides that "there may be established fundamental rules applicable to investments undertaken under this decree law which limit its access to internal credit." Article 9 proceeds to describe the kinds of actions that might result in discriminatory impact on foreign investors:

> The legal or regulatory provisions relative to a determined productive activity will be considered discriminatory if they are made applicable to most or the major part of such productive activity in this country but exclude foreign investment. Similarly, legal or regulatory dispositions that establish exceptional sectoral or geographical regimens will be considered discriminatory if foreign investment has no access thereto, notwithstanding the compliance with the same conditions and requirements necessary for the enjoyment thereof imposed on national investors.

Nevertheless, other applicable laws do, in fact, restrict certain sectoral and geographical areas within which foreign investment is not permitted. Economically, the most important restricted areas are the fishing industry and radio and television, but the prohibition extends to cabotage (transportation services between ports in the same country, an exception also imposed by the United States), and frontier (border) zones. An important exception to "national treatment" is that most foreign investment is excluded from access to Chilean financial markets. The rationale for this restriction was originally because the object of the statute was to attract resources from abroad given the (then) thinness of Chilean sources of financing. However, in November 1992, Resolution No. 257-02-921105 of the Central Bank provided that for investments undertaken under Law 600, the restriction would be applied only after "commencement" of the [investment] project and not to the preoperational phase of the project. In fairness, it should be pointed out that a number of

general or specific positive investment incentives affecting foreign investment exist that could be denominated forms of "positive" discrimination in favor of foreigners, detailed in the section entitled "FDI Incentives."

5.5 Taxation

5.5.1 Income Taxation

Under Article 20 of the Chilean Income Tax Law, all business income is subject to a so-called First Category tax rate of 15 percent in the year accrued. Under Articles 58 and 60 of the same law, income is also subject to an additional 35 percent tax when distributed to shareholders or partners or, in the case of Chilean branches of foreign companies, when withdrawn or remitted abroad, but subject to a credit for the First Category tax already paid.

However, Chile provides a form of tax incentive to foreign investors, referred to as the *invariabilidad tributaria*, who formalize a foreign investment contract with the state through the Foreign Investment Committee and subject their investments to the FIS. Article 7 of the FIS confers on investors the right to opt for a fixed overall taxation rate of 42 percent for a period of 10 years once business activities start, instead of the standard income tax provisions. Under Article 11 the period is extendable for up to 20 years for investments in manufacturing or extractive industries exceeding US$50 million. The fixed rate option gives investors the security that their income tax rates cannot be raised during the term of the incentive regardless of legislative changes otherwise in the tax laws. However, should tax rates actually go down, Article 7 also provides that

> even though the foreign investor may have opted to request the [fixed rate], it shall have the right, only once, to renounce [the fixed rate] and integrate itself into the common tax regime, in which case it shall remain subject to the alternatives of general tax legislation, with the same rights, options, and obligations governing national investors.

This tax incentive does not, however, exempt foreign investors from the standard substantive provisions of Chile's tax law, for example, definition and calculation of income and deductions.

5.5.2 Capital/Profits Repatriation

A foreign investor's primary concern about remission of profits is the ability to acquire the foreign exchange necessary to transfer profits abroad. Law 18,840 of 1989 constitutes the Organic Law for the Chilean Central Bank. Under the Law, Chile recognizes two foreign exchange markets in the country, the formal exchange market and the informal market. The formal market constitutes the nation's banking system and is regulated by the Central Bank, which, although it does not set the formal exchange rate, influences the rate through its regulatory powers. Article 42 of the Organic Law specifies that all international exchange operations related to foreign investment shall be realized through the formal exchange market. This rubric is incorporated into Chapter 2 of the Central Bank's Compendium of Rules for Foreign Exchange, which contains the bank's overall set of regulations affecting foreign exchange transactions. As a result, all transactions in foreign exchange related to incoming foreign investment and remission abroad of capital and profits must occur in the formal market.

Nevertheless, although it is possible actually to effect foreign investment in Chile without following the approval and contract procedures of the Foreign Investment Committee by merely registering the investment with the Central Bank, formalizing a foreign investment contract with the Chilean state subjects the foreign investor to the FDI regime established under the FIS. Acceding to the FIS legal regime guarantees a foreign investor of two important rights: (1) the right to remit capital and profits of the investment abroad, and (2) unencumbered access to the formal exchange market (banks) to acquire the necessary foreign exchange for such remissions. Article 4 of the FIS provides that

> remissions of capital may be made once there has elapsed one year from the date of the respective entry thereof. Increases in capital representing profits are susceptible to being remitted abroad without expiration of any time period once there has been compliance with taxation obligations. The regime applicable to the remission of capital and liquid profits may not be less favorable than that which governs the payment of most importations.

Remission of profits does require issuance by the Foreign Investment Committee of a certificate specifying the amount to be remitted in order to receive clearance to acquire the necessary exchange in the formal exchange market. The current regime affecting remissions abroad was enacted in the March 1993 amendments to the FIS, which, among other things, reduced the waiting period for remissions of capital from 3 years to 1 year and removed time limitations affecting remission of profits. However, it should be noted that although remissions of capital up to the

amount of the original capital invested are not subject to any remissions tax, any remissions in excess thereof are subject to taxation but only up to an overall effective rate that fits within the invariabilidad tributaria fixed rate of overall taxation elected by the investor in its foreign investment contract.

5.6 Expropriation

Article 19 ("Constitutional Rights and Obligations") of the Chilean Constitution of 1980 enumerates rights "assured to every person." Section 23 guarantees to every person

> the freedom to acquire ownership of all classes of property, except that which nature has made common to all men or which ought to pertain to the Nation as a whole and the law declares as such. . . . A law . . . when the national interest so requires, may impose limitations or requirements on the acquisition of ownership of certain property.

Section 24 of Article 19 addresses the issue of expropriation specifically (and exhaustively), assuring every person that

> The right of property in its diverse forms over all classes of things, tangible and intangible.
>
> Only the law may establish the method of acquiring property, of its use, enjoyment, and disposition, and the limitations and obligations derived from its social function. This includes [those cases] when required by the general interest of the nation, national security, public utility and health, and conservation of the Nation's environment.
>
> No one, in any case, may be deprived of their property, of the enjoyment thereof, or of any of the essential attributes or powers of ownership, except by virtue of a general or special law authorizing the expropriation for reasons of public utility or national interest enacted by the legislature. The owner may attack the legality of the expropriatory acts before the common courts and shall always have the right to indemnification for damage to his property right caused thereby, which shall be assessed by common agreement or by a judgment issued by such courts in accordance with law. Failing agreement, the indemnity should be paid in ready cash.
>
> Entry into material possession of the property expropriated shall take place upon prior payment of the full amount of the indemnity which, in the absence of agreement, shall be determined by experts in the manner prescribed by law. In the event of a claim regarding the manner of the expropriation, the judge may, upon the

basis of the precedents invoked, decree suspension of the taking of possession.

The article proceeds to enumerate at length special provisions for the absolute dominion of the state over mines and the resolution of controversies involving the rights of concessionaires thereof.

Chile has an OPIC agreement with the United States and an agreement with MIGA that provide insurance covering political risks including expropriation and risks of currency inconvertibility. It has entered into bilateral investment protection agreements with Argentina, Belgium, France, Germany, Malaysia, Spain, and Switzerland and has entered into negotiations for such agreements with Finland, Great Britain, Italy, the Netherlands, Sweden, and Venezuela. Although the United States has requested Chile to enter into negotiations for a bilateral investment treaty, Chile has demurred on the grounds that the subject matter of such a treaty should be incorporated into the overall negotiations for a free trade agreement between the two nations. Chile signed the convention creating the International Center for the Settlement of Investment Disputes (ICSID) in 1991.

5.7 FDI Incentives

Under the FIS, Chile extends a number of general incentives, described earlier, that benefit foreign investors, including formalization of a contract that guarantees "rules of the game" for the life of the investment; an option to elect a fixed rate of income taxation; and, under Article 8 of the FIS, exemption from Chile's VAT on certain imports and fixed rate guarantees on the VAT rate and import duties otherwise applicable on imports of machinery and equipment. The incentives run for 3 years for most investments, up to 8 years for investments in extractive industries, and up to 20 years for "megaprojects" in such industries for investments exceeding US$50 million.

Beyond these incentives, however, Chile also maintains certain specific positive incentives focused on targeted geographical areas or industrial sectors. Special tax and other promotional regulations have been established for the economic development of distant areas in the extreme north and south that include a reduced (9 percent) First Category income tax. Certain industrial, mining, tourism, fishing and transportation activities carried out in the Strait of Magellan qualify for full exemption from the First Category income tax, the VAT, and customs duties whether they involve domestic or foreign investment. Chile has also established free zones in the remote towns of Iquique and Punta Arenas for assembly and processing, deposit, or display of goods; these services are exempted from the VAT and First Category income tax.

Chile's sectoral specific incentives are targeted on forestry and certain extractive industries. Decree Law 701 of 1974 governs the preservation and development of Chile's forests. It grants a one-time-only tax-exempt "bonus" or government subsidy of up to 75 percent of the costs of forestry planting, as well as subsidization of the costs of dune stabilization and replanting, and 50 percent of earnings from forestry operations are deemed tax exempt. Although the Chilean constitution reserves dominion over mines and mining operations to the state, the constitution and the Mining Law provide for the granting of mining concessions for exploration and exploitation of natural resources under agreements with and conditions fixed by presidential decree. Under this authority, the president of Chile may exempt concessionaires from the common income tax regime in favor of a special reduced rate of 50 percent or more as well as waive payment of other applicable taxes or duties.

6.0 COUNTRY PROFILE: COSTA RICA

6.1 Basic Comparative Indicators

Costa Rica is one of the smallest of the Latin American countries, with a territory of 51,100 km^2 (19,730 mi^2) and a population of slightly more than 3 million. Despite its small size, Costa Rica's geography is diverse, with three mountain ranges dividing it into five distinct zones: tropical lowlands on both the Pacific and Atlantic coasts, the north central tropical plains, the high lands of the central valley, and the broad, semiarid lowlands of the northwest.

The Central Valley, with ample rainfall and an equable, mild climate serves as the population and economic center of the country. Greater San José is credited with over 1 million inhabitants, and the four central provinces, Cartago, San José, Heredia, and Alajuela encompass 75 percent of the national population. The diverse topography and heavy rainfall have provided Costa Rica with ample hydroelectric potential. The country meets its own present requirements for electric power and even exports some to neighboring countries. The generally rich and well-watered soils led to Costa Rican development based on export agriculture, beginning in the mid-19th century with coffee, grown in the central highlands, supplemented at the beginning of the 20th century with banana plantations along the Atlantic coast. Other traditional exports included sugar, cacao and beef. There has been almost no development of mineral resources. Logging has been extensive and has resulted in recent years in serious deforestation.

During the colonial period, Costa Rica was at the end of the line with respect to the colonial capital at Guatemala and, absent either mineral wealth or plantation agriculture, was the poorest of

the Central American provinces. The population, predominantly Spanish immigrants, consisted essentially of small, self-sufficient farming communities in the central highlands. Economic growth came from the development of coffee exports, cultivation of which could be profitable even for family enterprises, and further expanded by European immigration in the last half of the 19th century. Social development then took place more rapidly than elsewhere in Central America since there was little racial stratification or agricultural peonage.

After a civil insurrection in 1948, Costa Rica adopted a new constitution, which has since provided the framework for democratic elections. The constitution prohibits the existence of an army and distinguishes between Costa Rican citizens and foreign residents only in the right to vote and hold public office. Substantial expenditures through the years in education and health have led to a highly literate population (93 percent adult literacy) and health indicators on a par with the developed world.

Costa Rica enjoyed substantial economic growth into the decade of the 1970s based on its traditional agricultural exports. The country joined the Central American Common Market (CACM) in 1963 and there was modest growth in industry, principally pharmaceutical and plastics, intended to supply the common market. By the late 1970s, the CACM was moribund and the combination of political violence elsewhere in Central America and the world economic crisis resulted in an economic crisis for Costa Rica. Costa Rica's recently resumed economic growth has been the result of development of two, non-traditional economic activities: tourism and industrial assembly operations. There has also been development in non-traditional agricultural products, but these have not matched the volume of the traditional exports such as bananas and coffee. The non-traditional economic activities have been strongly favored by Costa Rica's proximity to the United States, its social and political stability, educated work force and relatively open economy.

Costa Rica's per capita income in 1993 is estimated at more than US$2,000 a year. Inflation exceeded 25 percent in 1991, was estimated at 17 percent in 1992 and appears to be running at an even lower rate in 1993. GDP growth in real terms was 2.2 percent in 1991, exceeded 7 percent in 1992 and is expected to exceed 2.5 percent in 1993. Foreign exchange restrictions were lifted in 1992 with the Costa Rican colón allowed to float. Foreign currency deposits are permitted and there are no restrictions on movement of capital. Current central bank foreign exchange reserves are more than US$1 billion. In keeping with a series of agreements with the International Monetary Fund and World Bank, the central government's fiscal deficit has been reduced from 5.1 percent of GDP in 1989 to 1.5 percent as of 1992. The foreign debt is approximately $3.5 billion, one of the highest in Latin America, if considered in per capita terms.

Costa Rica's economy is highly dependent upon foreign trade. Exports in 1992 were calculated at $1.8 billion. Imports, however, were nearly $2.5 billion, leaving a commercial trade deficit of over $600 million. Foreign exchange earnings from tourism generated over $400 million in 1992 and together with inflows of foreign capital both for direct as well as portfolio investment have led to the retention of adequate reserves and contributed to a generally stable foreign exchange rate.

Costa Rica acceded to the GATT in 1990. It is also signatory to the Tegucigalpa Protocol of 1991 reactivating the movement to seek Central American economic integration. Costa Rica has participated in the distinct conferences and organizational efforts but has expressed substantial reservations as to the terms of integration. Costa Rica independently and in conjunction with the other Central American states has been engaged with discussions with Mexico, Colombia and Venezuela with regard to some form of free trade arrangement. There have also been discussions between Costa Rica and Chile. Costa Rica is committed to expanding its foreign trade relations and has joined the other Central American countries in opening its economies through significant reductions in tariff rates and the elimination of many import quotas and licensing requirements. The U.S. accounts for 46 percent of Costa Rica's exports and 41 percent of its imports.

Costa Rica has bilateral investment treaties with Great Britain, France, Switzerland and Germany. A treaty with the United States is under negotiation. The Friendship, Commerce and Navigation Treaty between Costa Rica and the United States dates to 1851. Costa Rica is a beneficiary country of both the U.S. Generalized System of Preferences (GSP) and the Caribbean Basin Economic Recovery Act (CBERA) and has entered into a tax information exchange agreement with the U.S. and so is eligible for so-called 936 financing.

Since there is at present no requirement that foreign investment be registered, no direct investment statistics are kept. The U.S. Department of Commerce estimated FDI in 1991 at $135 million, of which 75 percent derived from the United States. Estimates for 1992 are around $120 million. Owing to proximity and its status as a favored tourist destination, Costa Rica has attracted significant numbers of individual American investors in such things as macadamia orchards, teak plantations and beach property. There are questions as to the validity of some of these investments and the legality of direct sales in the U.S. without registration with securities exchange authorities in either country.

6.2 Basic Investment Regime

Costa Rica does not have a formal investment code nor legislation dealing specifically with foreign investment. Article 19 of the Constitution grants foreign residents the same social and individual rights as Costa Rican nationals except as specified in the Constitution: the only exception listed in Article 19 is the right to intervene in the political life of the country.

The dominant political party in Costa Rica, which controlled the Congress from 1948 until 1990, supported a strong role for the state in economic and social matters. In addition to reserving the ownership of radio stations and newspapers to Costa Rican citizens, legislation reserves medical services, demand and time deposits, generation and distribution of electric power, telecommunications, roads, ports and airports, customs brokerage services, insurance, alcohol distillation, petroleum refining and pension funds either to Costa Ricans or to control by the state. The state may grant concessions within the areas reserved for its control, such as private medical services, private banks (which may not offer demand or regular savings deposits), cellular telephone services, the generation of electric power in plants with capacity of no more than 20 megawatts and in legislation just passed, the Government may contract to private enterprises the building and operation of roads and port facilities. Private companies retail gasoline and blend alcohol to make beverages. The Government insurance institute also reinsures with private companies.

The Government's development bank (CODESA) during the 1980's acquired an array of failed private companies as a result of loan defaults but has nearly completed the divestiture of its portfolio. Two major companies remain with CODESA, a cement and a fertilizer producer. Under pressure from the IMF plans are being completed to privatize these two firms.

From 1982 until 1992 there were requirements to register foreign investment, motivated principally to conserve foreign exchange holdings. This requirement was eliminated in 1992 and there are no present restrictions on repatriation of capital or conversion of local currency into foreign. However, to benefit from selected investment and export incentives it is necessary to register the investment. There are three channels for such registration: the Tourism Board (Instituto Costarricense de Turismo, ICT); the Center for Export and Investment Promotion (CENPRO); and the Free Trade Zone Corporation. ICT is responsible for approving investments related to tourism, including hotels, car rental agencies, travel agencies and tour companies. CENPRO is responsible for export contracts and temporary import regimes, both of which provide incentives for Costa Rican-based companies to export. The Free Zone Corporation must approve the granting of free

trade zone status to applicant companies and thus in practice acts to review and approve their investment plans.

While there is no prohibition on foreigners owing land within Costa Rica, there is one restriction, applicable to Costa Ricans and foreigners, which has caused problems, the law of maritime property. This holds that the first 50 meters of land measured from the mean tide level remains forever in the public domain. The next 150 meters can only be utilized under terms of a concession granted by the Government. It means in effect, however, that Americans who buy "beach" property don't control the fifty meters closest to the beach and that they shouldn't really do anything within 200 meters without the appropriate permits. This is not always understood and may not be convenient for major beach resort developments. It is said that the Barceló people violated a number of the restrictions in the construction of the Tambor Beach resort (opened last year), finding that it was cheaper to pay the fines than to comply.

In sum, admission is generally open with the exception of those few areas restricted to Costa Rican citizens and the somewhat larger array of activities under state control. Restrictions on the latter apply to Costa Rican nationals as well. As noted above, foreign investors also receive national treatment.

With respect to taxation, Costa Rican law up to now has been less complex than in the U.S. or elsewhere in Latin America. Residents and corporations are taxed only on income earned in Costa Rica. Income tax law consists only of general regulations, allowing considerable latitude to the Finance Ministry (Ministerio de Hacienda) in tax administration. Deductions from income for tax purposes parallel those allowed in the U.S. and generally include all expenses necessary to produce income. The accrual basis of accounting is mandatory for tax purposes. As a general rule, capital gains and losses on non-depreciable fixed assets or shares of other companies are excluded for income tax purposes.

Unless proof to the contrary exists, for certain professionals as well as companies, presumptive net income is established by the Ministry of Finance and constitutes a minimum taxable base. Personal income taxes are graduated with the maximum rate of 25 percent. Corporate income taxes are assessed against net income at rates ranging from 10 to 30 percent, depending upon the amount of gross income reported. Property taxes are levied on fixed assets and range from 0.30 percent to 1.17 percent of the assessed value. Dividends are subject to 15 percent withholding tax, except for shares transacted on the Costa Rican stock exchange for which the withholding rate is 5 percent. Remittances for royalties, salaries or services are subject to withholding rates from between 5 and 50 percent. Payments or credits made by subsidiaries or branches to parent companies for royalties, trademarks, franchises, etc. are limited to 10 percent of gross sales. Companies are normally exempt from withholding on interest remittances provided that the lenders

are financial institutions recognized by the Central Bank. There are no state or city taxes except for minor fees for permits or stamps for legal documents. Currently there is an ad valorem tax of 11 percent on most goods sold in Costa Rica. This tax is scheduled to drop to 10 percent in 1994.

6.3 Expropriation

Article 45 of the Constitution states that no one may be deprived of property rights except for valid public purposes and with prior compensation. Despite this, there has been over the past 20 years numerous cases of uncompensated land expropriation involving American citizens. An agrarian law passed early in the 1960's further clouded the question of land tenure and has contributed to numerous incidents of land invasions by squatters some of which have resulted in the taking of the land while others have led to armed conflict as landowners have sought to defend their property or to evict the squatters. This latter phenomenon affects national as well as foreign land holdings.

In 1984, the U.S. Government initiated an intensive program of negotiation with respect to ten cases of expropriation which it judged offered the best possibilities for settlement. No more than three have been settled, and the record is one of deliberate delays and actions on the part of the Costa Rican government which can only be interpreted as acts in bad faith. This issue has come to the attention of the U.S. Congress and there is one A.I.D. foreign assistance program still in suspension as a result of failure to reach settlement on these cases.

6.4 Dispute Settlement

As noted above, disputes involving payment for government expropriation of real property are infrequently resolved. While theoretically it is possible to litigate against the Government of Costa Rica, in practice it has proven virtually impossible to obtain prompt or adequate redress. Costa Rican civil and commercial codes provide for settlement of commercial disputes through arbitration in Costa Rican courts. Arbitration outside Costa Rica is not acceptable. Costa Rica has not joined the United Nations Protocol for the Compulsory Settlement of Disputes between Countries nor has it agreed to abide by the guidelines of the International Center for the Settlement of Investment Disputes (Washington Convention) nor of the New York Convention of 1958 on the Recognition and Enforcement of Foreign Arbitral Awards.

In general, litigation in Costa Rica is time consuming and difficult with civil and criminal cases dragging on for years. The general climate for dispute settlement is thus not favorable.

6.5 Investment Incentives

Positive investment incentives were developed in 1984 and subsequent years to cover export production and tourist development. Export production incentives fall into three classes: free trade zone operations, export contracts and temporary admission of goods for processing. Tourism incentives cover hotels, water and air transportation of tourists, vehicle rentals to tourists, tour operators and travel agencies.

Free trade zone operations are exempt from import duties and foreign exchange controls and are exempt from all income taxes for 8 years, and have a 50 percent exemption for 4 years. For "designated areas," e.g., the coastal communities, the exemptions are for 12 and 6 years respectively. FTZ status is not granted except for companies involved in substantial transformation of product. Export contracts are entered with locally-based producers for the export outside Central America of non-traditional products. These include a variety of agricultural and manufactured products ranging from ornamental plants, fruits and chocolates to apparel and electrical products. For export contracts, exemption on import duties is offered in proportion to the amount of final product exported. Incentives for temporary admission are similar with the requirement in all cases that value added in Costa Rica equal 35 percent.

Until recently there was an added incentive, Cumulative Tax Certificates, which were granted in amounts up to 15 percent of export revenues. These certificates (CAT's) were negotiable instruments which could be used to meet Costa Rican tax obligations. In the case of cut flowers, the U.S. held that the CAT's constituted a subsidy subject to countervailing duty. To avoid the duty, Costa Rica agreed not to grant certificates to flower producers. Subsequent pressures from the international lending agencies to reduce the fiscal deficit have led the government to drop the CAT's and several other incentives. Export contracts which were scheduled to expire in 1996, have been extended to 1999 but with a lower level of income tax exemption. With the removal of the foreign exchange controls, basic export production incentives outside the free trade zones are now limited to duty free entry of materials and equipment so long as the items are not readily available in Costa Rica at price levels equivalent to those available internationally.

Tourism incentives also offered duty free entry of capital goods not available in Costa Rica as well as selected income tax

exemptions including a 50 percent tax exemption for income derived from the purchase of shares in tourism companies. These too are being phased out with new tourism permits offering limited exemptions from import duties as practically the sole incentive.

Nonmaterial incentives that most strongly affect the investment decision include proximity to the U.S., the country's wide variety of beaches, mountains and parks which attract tourism, its basic infrastructure, civil order and a high level of human resource development.

Disincentives are principally growing shortcomings in the physical infrastructure. The major ports of Limón and Moín are operating in excess of capacity with ships forced to wait for pier space. Decisions to expand port capacity have been under active discussion in the national congress for the past four years with no concrete results as yet. The only airport certified for international carriers—near San José—has not been improved in recent years and has inadequate facilities for baggage and passengers as well as cold storage and freight handling. Highway maintenance has been neglected and few new roads have been built. San José is afflicted with substantial traffic congestion.

Unemployment nationally is stated to be 4.5 percent, which means that in a number of specialties there exist labor shortages. Costa Rican labor rates are double those of neighboring Central American countries, albeit still quite low compared to the U.S. Productivity is rated to be higher and support services are better developed than elsewhere in Central America.

7.0 ECUADOR: GENERAL INCENTIVES FOR FDI

Although a small market in itself in comparison to other major Latin American nations, Ecuador nevertheless counts a number of basic general incentives for FDI. It is centrally located on the West Coast of South America and (especially given Colombia's prolonged political and narcoterrorism problems) is ideally situated to service the extended Andean market, especially by air from two major cities. It comprises an unusual variety of climates hospitable to nearly all forms of traditional and non-traditional agriculture, a sector in which it is universally agreed to have significant natural comparative advantages. It is well-endowed with basic natural resources, providing a degree of natural comparative advantage in the exploitation of minerals, petroleum, and fisheries. Its touristic potential is described later. In terms of the manufacturing sector, it is believed to have notable comparative advantages in the areas of textiles/yarn/fabric, nonmetallic mineral manufacturing, and chemicals.

While its current democratic government is only a little over a decade old, Ecuador is almost unique in South America in its strongly ingrained traditions of civility and political stability. Ecuador has been relatively untouched by drug trafficking and narcoterrorism. It has a competitive, reasonably productive work force. One expatriate manager interviewed noted that Ecuadoran labor productivity on a "per Dollar" basis is "much more productive" than its Andean neighbors, while on a "per head" basis it is roughly equivalent. Ecuador has a small but rapidly growing spectrum of experienced, competent technocrats and professionals who more than meet international qualitative standards. Its public officials were found by a number of private sector interviewees to be "unusually accessible." Its current government has undertaken or attempted to initiate a number of macroeconomic reforms, and it has recorded significant, even dramatic progress just recently in liberalizing its FDI and foreign exchange regimes.

8.0 ECUADOR: DISINCENTIVES FOR FDI

Normally, availability of positive FDI incentives will not, of itself, be a deciding factor in business decision making about whether or where to undertake FDI if the investment itself either doesn't make economic sense or the contraindications for such investment or "disincentives" to investment in the aggregate outweigh the positive impacts of incentives or impair the economic logic of the investment. Despite its laudable progress in recent initiatives to eliminate a number of overt barriers to FDI, Ecuador still exhibits a number of significant disincentives to FDI that, in the aggregate, will undercut any positive incentives designed to attract new FDI. These disincentives are both general and specific, in terms of the immediacy of their negative impact on FDI or potential foreign investors.

8.1 General Disincentives

Ecuador is lagging behind the pace of macroeconomic reforms and economic growth and prospects of most Latin American countries, especially its major competitors for attracting FDI, certainly those in this study. In particular, it is lagging behind the progress of restructuring of its economy. While Government rhetoric and policies suggest a disposition toward macroeconomic reform and restructuring and a number of initiatives in that direction have been launched, little real progress has been made in areas of principal concern to potential foreign investors.

8.1.1 Market Size

While Ecuador cannot change its physical endowments, it is significant to the thinking of prospective foreign investors that Ecuador is not as large in either area or population as its major Andean rivals for FDI. Its GDP is roughly 40 percent of Chile's, less than a third of Colombia's, and a fifth of Venezuela's. Its total consumption (a figure that roughly delineates its market potential) in 1991 was 41 percent that of Chile's, less than a third of Colombia's, and less than a fifth of Venezuela's. Its imports were a quarter of Chile's and Venezuela's and some 40 percent of Colombia's. Unless Ecuador can hold out the promise of according an unusually large percentage share of its small market or of being an effective export platform to the other member countries of the Andean Pact, potential investors are likely to pass up Ecuador for the volume gains and consequent profits realizable elsewhere. However it has—absent the disincentives discussed later—the opportunity to develop as a regional production and marketing center for the other Andean countries. In this regard, it already holds a geographical advantage over Chile with its more centralized location and an apparent advantage over its major Andean rivals in terms of wage costs. It is significant for its prospects as an export platform, however, that Ecuador counts only one other Andean Pact country—Peru—as one of its leading export markets. It appears that Ecuador's domestic producers have not found significant benefits in the Andean connection, perhaps for reasons beyond Ecuador's ability to influence, but, its performance to date does not suggest its attractiveness as a regional marketing resource to take advantage of the tariff preferences of the Pact. Even with its indirect market possibilities, given the small size of its direct market, Ecuador will have to make significant real progress in removing most or all of the disincentives described later in order to make an attractive location for future FDI.

8.1.2 Exchange Rate Volatility

Ecuador has experienced considerable volatility in exchange rates for the Sucre to the U.S. dollar and other hard currencies. In recent years it has repeatedly devalued its currency for domestic political purposes. Continued volatility of this degree makes it difficult to impossible for prospective foreign investors to forecast transactional costs in the importation or purchase of required resource inputs, foreign debt service, and to plan for tax liabilities as well as to price and sell items destined for global markets and compete effectively therein. Volatile exchange rates tend to reflect underlying economic and even political instability that makes it difficult to project return on investment, creates uncertainties for the future, and

thereby complicates and inhibits forward investment planning. It should be noted, however, that since an initial 35 percent devaluation under the Durán-Ballen administration, exchange rates have remained reasonably stable.

8.1.3 Inflation

Ecuador's 1991 inflation rate of 49 percent is well above those for the other countries studied and, while it appears to have slowed in the last year, is unlikely to meet agreed IMF year-end targets of 25 to 30 percent. Moreover, official inflation figures tend to be lower than private estimates of inflation which range well upward of 40 percent for 1993. As with exchange rate volatility, inflation reflects falling productivity and a deteriorating economy, unattractive characteristics for prospective foreign investment.

8.1.4 External Debt

Ecuador has the highest external debt as a percentage of GDP of the countries studied, indeed the only country whose external debt actually exceeds current GDP. Its outstanding external debt in 1992 amounted to US$12,960 million. It currently has one of the lowest debtor ratings in Latin America—reportedly a "D" rating—compared with Chile which recently received a BBB rating and Venezuela with a BB and Colombia with a B rating. Ecuador currently is in arrears on payments both of its external debt principal and interest. It has been unable to reach agreement on its private external debt with its bank creditors and it does not appear that an agreement for a Brady Plan rescheduling of its debt is likely in the near future. The pressure on foreign exchange reserves and credit rating occasioned by its external debt together with continuing uncertainty over the timing, nature, and distributive impacts of a payments accord add significant uncertainty to its overall economic position and make it difficult for industries and investors dependent on large-scale imports of needed inputs and foreign investment financing to plan for investments and operations.

8.1.5 Government Intervention/Competition

Although the new administration has articulated the Ecuadoran Government's commitment to modernization of the State in terms of privatization and reduction of government fiscal deficits, Ecuador still has one of the highest levels of State intervention in and control—direct or indirect—over its own

economy. Its industrial sector is characterized by substantial direct Government ownership or influence in what are normally private sector industrial areas including electricity supply, finance, water supply, tourism, oil, cement, sugar, fertilizers, and mining. Business International reported in June 1993 that there are still some 167 companies in Ecuador in which the State has a determinative ownership interest, many of which are 100 percent owned. The Government's "modernization" program provides for initiatives either to privatize State entities or to enable the private sector to compete with them in certain sectors. However, the Government's centerpiece legislative proposal for privatization (the "Modernization Law") has been effectively blocked in the Ecuadoran Congress and appears unlikely of passage in the near future without substantial dilution or overpoliticization. While substantial privatization of government-owned State entities could provide significant incremental FDI possibilities for the country, it appears that the modernization effort has bogged down, with the Government either unwilling administratively or organically unable legislatively to force it through to realization (although some say that much of the substance of the modernization bill could be accomplished without the law by administrative action. As a result, although prospective foreign investors have monitored the progress of macroeconomic policy reforms and the privatization initiative, there has been little, if any, follow-on interest demonstrated.

It should be noted as well that the Ecuadoran Armed Forces either directly or through military pension funds own or control and operate a substantial number of private commercial entities that compete with other businesses in the private sector while benefiting from customs exemptions and other privileges that reduce costs of inputs and enable them to undercut the business of competing firms. A major domestic airline, TAME, is owned by the military.

Concerns about the extent of government involvement in the economy whether directly or through the military are basically founded in their impacts on competition in the economy. The problems these present for Ecuador are exacerbated by the fact that much of Ecuador's private sector is characterized by oligopolies, narrow concentrations of ownership across sectors that result, in some sectors, in only a very few, large concerns whose presence and power inhibit competition and, thus, prospects for new investment.

8.1.6 Political Disorganization

While Ecuador has enjoyed some 10 years of democracy and has a long history of relative civility in its politics, the factionalization of its politics appears to have scrambled its

political system and its ability to achieve national consensus and cooperation necessary to effect wide-ranging macroeconomic reforms and restructuring. Its existing political institutions appear unable to accommodate any major degree of Executive-Legislative consensus or accommodation, while its Presidency appears either psychologically unwilling or structurally unable to force issues of reform through toward resolution. As a result, engagements between Government and the private sector remain essentially adversarial and little real progress of interest to prospective foreign investors is taking place. The new President's administration consistently articulates a rhetoric favorable to FDI and has managed to dismantle most of the legal impediments thereto, but its management of economic policy and of the Government bureaucracy has been unable to rid the country of major inhibitions to economic growth and disincentives to investment.

8.1.7 Officious Bureaucracy

Interviews with both private sector entrepreneurs and managers and public sector officials suggest a high degree of officiousness and corruption on the part of the Ecuadoran Government's bureaucracy, especially at the middle and lower levels which function at the day-to-day "confrontational level." There appears to remain within the entrenched middle level bureaucracy a still socialist style form of FDI xenophobia which sees foreign investment as essentially exploitative of Ecuadoran society and undermining of its sovereignty. The bureaucracy is alleged to substantially ignore the macroeconomic reform rhetoric and policies articulated by the President and senior ministers, while the Presidency seems unable to enforce policy conformity and discipline within the bureaucracy or, on some well publicized occasions, within the cabinet. Bureaucrats are alleged to violate the law on occasion and to continue to frustrate reforms and complicate, delay, and harass business firms and entrepreneurs, especially in highly regulated industries. Even if the government's modernization bill in the Congress were approved, some say it will be difficult to implement because of bureaucratic resistance and foot-dragging. Interviewees nearly uniformly complained at length about the bureaucracy's ability to create situations of increasing costs involved with any interaction with government, generating unnecessary complications, unreasonable demands, excessive delays in normally routine operations, and outright corruption with the situation reaching crisis proportions in Customs administration, the provision of Government-owned public services and the processing of labor disputes. A number of interviewees complained about the unnecessarily complex and lengthy import procedures and practices of Ecuadoran Customs. Costs associated with such procedures and delays, it has been

said, often surpass any tariff reductions or exemptions granted as incentives.

8.1.8 Government Deficits

One reflection of the overinvolvement of the Ecuadoran Government in normally private commercial activities is the continuing governmental fiscal deficits, attributable to major overstaffing of functions. The fiscal deficits squeeze resources for credit available to the private sector, drive up interest rates, and inhibit private investment and private sector business operations. Although the Government has agreed with the IMF to reduce the size of the Government Sector deficit to 0.5 percent of GDP, overall, Government deficits ran to some 2.5 percent of GDP in 1992. The Durán-Ballen administration has taken some actions to privatize government operations but its efforts to reduce the size and cost and increase the efficiency of government continue to be stymied in the Congress, which is motivated as much with partisan political advantage as by concerns for the impact of such initiatives on the social safety net.

8.1.9 Investment Financing Problems

A near-universal complaint encountered in interviews with private sector entrepreneurs and business people is the lack of medium to long-term investment financing, a problem that inhibits domestic as well as prospective foreign investment.

The Ecuadoran banking system is presided over by the Monetary Board and the Central Bank, which have charge of monetary policy and the implementation thereof, respectively, within the monetary, financial, exchange, and credit subsectors. The banking system is comprised of the Central Bank; public financial institutions like the Banco del Estado, the Corporación Financiera Nacional (National Financing Corporation), and the Banco Nacional de Fomento (National Development Bank); approximately 31 commercial banks, four of which are foreign-owned (Citibank, Bank of America, Lloyds Bank, and the Banco Holandés); and some 10 savings and loan and other finance companies. A number of other foreign banks are present (but not active) through representative offices. While foreign companies are not restricted as such from accessing local financial resources directly, foreign-owned banks are not permitted to accept and draw upon private savings accounts for investment lending purposes.

Ecuador's conventional legal interest ceiling is 49 percent, except for a number of specified types of loans for which the

legal interest rate can ascend up to 58 percent. These formal, legal rates, however, are often evaded through the imposition of commissions, fees, points and other charges, up to a combined "use rate" of as much as 70 percent. Foreign companies can borrow locally for investment purposes, with private commercial bank credit generally available for short-term financing and medium to long-term development loans mostly channeled through Ecuadoran Government financial institutions either directly or through relenting activities. Finance companies provide short and medium-term loans to commercial and industrial sectors for capital goods, fixed assets, working capital, and establishment and upgrading of industrial/manufacturing facilities.

The major complaints expressed about local investment financing are two: interest rates are much too high and the Ecuadoran commercial banking system is tribalized into extended family and other oligopolistic diversified economic groups (similar to Japanese keiretsu) which tend to service only the credit needs of their own members, often via unwise and economically unjustifiable sweetheart-style loans rather than providing credit generally on an economic rationale basis. The result of the tribalization has been the creation of a network of many small, closely-held, so-called "regional" banks and financial institutions some of which could not survive in a truly free, highly-competitive banking system.

Business people in the private sector, including a majority of bankers interviewed, agreed there was such tribalization of banks. But nearly everyone agreed as well that the major credit problem is not that there isn't enough money available as such - it was estimated that money in circulation has expanded some 60 percent in recent years—but that interest rates (driven up in the past by persistent Ecuadoran inflation at effective levels of 50 to 60 percent) have surged well past the real value of money while most of the available funds in circulation are used up in non-productive, non-investment-related speculative pursuits. Even though interest rates are now tending downward, the consensus of interviewees is that they continue to inhibit investment. On the one hand, the sheer size of the Ecuadoran public sector as a percentage of the country's overall economy is such that government deficits are said to absorb up to 70 percent of otherwise available capital. On the other hand, there is the impact of returning Ecuadoran fight capital—estimated at over US$9 billion in the aggregate—some US$350 million of which returned to Ecuador in 1992, because of the dramatically high domestic interest rates in comparison to other world rates, and is being devoted almost exclusively to short-term speculation in domestic interest rates and not entering the Ecuadoran direct investment stream.

Apparently the Ecuadoran Government recognizes and has tried to address the investment capital problem. First, it innovated

the recently-introduced, inflation-indexed "unidad de valor constante" or "constant value unit" in credit markets to ease the ratcheting-up impact of inflation on interest rates. Secondly, it enacted the recent "Ley de Mercado de Valores" (Securities Market Law) to revitalize and expand the scope of securities trading on the Ecuadoran Stock Exchange, created in 1969. The new law provides for new authorities for stock exchanges, securities houses, public offerings, subscriptions, and other market activities in stocks and bonds, under the regulatory oversight of the newly-established National Securities Council.

But, much of the real problem, according to interviewees, derives from a general business sector lack of confidence in the capacity of the Ecuadoran political system to deal with basic, structural economic issues confronting the country, including the size of the public sector, inflation, the external debt overhang, and the partisan constraints against achievement of macroeconomic policy consensus and implementation within the Government.

8.1.10 Infrastructural Problems

A number of interviewees, especially business people, noted that Ecuador's existing infrastructure is not attractive for FDI, especially in the areas of transportation and public utility services. Ecuador's infrastructure remains considerably less developed than in that in Chile, Colombia, and Costa Rica. With regard to the latter, they noted that most utilities are still State-owned and Government-operated and were so overstaffed but inefficient that they supply deteriorating levels of service at ever-increasing costs to consumers and they frequently charge prejudicially higher rates to industrial users.

Ecuador's telecommunications infrastructure is poor, and it is difficult to obtain service, deficient or not. Similarly, electricity supply is unreliable, and power outages are frequent. Multinational corporations simply cannot function without these essential services, and their scarcity poses an enormous impediment to FDI. Nearly all interviewed agreed that the clear solution to deteriorating services is to privatize most utilities although they expressed concerns about the resulting costs to users because of the likelihood that the Congress, as a precondition to such privatization, would effectively impair the new owners' efforts to achieve increased productivity at lower cost by significant cuts in the labor force.

8.2 Specific Disincentives

While Ecuador's overall economic climate and the various macroeconomic and political problems just described affect the domestic as well as the foreign business sectors equally, the nation has a number of specific disincentives either targeted directly on FDI or whose impact appears to fall more heavily upon foreign investors than on wholly domestic firms. These arise out of laws/regulations, government policies, and certain factual situations that have arisen in recent years.

8.2.1 Labor Regime

The single most frequently invoked specific disincentive to FDI is Ecuador's labor law regime. Although it affects all business firms, it has a particularly inhibiting impact on potential foreign investment. Although the minimum wage in Ecuador is lower than in most Latin American countries—and from a strictly labor cost standpoint Ecuadoran labor is more productive than in the other countries studied—nearly everyone interviewed complained about labor problems. The basic complaints are twofold: (1) the minimum wage is meaningless, and (2) the entire system is biased against and unfair to private enterprise. Moreover, an unduly rigid, prejudicial labor regime may be counterproductive since it tends to lead enterprises to seek investments in technology designed to reduce the overall percentage level of labor inputs.

Minimum Wage The "minimum wage" is figured, not on an hourly basis, but on a month's salary basis, but even that figure has lost any meaning because it does not accurately reflect considerably larger labor costs resulting from so-called "monthly wage add-ons" adopted from time to time over recent years, which now amount up to some two to five additional "months" of salary that must be paid to workers in any year. These have been added for purposes of Christmas bonuses, family support, educational expenses, etc. Interviewees complained that the existing Labor regime is out of touch with the economic realities of industrial development in a country in having competition with other countries for new FDI because wage liabilities have become essentially unconnected from productivity input/output or investment capacity. Apart from the excessive costs of current wage/benefits requirements, the system occasions irrational complexity in attempting to determine wage levels and salary payments correctly and make it very difficult for managers to quantify their wage liabilities in a manner that facilitates forward business planning.

Biased Labor Laws Nearly everyone interviewed expressed the opinion that the labor laws, processes, and adjudicatory

procedures adopted over recent years are highly politicized and "stacked against" management. They give rise to endless wrangling with unions while employers are required to pay workers while they are on strike, regardless of the merits of their complaints. This last requirement makes the threat or reality of a strike a form of extortionate leverage over management that effectively precludes meaningful negotiations and judicial adjudication of worker grievances since most employers cannot afford to idle production and still pay workers on strike or to wait out a strike through adjudication. One manager recounted how his workers seized and occupied his plant for two weeks while local authorities refused to take any action. It is believed at least one major former U.S. investor in the agribusiness sector abandoned its investment in Ecuador because of difficulties with the labor regime, while at least two business interviewees reported incidents in which prospective foreign investors cancelled contemplated investments because of the labor situation.

Two other major complaints surfaced. The Labor Code requirement giving workers the right to a 15 percent share of profits is a significant disincentive to FDI. The Labor Code provides for worker "stability" by requiring employers to pay separation indemnities to fire or lay off a worker. The basic separation payment amounts to one year of salary, regardless of the reasons for the separation.

These problems artificially raise the input costs for labor in an economy with considerable surplus labor. While all local business people interviewed expressed dismay at the impacts of the labor regime on private investment, some managers of foreign-owned companies said they did not find the labor situation so bad they couldn't conduct normal business profitably. They indicated that they, in effect, co-opted unions and labor agitators and diffused labor worker unrest by paying wage rates well above minimum scale, while striving to treat their workers according to U.S. or European standards. These noted that complaints of Ecuadoran managers of local firms tended to be founded in what they characterized as a distinctively Latin mindset that treats workers as just another resource input whose costs should be minimized and can be squeezed without concern for the human or social impacts.

The new Minister of Labor, in a speech to the Ecuadoran-American Chamber of Commerce of Quito, indicated that the Government was drafting a comprehensive legislative proposal for the Congress that would attempt to eliminate some and reintegrate the remaining monthly wage "add-ons" back into a coherent, integrated, more meaningful minimum wage/benefits computation procedure, while probably raising the resulting minimum wage. But he did not mention any changes to the labor law regime as such or to labor procedures, and business people interviewed were

skeptical about the chances for getting any real labor reform through the Ecuadoran Congress.

It should be noted also that managers of foreign-owned companies reported a form of discrimination against FDI in the administration of labor laws in that they were often the only companies to be targeted for inspections or enforcement actions regarding labor standards or work place safety, while domestic concerns with greater problems in those areas were largely ignored. These also reported that there was a high degree of correlation by Labor bureaucrats in selecting targets for enforcement and settlement and those (nearly always foreign) firms' ability to pay either officially or to provide "informal consideration."

8.2.2 National Treatment

Although Article 14 of Ecuador's Constitution provides that "Foreigners shall enjoy, in general, the same rights as Ecuadorans within the limits established in the Constitution and the law," study interviews elicited a number of allegations of non-national treatment of FDI, e.g., bias or discrimination against foreign investors.

It was alleged that foreign-owned companies are frequently targeted for labor and worker safety standards plant-site investigations and enforcement actions while more flagrant situations existing in locally owned plants are simply ignored. The situation was that foreign plants frequently are targeted for such actions as opportunities for corruption on a "what-the-market-will-bear" basis rather than from any genuine concern for Ecuadoran workers.

Similarly, the study elicited allegations in an industry sector subject to a higher than usual standard of regulation that nearly all foreign-owned companies were targeted for officious over-enforcement of quality controls largely because of the opportunities for informal consideration expected while domestic companies similarly situated were left alone.

As has been seen, foreign-owned banks are not allowed to accept and draw upon on local savings accounts for investment lending, while domestic competitors may do so. Finally, it was asserted that Government-owned utility and other services are routinely charged at higher unit cost rates to foreign-owned

concessionaires in the petroleum and mining sectors than are charged to domestic entities.[1]

Still, the problem of bureaucratic discrimination against foreign investors, while it exists, does not apply, apparently, across-the-board and seems limited to certain sectors. In this regard, local private sector interviewees noted that very recently the Managerial Committee of the Ministry of Commerce, Industry, etc. addressed the issue, dictating a resolution to the effect that foreign investors are, in all cases, to be treated just like domestic investors, with no special restrictions or limitations to be applied to them.

8.2.3 Property Rights

There were three basic areas of concern regarding foreign investor property rights from the study interviews. They are (1) legal restrictions against foreign ownership of real property; (2) certain abuses of property rights; and (3) at least one incident of effective—if not formal—expropriation.

Legal Restrictions At first glance, Ecuadoran restrictions on foreign ownership of real property appear minimal. Article 18 of the Ecuadoran Constitution provides that foreigners may not, directly or indirectly, own or acquire dominion or other real ownership rights in "frontier zones" or in certain so-called "reserved areas" except with prior authorization of law. Frontier areas include all real estate within a strip of 50 km wide along the borders of Ecuador as well as the Pacific coastline of Ecuador. In effect, the law prohibits foreign ownership or use except as permitted in frontier areas under the National Security Law by Ecuador's Joint Council of the Armed Forces or in reserved areas by concessions or other authorizations of competent authorities. Of much greater importance are the reserved areas. Article 46 of the Ecuadoran Constitution provides that certain areas of economic exploitation are reserved to the State, including "natural resources." Ecuador's Mining Law established a form of mining/petroleum exploration/exploitation contract between the State and successful bidders pursuant to which concessionaires enter into a "Risk Contract" with the Government that concedes to them the right to undertake exploration at their own economic risk for a period of years, usually four. If the

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[1]It should be noted that, although not specifically targeted against foreigners, a recent regulation was promulgated under pressure from domestic bankers preventing establishment of new banks, whether domestic or foreign. Consequently, the only way a foreign bank can enter the Ecuadoran market is by buying out or buying into an existing bank.

concessionaire declares a commercially-exploitable "find," the contract provides for a 20 year exploitation concession under which the State and the Company share profits realized after the company has absorbed its costs.

The problem has been raised in connection with certain tourism investments in Ecuador's Amazonian "reserved area." Tourism operators have asserted that they emplaced certain structures and improvements on military-controlled reserved areas with the passive consent of military authorities but could not obtain leases or other external indicia of legal rights thereto. Later, a concessionaire simply destroyed the tourism structures, leaving the tourism investors with no legal recourse for damage or loss of property because they had received no documentary evidence of the legitimacy of their presence on the land or of ownership of the structures and other property destroyed. Indeed, the investors' application to OPIC for investment insurance was denied, they say, for their failure to demonstrate legal rights in and to the land and structures.

Abuse of Property Rights A problem has arisen in recent years over the invasions by campesinos and ethnic Indians of properties held by foreign-owned (usually absentee) firms and individuals. Many of these properties are in mining concession or petroleum exploration/exploitation areas as well as in some tourism-adaptable areas, and even some in urban lands in the Guayaquil area, Ecuador's largest city. Although landowners are generally protected from such invasions under the trespass provisions of the Penal code, enactment a few years ago of a Land Redistribution law clouds the rights of "absentee landlords" over "unused" land, while the special Land Courts established under the Law to adjudicate issues of rights in the land and adverse possession are alleged to be biased in favor os squatters and to rule in their favor in the vast majority of cases. The problem is exacerbated for property owners because government police and military authorities have generally been reluctant to attempt the forcible removal of squatters and are generally tolerant of such invasions.

Expropriation Current and prospective foreign investors are acutely conscious of an only recently resolved instance that some have asserted reflects the real antipathy of the Ecuadoran Government toward safeguards for foreign investment. Emelec, the electrical utility servicing the Guayaquil area, had been in foreign ownership for many years. Apparently, under the prior presidential regime, the Ecuadoran Government made the decision that the utility should be pressed to sell off controlling interest in the utility to Ecuadorans. A syndicate of local investors proposed to buy the utility, but the owner thereof held out. According to versions heard from study interviewees, the Government then began a systematic campaign of legal and other harassment of the utility and its owner designed to force

agreement for the sale of controlling interest to the Ecuadoran syndicate. Eventually, the foreign investor characterized the Government's activities as the equivalent of a "taking" and demanded that the matter be referred to international arbitration. An international arbitral panel was commissioned to hear the case and to make recommendations as to sale and compensation. Ultimately, it issued what had been agreed among the parties would be a binding determination regarding the sale and compensation, fixing the compensation at a figure the Ecuadorans refused to accept. Eventually, the Ecuadoran Government refused to enforce the binding arbitration award and the foreign investor determined to take what he could and get out of the investment. Some interviewees associated with foreign-owned companies asserted that the results of Ecuador's abrupt rejection of "binding arbitration" would be to scare off any foreign investors from big-ticket investments in utilities and other high profile companies, and would have an especially crippling effect on efforts to privatize some of Ecuador's larger utilities.

8.2.4 Intellectual Property Rights

Regardless of the merits of ideological concerns about intellectual property and its protection, it remains a fact of economic life that a country's failure to adequately safeguard intellectual property of foreign firms and individuals in its markets acts as a deterrent to FDI, innovation, and the introduction of new technology. The U.S. Government concluded officially in 1992 that Ecuador does not provide adequate and effective protection of IPR and, in 1992, Ecuador was placed on its "watch list" under the "Special 301" provisions of its 1988 Omnibus Trade and Competitiveness Act. Managers of foreign companies in Ecuador interviewed indicated that they felt that, while the patent regime needed considerable improvement, they were relatively satisfied with the copyright protections afforded their intellectual property.

Ecuador is not a member of the Paris Convention for the Protection of Industrial Property. It is became a member of the World Intellectual Property Organization (WIPO) in 1988 and is also a member of the Berne Convention for the Protection of Literary and Artistic Work and the Universal Copyright Convention.

As a member of the Andean Pact, Ecuador's IPR regime is dictated by Andean Pact Decision 313 of December 5, 1991, which was implemented in Ecuador in March 1992, with implementing regulations in June 1992. Decision 313 provides for patent protection for 15 years, which can be extended for 5 years if local use is documented. Pharmaceutical products may be patented

except for those on the World Health Organization's list of essential drugs. The decision does not allow for so-called "pipeline" protection and permits some forms of compulsory licensing. Trademark registration is permitted for renewable 10 year periods, but may be cancelled if not used in the Andean Pact countries over a period of 5 years. Decision 313 prohibits registration of internationally-well-known trademarks, although the Commercial Attache's office of the U.S. Embassy in Quito reports registrations by other than legitimate owners have occurred. Copyright protection is based on the 1976 Ley de Autor (Law 610, R.O. 149, Aug. 13, 1976) which protects most printed and recorded materials but does not specifically cover software, although the Government has indicated its intention to seek such coverage. Although the Ecuadoran Government has said that infringement of IPR in <u>any</u> field is treated and penalized as a crime, and penalties were increased in 1992, pirating of recorded materials and software is said to be common. There appear to be no positive civil remedies of injunction or contempt to enforce the law.

Ecuador and the United States signed an IPR agreement on or about October 15. A copy of the agreement is not yet available, but it is believed that it includes provisions (1) applying all provisions of the Geneva Agreement on Phonograms, (2) requiring Ecuador to enforce the Paris Convention on Protection of Intellectual Property, (3) treating computer programs as literary works entitled to copyright protection and—if they are part of a patented system—to receive patent law protection, (4) for protection for encrypted satellite signals with unauthorized use thereof subject to criminal penalties, (5) extending patent law protection to pharmaceutical and certain other uncovered property, (6) protecting contractors' layout and integrated systems designs, (7) protecting trade secrets, and (8) mandating the Government of Ecuador to issue executive branch regulations to implement and enforce the provisions of the agreement.

9.0 <u>ECUADOR'S FDI COMPETITIVENESS: PROBLEMS & APPROACHES</u>

9.1 <u>"Openness" vs "Attractiveness"</u>

Of the four countries studied, Ecuador has the most "open"—on paper—FDI legal/regulatory regime. It has made significant, even dramatic, progress under the current administration in dismantling what was once one of Latin America's more onerous and biased FDI regimes. From the Constitution to Decree 415 to the new Ley de Mercado de Valores, Ecuador now has an entirely "neutral" policy of impartiality regarding FDI under which foreign investors are (or, under the law, are supposed to be) treated the same as domestic investors. Moreover, Ecuador appears

to have entirely deregulated its foreign exchange regime into one of the most open in Latin America and eliminated special taxation on remitted profits of FDI.

Unfortunately, many Ecuadoran officials and policy makers, as well as some advocates for the private sector, confuse "openness" with "attractiveness." The fact that Ecuador has become substantially "open" to FDI is only one aspect of "attraction" for prospective foreign direct investors. Vastly more important than openness-on-paper is investor confidence in the economy and in the system, governmental and political, that manages it. In a talk given October 18, 1993, in Washington, D.C., at an Andean investment conference sponsored by A.I.D., OPIC, and the Institute of the Americas, Ana Lucía Armijos, president of the Ecuadoran Monetary Board, acknowledged the importance of investor confidence. She said, "Ecuador subscribes to the point of view of the IDB and UNDP that the level and continuity of private investment reflects in general the level of confidence in the economy."

Nonetheless, it appears that many potential investors, domestic and foreign, simply do not have confidence in the way Ecuador currently manages its economy while foreign investors, especially, are concerned with how the system of government and politics work, wondering, for example, if the rules will change yet again with a new election and a new government—as Ecuador's political rhetoric often suggests. The difference compared to Chile and Colombia, is that, while their FDI admission/approval procedures are more complex, foreigners have confidence in the economies and in the system and believe Government guarantees that the rules won't change for them. Foreign investors are acutely conscious that host governments may reverse their free market policies and FDI liberalization initiatives if economic growth remains weak, if foreign companies do not transfer technology and skills as rapidly as expected, if world markets are closed, or political pressures threaten incumbent governments. Ecuador's "open" and unqualified FDI regime, while it imposes no burdens on FDI, also confers no guarantees for the future.

Also, the "climate" for foreign direct investment can be no better than the climate for domestic investment or business generally. Ecuador isn't "attractive" to prospective foreign investors because, while it may now treat foreign investors the same as it treats domestic investors, it doesn't appear to treat its own domestic investors very well. It is simply naive for Ecuadoran officials to believe foreign investors will find a country attractive for FDI when its own private sector entrepreneurs do not. FDI doesn't lead or catalyze domestic investment—it follows domestic investment. Foreign investors will only find a country attractive when that country's own domestic investors are willing to undertake risk-based investment in their

own economy, and they will do so only when they are convinced theirs is a dynamic, productive, growing yet stable economy. In this regard, Ecuador lags well behind the other countries studied, and most other major countries in Latin America, in macroeconomic reform, restructuring, and consequent economic growth and stability.

The recent liberalization of Ecuador's FDI legal and regulatory regime has had an impact among possible investors around the world. Ecuadoran officials and others described instances of a high degree of interest on the part of prospective foreign investors as a direct result of the liberalization, but, upon visiting the country and scrutinizing of its economic and political situation, practically no follow-up interest in actually investing there.

Ecuador starts out with certain built-in disadvantages in terms of its natural endowment of geographical size, location, and population, which affects its market size and potential. But, it is unfair to assay the desirability of Ecuador for FDI on the basis only of direct market potential (unless a foreign investor is assured of an unusually large share of its market) because as a member country of the Andean Pact, it has (or should have) favored access to the potentially much larger indirect markets of Venezuela, Colombia, Peru, and Bolivia. But, for the moment, for reasons internal to Ecuador as well as internal to the member countries of the Pact, including delay and complication of the trade preference regime, Ecuadorans have been unable to penetrate successfully most of these other markets.

But, added to problem of natural endowments (which Ecuador can do nothing about) and the unrealized potential of the Andean Pact (with regard to which Ecuador has little influence), Ecuador has a plethora of economic and political disincentives that effectively undercut its "open" FDI regime and have produced a climate unfavorable to investment, problems for which Ecuador must take principal responsibility and alone can resolve. Until Ecuador makes clearly effective and measurable progress in reducing or resolving these disincentives—a bloated public sector, inflation, external debt, volatile exchange rates, labor strife, lack of productivity, outright corruption, and political paralysis—its "openness" will be irrelevant to international FDI decision making.

The Government of Ecuador has made it clear it recognizes these many problems and concerns for prospective foreign investors. On August 13, The Minister of MICIP announced that the Government was in the process of drafting a "new industrial policy" which has as its object to attract foreign capital to Ecuadoran industry, and promised to table its initiative within 90 days. There may be short-term improvements Ecuador can undertake to reduce or at least ameliorate some of the disincentives

described earlier and improve the climate for FDI. These should be undertaken before resort to any new positive incentives. They are: installation of a so-called "one-stop shop" (Ventanilla Unica) to assist foreign investors; active pursuit of Ecuador's GATT application; liberalization of its debt/equity conversion legislation; and aggressive FDI promotion.

Ecuador's officious and often capricious bureaucracy is a clear disincentive to FDI. With their new, more open attitude toward FDI, a number of governments have sought to promote and facilitate FDI by offering potential investors needed information, advice, and assistance in navigating the maze of permits, approvals, licenses, and registrations required to establish or constitute companies and commence operations, e.g., facilitating contacts with Customs, the Superintendency of Banks, the Central Bank, immigration authorities, and various chambers of commerce and other institutions with whom the investor must deal incident to effecting his investment. For example, it appears there are some 14 separate steps involving some 90 days lead time required for the constitution, registration, and licensing of a new Ecuadoran company to do business <u>before</u> it can enter into valid contracts and actually commence operations. Many investor interviewees complained about the complexities and delays seemingly inherent in this process and any effective action to simplify and accelerate it for potential investors would certainly send a signal of the Government's genuine commitment to investment liberalization.

In this regard, it should be noted that Ecuador's Government recognizes the problem. Article 7 of Decree 415 quoted above enjoined certain public agencies not to demand compliance with more requirements than those contemplated in the law and implementing regulations. In the draft Modernization Law submitted to the Congress appear two articles that directly and explicitly address the issue. Article 16 of the draft, entitled "Unnecessary Requirements" charges CONAM, the National Council on State Modernization, to "identify functions that are developed in a repetitive form and unjustified administrative requirements and controls with the goal of taking action that will speed up and enhance public administration."

Article 18 "Legal Requirements" provides that neither the State nor other public sector entities shall require proofs other than those expressly required by law, nor shall they require information to prove facts that have not been controverted (as long as not otherwise found to be inaccurate), nor shall they request authorizations or reports not expressly called for in the law or require observance of any procedures not expressly provided for in the law.

The Ventanilla Unica should be authorized to develop the Government of Ecuador executive branch's FDI policies, coordinate

the activities of all government agencies with discretionary direct or collateral regulatory authorities over FDI, coordinate and oversee FDI promotion activities (although most such promotion should be delegated to or left in the private sector), and provide FDI informational and facilitating services to prospective and actual investors.

Establishment of a Ventanilla Unica for FDI in the executive branch would be the clearest, quickest, and most explicit signal to potential foreign investors of Ecuador's real commitment to the promotion of FDI and the seriousness of its determination to address disincentives for and obstacles to FDI. Both Chile and Colombia have such offices, and foreign investors around the world expect such a service as a reflection of a country's attractiveness for FDI.

However, to work efficiently and effectively, a one-stop shop service facility must have the clear authority and backing of the highest level of the Government in order to assure necessary coordination among agencies and the cooperation of bureaucrats at what is known as the "confrontation" level of the bureaucracy. Merely creating a one-stop-shop office in one of the ministries and citing it as an embodiment of the Government's desire for new FDI could actually result in more damage to Ecuador's prospects by raising and frustrating investor expectations if the personnel thereof are without authority and clout to command the respect and cooperation of the rest of the bureaucracy. It is important that a one-stop shop not simply evolve into yet "one more stop."

The structure of Ecuador's FDI promotion responsibilities remains unclear. Article 15 of Decree 415 provides that "MICIP shall coordinate the promotion of foreign investment which is developed by the various agencies of the public sector. Public sector agencies are required to furnish such information and technical assistance as required by MICIP to effectuate its promotional functions." Article 16 provides that "MICIP shall coordinate with the Ministry of Foreign Relations [with respect to] the signing of agreements to promote foreign investment as well as tax agreements to avoid double taxation. Diplomatic and consular representatives abroad shall actively support promotional programs designed to attract foreign investments, as well as furnish information and orientation to the investor." So, while MICIP is given authority to "coordinate . . . promotion"—and that promotion is somehow to be "developed by the various agencies of the public sector"—even after Decree 415 there still is no clear, explicit delegation among them of primacy to plan, develop, staff, and conduct FDI promotion for Ecuador.

Cognizant of this, the President issued Decree No. 459 of February 2, 1993, establishing the interagency National Coordinating Committee for the Promotion of Exports and Investment

(CONAPEI) and charged it "to establish and suggest programs directed at promoting investments, national and foreign, in Ecuador and traditional exports." CONAPEI includes representatives of the Private Sector including the President of Fundación Ecuador; presidents of the National Federation of Chambers of Commerce, Agriculture, and Industry; and the President of the National Federation of Exporters (FEDEXPOR). MICIP is delegated responsibility to provide staff support to CONAPEI and to identify and prepare projects for it. However, rather than a policy making or operational body, CONAPEI's role appears to be one of coordinating public and private sector activities in the areas of export and investment, but not necessarily FDI promotion.

Moreover, there appears to be some rivalry within the Government between MICIP and the Ministry of Foreign Affairs as to policy formation, staffing, and operational hegemony over foreign commercial activities with the result that little is actually getting done in the way of productive efforts to publicize Ecuador's new openness to FDI and its attractiveness therefor. In this regard, the Ministry of Foreign Affairs has apparently drafted and contemplates implementing a plan to "modernize and technify" economic and commercial efforts of the Ecuadoran foreign service which projects creation of Ecuadoran commercial offices in strategic locations around the world as well as enhancing and expanding the commercial promotion of investment and tourism by embassies and consulates abroad. On March 6, the Foreign Ministry entered into an agreement with FEDEXPOR for export promotion through export promotion centers in Miami, Hamburg, and two in South America as well as through its major embassies. But the Foreign Affairs Ministry appears to have tilted toward trade, rather than investment, promotion. Their initiative followed upon action by MICIP in September 1992 that closed 17 of its 19 foreign commercial offices abroad for budgetary reasons.

If the Presidency of Ecuador is really serious about actively promoting FDI in Ecuador, the Government needs to develop a forward-looking, coherent, measurable, results-oriented FDI promotion policy and strategy. It should be developed in close coordination and cooperation with the Ecuadoran Private Sector and should be exclusive in its focus and orientation, e.g., FDI. As a result, it should be run out of the Ventanilla Unica office within the Executive Office of the Presidency with direct oversight from the highest level of Government. The Presidency should create a specific Public-Private Sector Commission on FDI to advise and assist the Government specifically and only as to FDI and FDI promotion policies, strategies, and programs.

Ecuador is one of only two independent countries of the Western Hemisphere that is not a member of the General Agreement

on Tariffs and Trade (GATT), the international agreement setting rules subscribed to by some 120 nations of the world governing conduct in the area of international trade. Ecuador applied for GATT accession in September, 1992, but has only just recently tabled a draft document on its trade and macroeconomic regimes and has not yet begun real negotiations to become a Contracting Party. GATT membership is a precondition to any free trade agreement with the United States and all of the Andean Pact and other Latin American countries are already members. Since direct investment nearly always follows trade and the establishing of markets, a nation's absence from the major international trade deliberative forum is naturally a source of concern for prospective investors. Also, without membership in the GATT, Ecuador has no real standing to join with its fellow Central and South American nations to challenge EC restrictions on banana imports from their region.

What is of particular relevance to Ecuador's investment climate is that the Contracting Parties of the GATT are currently engaged in the so-called Uruguay Round of multilateral trade negotiations with the goal of rewriting existing GATT rules and developing new codes of conduct in such areas as Agriculture, Services, and Trade-Related aspects of both Investment and Intellectual Property Rights protection. The Uruguay Round negotiating group on Trade-Related Investment Measures (TRIMS) is attempting to bring worldwide consensus and discipline to certain national investment policies that inhibit or distort international trade, e.g., local equity requirements, domestic content rules, export or employment performance requirements, foreign exchange restrictions, etc. While Ecuador remains an outsider, it will have no voice or influence over the development of investment-related rules that may one day come to impact on its future investment decision making. In the same Round, the Contracting Parties are writing new rules on Trade-Related Intellectual Property, another area where Ecuador has some problems described above. Whatever IPR rules are elaborated will eventually become the international standard by which prospective investors will assess Ecuador's investment climate. Moreover, the GATT Code on International Standards governs most major trading nations. Ecuador will eventually have to implement such standards if it is to become a full participant in global trading, and to do so it will need to avail itself of assistance available through the GATT.

Given Ecuador's overhang of a large, unsettled debt, with its inevitable massive discounting on global secondary markets, it would make sense for the Government of Ecuador to extend its current debt conversion program to commercial enterprises for acquisitions of new or existing shares of private or public (especially as an inducement to privatization) companies or new shares of foreign-owned companies. The present program limits participation in debt swaps to nonprofit institutions with an

individual transaction ceiling of US$5 million. Under most debt-equity swap programs, investors purchase debt of a country at a steep discount and bring it into the debtor country through its banking system, where it is converted into local currency at its face value in order to effect an investment. The inducement to the government is that it helps retire external debts, whereas the inducement to potential investors is that they obtain more value in local currency than they could otherwise realize by disposing of the debt paper. Use of the debt-equity conversion facility for investment in private sector companies is permitted in Chile, upon Central Bank approval subject to certain conditions, for example,

- The capital may not be repatriated before expiration of a given period.
- Foreign exchange for the repatriation may be acquired only with the proceeds of the sale of shares or the total or partial liquidation of the investment.
- Profit remittances abroad are limited in the first 4 years; after that there are no limitations.

In regard to the last condition, a protocol to the recently signed Ecuador-U.S. bilateral investment treaty specifically provides that Ecuadoran deferral of repatriation of capital or remission of profits of debt-equity conversion programs is not prohibited by the treaty's guarantee of transfers without delay. By extending its debt conversion program, the Government of Ecuador could significantly increase the availability of financing for private sector (domestic and foreign) investments in industrial development. Chile, Brazil, and Mexico have debt conversion legislation that could serve as useful models for structuring such an expanded program.

The question now presented is, in the meantime (but <u>not</u> as an alternative thereto), can Ecuador build on its recent FDI liberalization by offering positive investment incentives that will offset or ameliorate its numerous disincentives to FDI?

9.2 Investment Incentives As Policy

Officials of other countries studied in this survey noted that, in general, the macroeconomic reforms and restructuring are usually accompanied by a trend away from the use of positive investment incentives for FDI because economic growth rates catalyzed by such actions generate the kind of dynamic, growing, stable economy that obviates the need for artificial inducements to invest therein, while at the same time, continuing such incentives acts as a drag on fiscal receipts, and result, on balance, negatively for the government. These same officials deplore the use of most positive investment incentives as a

substitute for required macroeconomic policy reforms and restructuring and resent other governments' resort to such incentives as a "handicapping" device in the ongoing Latin America-wide competition for new FDI.

Objections to incentives are twofold. According to these public officials and not a few business people, the basic economic objection to such incentives is that they tend to distort markets. The political objection is that they direct and defer public policy decision making away from the resolution of basic structural problems of the economy. As one official put it bluntly: "we don't think a country like Ecuador should consider starting an 'incentives war' in Latin America, because there are a lot of other competing economies that are larger and can beat them at their own game."

But this is not to say these same public officials opposed all use of positive incentives—only those that distort markets, which they see as a form of "unfair competition" and which, they note, may well violate principles of the General Agreement on Tariffs and Trade or "GATT." In this regard, a former high ranking public official of one of the countries studied, and one who has spent considerable time in analyzing incentives, noted that there may be two instances in which positive FDI incentives may be rational and useful. First, where there is, in fact, no existing market to distort, use of incentives to develop a market may be warranted. Second, incentives related to the economic development of a nation's natural resource endowments—like mining, petroleum, and tourism—would not be considered unfair if such incentives did not (1) discriminate between domestic and foreign investors or (2) among foreign investors by country. However, in certain cases (as with "big ticket" major utility privatization) wherein domestic investors clearly are unwilling or unable to generate sufficient risk capital to invest, incentives specially crafted to attract incremental FDI in the country may also be justified.

On the basis of study interviews and related research, it appears that the desirability and feasibility of investment incentives can be judged by certain criteria reflecting past experience of foreign investors. These include (1) the incentives are available on a widespread basis for a variety of economic and geographic areas; (2) they are available to foreign investors as well as domestic investors, in the case of foreigners, either directly, indirectly through a government entity, or via joint venture with a local firm; (3) the objectives of the incentives are consistent with the needs of foreign investors; (4) the incentives effectively reduce costs for foreign firms, e.g., land, labor, training, capital, raw materials, equipment, transportation, or terms of trade; and (5) the incentives are structured and administered to facilitate the grantee in locating

in an area where production costs are lowest but where access to product and labor markets is optimal.

9.3 Ecuador's Past Experience With Incentives

Ecuador is well-acquainted with positive investment incentives. Indeed, it appears that it only recently rejected incentives as an industrial development tool and dismantled most of its industrial incentives.

9.3.1 Industrial Development Incentives

The first Industrial Development Law was promulgated in 1921. The 1957 Industrial Development Law (R.O. 247) set forth the priorities and established the framework for the offering of incentives which came, in the years following, to represent the "industrial policy" of Ecuador. The 1957 law adopted recommendations and general designs developed by the United Nations Economic Commission for Latin America and the Caribbean (ECLAC). Its purpose was to promote and develop Ecuadoran industry, stimulate domestic and foreign investment in existing industry and future industry, and create employment. The Law was amended several times (1960, 1961, 1962, 1964 and it was codified in a new Industrial Development Law enacted in 1971 (R.O. 253, June 25, 1971) which repealed prior laws and set industrial incentives for the next decade.

It is important to an understanding of the role and impact of industrial incentives to divide recent Ecuadoran economic history into three epochs: (1) Pre-1972, (2) 1972 through 1981, and (3) Post 1982. From 1957 to 1971, the focus of industrial policy in Ecuador was to wean the country away from a dependency on and vulnerability to external factors in the global economy over which Ecuador had little influence but which often produced significant consequences for the nation. Policies were designed to encourage petroleum exploration and exploitation while promoting the expansion of Ecuador's domestic industrial base, in particular, the nurture of "infant" industries through import substitution. The period 1972 through 1981 marks the heady days in which Ecuador realized significant inflows of capital in payment for its exports of petroleum. During this period, the focus of industrial policy shifted toward the promotion of industrial development of certain regional areas as well as toward the development of sectoral areas likely to result in increased industrial exports. The third period reflects yet another shift in emphasis to deal with the impacts of the international oil debt crises and respond to the agreements

establishing the Andean free trade area by encouraging the diversification of Ecuador's export base.

The structure of positive investment incentives over the period from the 1957 Industrial Development Law through to the 1980s changed to reflect and accommodate the shifting policy targets for such incentives. From the beginning in 1957, Ecuadoran investment incentives have centered around tax exemptions, certain subsidies, and financial assistance. The 1957 law established three categories of industries, A, B, and C. Category A included industries considered basic for the economic development of the nation as well as those which produced goods that could substitute for importations; Category B included industries producing goods necessary for the subsistence and health of the Ecuadoran populace; and Category C included all other industries. The categories were established taking into account (1) salaries and wages paid; (2) the costs of raw materials and materials used in the manufacture of the products; (3) costs of machinery and equipment maintenance and amortization; and (4) energy costs necessarily to the enterprise.

Under the 1957 law, Category A and B industries received complete exemption from payment of customs duties and a 50 percent reduction of consular fees and export industries in that category received further concessions on import duties and exemption from export imposts. They also received reduced rates of income tax and were allowed to carry forward certain prior losses against subsequent income over four years. Category C industries received a reduction of 70 percent in customs duties payable and 30 percent in consular fees. They also received less generous reductions in income tax rates and a two-year loss carry forward.

Changes in the Industrial Development Law(s) enacted between 1964 and 1971 amended and added to incentives available. There was created an Interministerial Committee on Industrial Promotion comprised of the Ministers of Finance; Industry and Commerce; and Agriculture and Livestock; as well as a representative of the National Economic Planning Committee. There was added a new classification, the Special Category, firms engaged in high priority activities. Under a new Category A were included existing or new industries that exported or projected exporting at least 50 percent of their production or which produced goods needed in agricultural, fishery, mining or industrial production which could substitute for importations. The new Category B was defined to include all those industries that demonstrated an ability to contribute to the economic development of the country. All three categories received (1) total exoneration from business establishment taxes and fees; (2) similar exoneration from amendments to constitution and by-laws; (3) exemption from taxes on working capital; (4) complete exoneration from export duties and other charges; (5) full exoneration from import duties and

fees on imported raw materials; and (6) two years exemption from 70 percent of customs duties on imports of new machinery and parts. Participating firms were required to source all required goods for production domestically if available and to comply with all rules and regulations set forth to implement and administer the incentives. The Interministerial Committee established regulatory procedures for qualifying and administering the incentives and for investigating and enforcing compliance with all conditions imposed. Regulations were promulgated regulating definition of receipts and profits; local sourcing; classification of lines of production, and sale or other transfer of ownership of the enterprise.

"Reforms" to the Industrial Promotion Law were promulgated on June 2, 1965 by a Supreme Decree (R.O. 528) which added certain new incentives. All categories of industries were accorded exoneration from payment of all provincial and municipal taxes on transfers of improved real property to industrial enterprises. Firms in the Special Category were accorded exoneration from all sales taxes and permitted to accelerate depreciation on machinery and equipment up to a 20 percent of their investment. Category A firms received 100 percent exoneration from sales taxes for five years and Category B firms for 50 percent over the same period. Special Category firms received 100 percent exoneration from customs duties and fees for five years, and, thereafter, exoneration of 50 percent of consular fees on the importation of machinery and equipment. Category A firms received 100 percent exoneration of related customs fees and up to 40 percent of customs duties as determined by the Interministerial Committee for importation of necessary raw materials. Category B firms received exoneration from 100 percent of customs fees (other than duties) and from 50 percent of consular fees on machinery and equipment imports.

Reforms to the Law promulgated June 8, 1967 (R.O. 159) circumscribed a number of the incentives heretofore accorded because of the deteriorating fiscal situation of the Government and as a means of preventing abuses of incentives granted under the Law. Packing and shipping material was removed as a qualifying raw material import, the percentage exonerations from customs duties were reduced, and exemptions from consular fees and municipal sales taxes were repealed. The Law was once again reformed in June 1971 (R.O. 251) to implement agreements entered into by Ecuador with other member countries of the Andean Pact and to increase incentives for industrial development in financial, technology, and management areas. The changes included adding to the activities of the Special Category to include investments facilitating development of special geographical zones; and activities involving integration of the production of agricultural or raw materials with industrial phase of production. Fiscal incentives offered included the right to deduct initial investment in new enterprises and reinvestment of

earnings of existing enterprises from income; deduction of costs to increase production; deduction of accounting costs for computing income tax; and granting of a tax bonus of the value of exported production up to specified amounts. There was created a National Industrial Investment Fund to provide financing for industrial projects at below market interest rates and extended repayment periods.

It is interesting to note that, interviews with mangers of foreign-owned companies, most of whom initiated their investments in Ecuador in the decade of the 1970s, elicited statements that their companies elected not to invoke the industrial incentives described earlier for two major reasons: (1) their management felt that if the investment made any economic sense, they didn't need such incentives; and (2) taking advantage of such incentives would involve their company in extensive interaction with Ecuadoran Government officials in the areas of qualification, oversight, and enforcement to an extent they felt excessive, given that any such interaction nearly always had negative impacts and other costs.

A wide-ranging study of the effectiveness of the industrial incentives in realizing their goals of promoting industrial expansion, the growth of production, increased employment, maximization of domestic resources, and substitution-based self-sufficiency was conducted jointly by Ecuador's Center for Planning and Social Studies and the International Center for Development Research in 1990. They concluded that the expansion of the industrial sector that occurred during the period 1957 through 1986 was the result primarily of inflows of capital into the country occasioned first by the oil boom and then by the infusion of debt capital into Ecuador prior to 1982 rather than by industrial incentives. They found that the incentives were not a decisive factor for industrial growth and did not stimulate either the creation of employment, the use of domestic resources, nor adaptation of technology. And when, first the oil crisis and then the debt crisis dried up these sources of new capital for industry, the industrial sector lost its ability to expand notwithstanding the continued existence of such incentives. (Industrial Promotion Incentives in Ecuador: 1972-1986, CEPLAES-CIID, Quito, 1990.)

9.3.2 Export Incentives

In 1979, the Government enacted an export incentives law, the Ley de Abono Tributario a la Exportación (DS 3605, R.O. 883, Aug. 27, 1979), providing for the issuance of "Certificados de Abono Tributario" (CATs) granting a credit against various Ecuadoran taxes (apparently income and VAT taxes, but not import duties or export taxes or concession royalties due the Government). The law

granted a 50 percent credit for the value of agricultural exports, while exports of manufactures, handicrafts, and fishery products were granted a sliding scale of credits from 7 to 15 percent based on the percentage of Ecuadoran value-added to the total export cost of the product. In addition, products being exported to a new or "difficult access" market and non-traditional agricultural products (e.g., other than banana, cacao, coffee, or petroleum) received up to a 10 percent more tax credit. The granting of these incentives were suspended in 1986.

9.3.3 Other Incentives

Ecuador's Free Trade Zones Law and Maquila law, as well as special incentive regimes for agriculture, fisheries, and minerals, are described above.

9.4 Ecuadoran Business Views on Incentives

The CEPLAES-CIID study surveyed the opinions of Ecuadoran business people regarding the attractiveness and utility of the various positive incentives described earlier in promoting industrial development. In interviews conducted with 106 individual firms (8 percent of which were foreign-owned and 14 percent of which had some foreign capital), respondents were requested to rate and comment on the effectiveness of monetary incentives (concessionary credit programs) and fiscal incentives (taxes and customs duties).

The respondents clearly favored monetary incentives, feeling that the availability of subsidized concessionary or below-market financing from or though the Government constituted by far the most useful of the industrial incentives. This was explained in part because Ecuador's high inflation put the market costs of investment capital well beyond the reach of most investors. Moreover, uncertainties of inflation, and later on, the deregulation of foreign exchange, channeled most available private funds either offshore or into short-term speculation. It should be noted, however, that respondents indicated that only 60 percent of such concessionary financing went into new investments, while the rest was used for operating capital. The scarcity of investment capital—and thus the importance of the incentives—became more pronounced after 1982 and the end of the oil boom and the onset of the debt crisis. As important as they were, however, even monetary incentives were largely ineffectual in targeting new investments into specific regional development areas since, even with such inducements, investors remained leery of the lack of transport and distribution infrastructure and the isolation of such areas from markets and financial sectors.

Monetary incentives may actually have exacerbated the capital flight problem, to the extent they substituted for private capital they may have freed up private sector funds for sheltering offshore or speculation.

With regard to fiscal incentives, it is necessary to distinguish between the tax component (income, business establishment, VAT) and customs duties and fees. Approximately 50 percent of respondents reported availing themselves of exonerations from or reductions in business establishment taxes, although few found them to be decisive in investment decision making. What was of much greater interest is that less than 50 percent of respondents reported using (and depending upon in their investment decision making) incentives providing exoneration from or reductions in taxes on profits or working capital. According to the study, "It is difficult to determine if these results, surprising given the magnitude of the exonerations and deductions, are due to a general practice of evasion, deficient controls, or are simply not decisive for industrial activity." (One suspects a combination of poor tax administration/ enforcement on the one hand, and a generalized fear of involvement with the bureaucracy, on the other.) The CAT exporters' bonus incentive, which permitted exporters to deduct certain percentages of export income from taxes was found to have greater utility because it became, for investors, a sort of "hedge" against devaluation of the Sucre.

An even more surprising result surfaced when respondents were asked to evaluate incentives exonerating importers from or reducing the levels of import duties on imports of raw materials and capital goods. Over the three periods studied, the percentage of respondents availing themselves of such customs incentives fell from 54.5 percent before 1972 to 43 percent in the period 1972-1981, and rose again to 48.9 percent in the period since 1982. However, according to the study, of the average 34 percent of firms not drawing on the incentives, most were large enterprises with the ability to utilize their own resources or which considered the bureaucratic procedures too long and burdensome (the study did not indicate how many of these were foreign-owned). The authors noted, however, that 50 percent of Ecuadoran imports are duty-free while trading in contraband is common. They also voiced a suspicion that many firms were engaged in the illicit practice of over-invoicing imports and under-invoicing exports as a device to generate extra foreign exchange to use for speculation in exchange and short-term financial markets. Finally, they noted that customs duties are frequently simply added to costs passed on to customers, and that all of these factors, in the aggregate, effectively limited the utility of customs incentives as an industrial development tool. Overall, no more than 19 percent of respondents considered customs-related exemptions important to them. A much greater percentage complained of the negative impacts of import deposit requirements.

But, 13 percent of the firms—the majority of whom were foreign-owned or involved foreign capital—did recommend gradual reduction of customs duties to ensure future competitiveness of newer enterprises.

It should also be noted that a distinguished Ecuadoran attorney, whose firm has represented a number of foreign investors, actual and potential, opined in an interview for this study that positive investment incentives premised or targeted upon foreigners as opposed to domestic investors, would almost certainly be susceptible to legal attack on Constitutional grounds as violative of Articles 14 and 19 of the Constitución Política. Article 14, described at length earlier, provides that foreigners enjoy the same rights as Ecuadorans, while Article 19, Paragraph 5, provides that the State guarantees everyone "equality before the law."

Finally, there is another consideration raised in study interviews. For the moment, as a result of the liberalization of its FDI legal/regulatory regime, Ecuador currently has no general office or agency to "approve" new FDI. However, if new positive investment incentives are to be offered, their administration will almost certainly require that a new or existing government agency undertake to review, approve, and qualify and later administer and enforce all conditions to, such investments. This opens up Ecuador's newly liberalized FDI regime to the possibility of actually receding from its newly-found "openness." Some business people indicated that the benefits of the incentives might not justify such a development.

10.0 TOURISM: A PARADIGM FOR ECUADOR

Tourism is currently Ecuador's fourth largest earner of foreign exchange. Because it is such a distinct, clearly favorable area of potential foreign investment activity, and because Ecuador has accomplished so little in the area of effective inducements to FDI in tourism, we have selected that sector as a sort of case study, or paradigm, with the object of comparing the specific FDI regimes of the four countries studied to see how they utilize their FDI regimes to attract investment in the tourism sector, limit such investment, and/or reward such investment.

Tourism has a unique status as a development tool for the economic evolution of a country. It draws on a country's specific natural endowments and generally has a faster payback in contributing to economic growth by creating new jobs (often in areas where industrial development is unlikely) and introducing foreign exchange more rapidly than industrial development. In addition, as was seen earlier, the use of investment incentives

to encourage development of a nation's unique touristic resources is not viewed by other countries as an unfair form of economic competition, as is the case with industrial incentives. Tourism development represents what is probably Ecuador's fastest, surest route to incremental FDI given the disincentives earlier.

Ecuador has been an important tourist destination for decades and known by tour operators throughout the world primarily, and almost exclusively, because of its Galápagos Islands, consisting of 13 main islands with flora and fauna unique in all the world. Somewhat less well known tourist attractions of Ecuador include the country's rich colonial heritage; its colorful and artistic Indian ethnic heritage, and its relationships to the upper regions of the Amazon Basin. Another tourism asset, less well-known, are the mountains and valleys of its highlands. And, it also counts miles of Pacific Ocean beach. One would normally expect that, with these natural endowments, Ecuador would have experienced considerable development of its tourism resources. Especially so since tourism development offers the host country increased employment and foreign currency earnings for relatively little public investment, compared to other industrial sectors. Nonetheless, tourism, while the object of considerable public rhetoric, has been relatively ignored, and what steps the Government of Ecuador have taken have been generally unavailing of any surge of domestic interest (let alone foreign) in tourism development.

With practically no promotion, except the efforts of a few individual tour operators, the natural and unique attraction of the Galápagos Islands has resulted in a relatively small, stable, low-growth tourist industry. Still, despite Ecuador's lack of an effective, comprehensive, tourism promotion and investment policy, the country's natural tourist attractions earned it reported currency inflows of US$189 million in 1991 (fourth in terms of foreign currency earnings from "exports") and sectoral employment of just under 35,000 jobs. Notwithstanding these desirable results, there has been little growth in Ecuador's tourist industry over recent years (1989-1991).

In comparison, Chile had foreign currency earnings from Tourism of US$699.5 million in 1991 and has averaged over 50 percent growth per year. Ecuador's Andean neighbor, Colombia, reportedly earned over US$461 million in 1988 with continuing strong growth despite its problems of ongoing violence and political strife. Costa Rica this year (1993) projects total foreign currency earnings from tourism to exceed US$500 million.

10.1 Ecuador's Tourism Incentives

Ecuador, as has been pointed out above, does not discriminate between domestic and foreign investor in the sense of maintaining a separate, discrete set of positive investment incentives applicable solely to foreigners. Like the rest of its regime, the incentives available for investment in the tourism sector are the same for locals and for foreigners. The investment incentives are set forth in the current Tourism Law (Law 33 of 20 June 1989, R.O. 230, July 11, 1989) and its implementing Regulation of October 6, 1989 (R.O. 292, Oct. 11, 1989).

Article 1 of the Law creates CETUR (Corporación Ecuatoriana de Turismo) [formerly the Dirección Nacional de Turismo or DITURIS) and confides to it State powers relative to the promotion, development, and control of tourism. CETUR is empowered under the Law to (1) develop and direct the tourism policy of the country as well as to promote, regulate, and control tourism activities; (2) elaborate, implement, and evaluate tourism development plans; (3) set forth the administrative requirements for adequate levels of service for tourism, set and approve the rates therefor and establish registration, licensing and permit fees; and (4) supervise the education and training of tourism professionals. CETUR is governed by a Board comprising a delegate from the Presidency, the Minister of MICIP, Minister of Foreign Relations, Minister of Finance, and representatives from the associations for travel agencies, hotels, and airlines.

Articles 13 through 21 set forth Ecuador's incentives for Tourism development, consisting of "general benefits" and "special benefits." The general benefits provide (1) total exoneration from business establishment taxes, stamp taxes, and transfer fees; (2) stock transfer taxes; (3) exoneration from real property transfer taxes involving sales of tourism properties; and (4) access to preferential lending programs from Government financial institutions. This last incentive relates to the Government's Tourist Financing Fund, which can provide up to 170 million sucres to individuals or firms to cover operating capital and acquisition of assets for tourism activities such as hotels, restaurants, hostels, and other accommodations. The special benefits include (1) exoneration from customs duties and fees on the importation of construction materials, equipment, and implements required for a tourism development if not produced in Ecuador; (2) exoneration from customs duties, fees or other import charges on tourism-type passenger vehicles accommodating not less than 12 passengers that are devoted solely to internal tourism and which are not produced locally; (3) deduction, in determining taxable income, of the initial investment, additional investment, or reinvestments in the tourism enterprise, with the prior approval of CETUR when such investment is used for acquisi-

tion, construction, installation, expansion, or improvements of real property for tourism activities; and (4) deduction from taxable income of investments utilized in the financing of specific tourism promotion programs. This last deduction was withdrawn by Law 56 of 1989 (R.O. 341, Dec. 12, 1989) which also withdrew the deduction permitted to natural or legal persons for acquired stock of tourism enterprises.

The term of the incentives is specified as up to 10 years. The Law restricts the incentives to enterprises operating within Ecuador. But, similar to the elucidation of incentives under the Industrial Promotion Law, the Tourism Law parcels out these special benefits on a percentage basis determined by the category into which eligible firms are classified. Article 19 specifies the categories. Category A includes (1) tourism companies engaged in developing "high priority" [tourism] projects; (2) those dedicated principally to "social" tourism (e.g., low-cost tourism for workers, campesinos, students, etc.); (3) those establishing in zones or centers specifically declared (by CETUR) to be of touristic interest; and (4) those devoted to accelerated promotion of tourism. Category B includes those enterprises which, in CETUR's judgement, significantly contribute to national tourism development. Category C includes all other tourism-related enterprises. All categories are eligible for the general benefits. Category A enterprises are eligible for 100 percent of the special benefits; Category B firms for 75 percent thereof; and Category C firms for 50 percent thereof. Firms desiring to take advantage of the incentives must file an application with CETUR as prescribed in the implementing Regulation. These incentives remain in force and effect, although it appears the granting of such incentives has been effectively suspended, at least in part, because of pending legislation in the Ecuadoran Congress that would effect a number of changes in the Tourism Law.

The Tourism Law Regulation charges CETUR with establishing and maintaining a national tourism inventory. Its Article 7 defines tourism activities to include: providing hotel or living accommodations and complementary services; provision of food and drink; provision of recreation or entertainment services; provision of travel agency or tour services; tourist transportation via company-owned or leased vehicles; and publishing and editing of travel and tourism-related publications. Once an application for incentives is received by CETUR, its staff has up to 30 days to develop a report to the Board of CETUR (which grants the incentives) setting forth: suggested classification category; legal, financial, economic, administrative, and technical conditions that must be satisfied by or imposed on the applicant; specification of the periods within which the investment must be effected and operations commenced; and duration of the benefits. The incentives are granted via an "Accord" or resolution of the Board published in the Registro Oficial. Tax benefits can be

accorded provisionally to applicants prior to their formal submission of the application (Article 30) subject to a bond in the amount of the benefit and submission of the required application within four months. Incentive benefits can be transferred upon sale of the business only if the purchaser continues to conduct qualified tourism activities. Article 47 requires tourism entities (whether operating with incentives or not) to obtain an annual operating license from CETUR that sets forth its approval of their charges for goods and services. The cost of the license is figured as a percentage of business volume, e.g., the number of [hotel] rooms, [bar or restaurant] tables, etc. times a fixed percentage of the minimum salary (anywhere from 4 percent to 500 percent).

Under Article 66 of the Regulation, CETUR was granted the responsibility of undertaking promotional campaigns designed to create a tourism image for Ecuador. They were to do this by setting the policy and norms therefor but authorizing the implementation thereof by the private sector in the form of commercial promotion of Ecuador's tourism possibilities. Until Presidential establishment in August 1992 of a new Ministry of Communication and Tourism, CETUR was the lead Ecuadoran Government agency relative to tourism. With the establishment of the new Ministry under Executive Decree 4 of August 11 (R.O. 1, Aug. 11, 1993) in effect, CETUR retained staff administrative responsibilities but the Minister of Communications and Tourism became CETUR's Board chairman and the "Ministry" was given authority to set the Government's tourism policy.

We also established tourism as a paradigm for Ecuador because the Government's management of that important sector of its economy reflects a number of the disincentives to FDI and problems described above. For example, some individuals interviewed with connections to the tourism industry indicated that, whether or not there was a tourism law in effect (and at least one said there was not), it is clear the Government of Ecuador has no real policy on tourism development nor any effective program to promote either tourism or investment (domestic or foreign) in the tourism sector. While the Tourism Law described above clearly provides for the granting of incentives and confides authority to CETUR to administer and implement its provisions, there appear to have been no incentives granted under the Law. Similarly, while the Law provides for CETUR to elaborate standards of service for tourism, there are apparently none in effect. Moreover, despite the obvious intent of the Congress in passing the current Tourism Law, there remain collateral legal impediments that substantially operate to frustrate investment in tourism facilities, particularly in the most tourism-attractive areas.

In the area of standards, there are, at present, few quality control, safety, and environmental standards extant for tourism.

Service quality standards, boat and bus safety standards, and waste disposal norms for tourism facilities are left largely to the decisions of facility operators. While many of these facilities are insured and operated safely according to basic international standards, some tourist facility operators have ignored both quality and safety standards and remain uninsured, resulting in serious problems for all of Ecuador's tourism establishment. During the last few years, for example, an explosion and several deaths occurred on an unregulated tour boat in the Galápagos Islands, resulting in a warning issued by the U.S. Embassy in Ecuador.

As noted in the section on Ecuador's FDI regime, Article 18 of Ecuador's Constitution provides that foreigners may not, directly or indirectly, acquire real property in the frontier zones nor in certain "reserved" areas except as specifically authorized by law. As it happens, most of Ecuador's non-urban tourist attractions may be found within "reserved" areas, areas specially set aside for public ownership because of their natural resource endowments or for environmental or Indian population conservation and protection, the latter two usually denominated as "national parks." Private investors, whether Ecuadoran or foreign, may not acquire and "own" real property in such areas. However, in some cases, tourism firms have been granted informal "concessions" to develop such areas for limited forms of "ecotourism" or have simply entered such areas and constructed facilities—wharves, docks, lodges—with the passive indifference of local authorities.

In certain cases, a responsible government agency, usually the Institute for Natural Areas (INEFAN), has allowed such facilities to be built, depreciated, and taxed as if they were private property. But, apparently in no instance, was any external indicia of right to possession or use, e.g., a "lease" or "concession contract," formalized with the result that the operators of such facilities had no formal evidence of their rights to use such properties. In at least one well-known case of an operator of a floating barge/hotel for tourists in the upper Amazon region, a petroleum exploration company that had been granted a formal concession for the area tore down the tour operator's docks and other facilities. The operator, for lack of any external indication of the legitimacy of its use and occupation of such facilities, had no recourse at law for the value of the facilities lost. In another case, an U.S. investor was interested in a joint venture with an Ecuadoran tour operator involving lodging and other such facilities in the same area, but, for lack of a title or lease or other indicative of right-to-use, was refused OPIC risk insurance and subsequently withdrew from the venture. Another structural impediment to tourism development relates to the country's beaches. Also under the Constitution, beaches are reserved to State ownership and control. But, on a day-to-day basis, beach development and

maintenance is regulated by provincial and municipal authorities, with the result that prospective investors are unable to determine appropriate levels of government and contacts therein with whom to discuss requests for information and development proposals.

Another problem in tourism development is the piecemeal factionalization of efforts in both the public and private sector toward tourism and its promotion and development. A 1992 IESC study suggested there are as many as 14 different public or private sector organizations engaged in tourism development/ promotion or related activities or whose activities directly impact on tourism. These include FEPROTUR (Ecuadoran Foundation for Promotion of Tourism), the Ecuador Hotel Association, and the Association of Travel Agencies and Tourism. The Fundación Ecuador has also made tourism development and promotion a leading activity area for its membership and has advocated a number of initiatives on tourism with the Government.

Earlier this year, the Government submitted draft legislation to the Ecuadoran Congress to rewrite the Tourism Law to give organic legal existence to the new Ministry and to incorporate certain other changes into the tourism law. The bill drafted by the Presidency establishes, under the Minister of Communications and Tourism, a new Subsecretary of Tourism who exercises the Minister's duties vis à vis CETUR, but more important, expanded the set of investment incentives for tourism. The draft legislation reclassifies categories: Category A now relates only to projects located in lesser developed zones or regions and which "contribute to the generation of economies of scale." Category B now relates to projects of "high priority" established in defined special interest tourism zones. Category C are projects which, although they don't qualify for categories A or B, are found to contribute to national tourism development. And new Category D are projects that may be classified eligible within criteria established by the Board of CETUR. The "special" benefits, now called "specific" benefits in the draft legislation, run for periods and percentages determined by the category to which the applicant is consigned, as given in Table 1. It should also be noted that the Customs Duties exemptions available under the incentives have been expanded.

After the Government introduced its legislative proposal, the Ecuadoran tourism private sector gathered together to consider ways of amending the draft legislation to liberalize the scope of the incentives and to ensure private sector consultation and involvement in implementing a national tourism policy and the incentives for investment. In a letter to the Minister of Communications and Tourism of July 6, they recommended eliminating the classification categories so that all companies in any way

Table 1. Special Benefits Under Draft Legislation

Category	Customs Exemption (percent)	Income Tax Exoneration (years)	Investment Deduction from Taxable Income (percent)	Period of Incentive (years)
A	100	12	100	12
B	80	8	100	8
C	50	5	100	5
D	25	3	50	3

related to the tourism industry could avail themselves of incentives. They also recommended that all exonerations and exemptions be made total and that they run for 12 years.

Moreover, they directly addressed the problem of non-title tourism activities on public or "reserved" lands. The recommended to the Government new language (Article 30 of their redraft of the Government's draft tourism law) which provides that

> A tourist concession is a property right and fixture, distinct and independent from ownership of land, which may exist even when [both] are found in the same person. The property right emanating from a tourist concession may be asserted against third parties, is transferable and transmittable, susceptible of mortgage and, in general, to any act or contract, except for the constitution of estates. There shall be considered as accessory fixtures to the concession structures, installations, paths, and other goods and objects assigned permanently to its operation. The tourist concession is not susceptible of material division and may only be divided by percentages in stock or shares.

With regard to environmental consequences of tourism development, the group suggested draft language to the effect that "the tourist concession has as its goal to promote the protection of natural areas and their ecosystems, as well as ethnicity, customs, and traditions by means of tourism promotion." The redraft provides language to the effect that "The State may grant concessions over natural areas [reserved] to its charge. [But] prior to its concession, CETUR shall require presentation of an Environmental and Social Impact Study for the tourism project, as well as plans for prevention, mitigation, control, and compensation for its impacts." Under the language suggested by the tourism private sector group, such tourist concessions could

not exceed 1,000 hectares in size and would have a term of 20 years subject to renewal.

10.2 How the Other Countries Approach Tourism

10.2.1 Chile

Except for Law 600 which incorporates Chile's overall FDI regime, Chile does not provide any special positive incentives for foreign (or domestic) investment specific to its tourism sector. There are basically no limits on or discrimination against foreigners' investments in Chilean tourism facilities. Foreigners are permitted to acquire and own privately-held real property anywhere in Chile (with the exceptions of certain frontier restrictions on Argentines, Bolivians, and Peruvians). Foreigners as well as locals may acquire ownership or concessions to use public lands except in the same frontier areas. Non-resident foreigners may not own certain real property adjoining Chile's beaches up to 5 km from high water but foreigners resident in Chile may be allowed to rent and to construct improvements thereon by the Ministry of National Defense. While all beaches remain in public ownership, any person may receive concessions from the Ministry of Marine [Affairs] for from 5 to 30 years to construct and operate tourist facilities thereon.

Notwithstanding that it provides no specific incentives for investment in tourism, Chile experienced some US$138.4 million in new private investments in the tourism sector in 1991, with foreign investment accounting for 52.8 percent of it. Total private investment in the Chilean tourism sector grew 48.4 percent in 1991 over 1990 and 123.9 percent over 1989. Some 1,349,000 tourists visited Chile in 1991 accounting for foreign exchange earnings of US$700 million in that year, representing 20 percent growth over 1990 and 72 percent growth over 1989.

10.2.2 Colombia

Without discriminating between domestic and foreign investment, Colombia makes available certain positive incentives for investment in three declared "tourism zones": Baru, Pozos Colorados, and Guajira, all on its Northwest (Caribbean) coast. Although available to all investors, they were designed to attract foreign investment and tourism in these areas. Its incentives include Fiscal, Customs, and Financial rewards for investment. Corporate taxes are waived for 30 years for development activities. The exemption for end-users is calculated on a pro-rata basis reflecting the services sold to foreign

tourists. All goods destined for the tourism zones are exempt from customs duties, VAT taxes, and import regulations. Investors have total freedom to exchange currencies and to open bank accounts in foreign or national currency in either Colombian or foreign banks with complete freedom to remit capital and profits out of the country.

10.2.3 Costa Rica

Costa Rica's Incentives Law for Tourism Development (Law No. 6990 of July 30, 1985 as amended by Law No. 7293, G.O. No. 66, April 3, 1992) provides a complex and very specific set of positive investment incentives for major subsectors of the Tourism industry. The incentives are granted by means of a contract entered into between the Costa Rican Institute of Tourism, which administers the incentives, and the investor, which agreement must receive the approval of the Tourism Regulatory Commission. The Tourism industry is divided into five subsectors: (1) hotels, (2) national and international tourism air transportation, (3) water transportation for tourists, (4) tour agencies, and (5) auto rental companies.

Hotels may receive total exemption from all taxes and surcharges on either the importation or local purchase of articles necessary to the operation or installation of new enterprises as well as for the construction, expansion, or remodeling of structures (exemption does not extend to vehicles and fuel); accelerated depreciation of tourism properties for income tax purposes; thirty days granting of municipal operating licenses; authorization from the Central Bank to deal in foreign exchange with tourists; and six years exoneration from the "territories tax" for installations in non-urban areas. Air transportation firms receive accelerated depreciation; guaranteed supply of fuel at prices no greater than international market averages; and total exoneration from taxes and surcharges on the importation or local purchase of spare parts. Marine transport companies receive total exemption from taxes and surcharges on the importation or local purchase of goods necessary for the construction, expansion, or remodeling of wharves, docks, and passenger facilities as well as for construction and maintenance of marinas, warehouses, except with regard to goods from other member countries of the Central American Convention on Customs Regimen; accelerated depreciation; and total exemption from import taxes and surcharges up to 20 percent of the local cost of passenger vessels. Tourism agencies receive total exoneration from taxes and surcharges for transport vehicles accommodating at least 15 tourists. Auto leasing firms receive exoneration for 50 percent of the total duties on imports of autos destined solely for tourism rentals.

10.3 Indicators for Ecuador

There are at least three basic types of tourism: Specialized tourism (tourism drawing on a limited, specialized market of only a few individuals who will travel anywhere to satisfy their interests, pretty much regardless of amenities, e.g., diving, trekkers, hikers, rock climbers, and conservationists, game fishing, anthropology); Resort-oriented tourism (appealing to individuals who want to relax in self-contained resort environments, e.g., beaches, ski lodges, golf, health recuperation spas, casinos, etc.); and General tourism ("see-the-country" cultural/history-oriented tourism in which tourists visit areas of attraction or interest around a particular country, to sample culture, history, traditions, cuisine, amenities, history, etc.). Specialized tourism draws on a narrow market base that may be found anywhere in the world. Resort tourism represents the kind of tourism most frequently found in either beach or ski areas, relatively self-contained facilities (prime example: Club Mediterranée) that more or less hermetically seal patrons from the external environment. Markets for resort-type tourism are generally targeted on affluent European and North American tourists.

Ecuador has unrivalled specialized tourism attractions primarily oriented toward ecotourism in the Galápagos Islands and upper reaches of the Amazon Basin as well as extraordinary endowment of Indian heritage and culture. It has identifiable possibilities for resort style tourism in its Andean mountain regions and interior valleys, and possibly in some of its Pacific beaches. And it is, overall, a lovely, delightful country that will reward the broad interests of the general tourist. These natural endowments represent a huge potential for aggressive, targeted tourism development that may remain unrealized unless Ecuador develops a dynamic and coherent national tourism development and initiates and funds extensive foreign promotion of its tourism potential and opportunities for foreign involvement therein.

Ecuador's external debt overhang and internal scarcity of private sector financing (described earlier) suggest that the quickest, most efficient way to incremental investment in and realization of its tourism potential is an aggressive campaign through its public and private sectors to catch the attention of potential foreign investors, especially those major tourism organizations with the developed technologies and managerial skills to emplace attractive tourism infrastructure in the shortest possible time. To accomplish this, Ecuador must be willing and able to both facilitate and reward such investment. But to do so, it must be prepared to give up outdated and sometimes xenophobic concerns about national sovereignty and elaborate and pursue a national policy on tourism and a national

strategy for tourism development. Progress—or at least the perception of movement forward—is an essential factor in the worldwide competition for tourism investment and tourist dollars. In relative terms, the choices are only two: to plunge forward or get left behind because in a race of relatives, to remain still is to fall behind.

11.0 RECOMMENDATIONS

Following are a set of recommendations for both the Government of Ecuador in terms of suggestions for improving Ecuador's FDI climate and its attractiveness for new foreign investors, as well as certain recommendations for USAID/Ecuador for programs of assistance to the Government of Ecuador to facilitate some of the recommendations set forth herein. The recommendations for the government are categorized in terms of "short-term" action initiatives (activities that should be undertaken within a year and that could be productive of measurable results within that year or the next), and in terms of "medium-term" action initiatives (activities that should be initiated as soon as feasible, but whose accomplishment or impact may not be measurable in terms of results within the first 2 years).

11.1 Recommendations for the Government of Ecuador

Our recommendations for the Government of Ecuador represent a distillation of the ideas expressed by a number of persons interviewed in Ecuador and elsewhere as well as self-generated suggestions that we believe respond to the problems and issue areas discussed in this report. Some are necessarily general in nature, and others are specific. Our recommendations relate to the general FDI regime, macroeconomic policies, government bureaucracy, infrastructure and productivity, labor regime, trade-Related measures, and tourism.

11.1.1 General FDI Regime

Short-Term Action

Ventanilla Unica

- The Government of Ecuador should immediately establish a "one-stop shop," or Ventanilla Unica office, within the Executive Office of the Presidency to provide information, advice, and services to prospective foreign investors regarding FDI in Ecuador and to

simplify the steps necessary to enable such investors to effect their investments and to comply with the laws, regulations, and procedures required to realize their investment and commence business operations, such as constitution of companies, registration of investment, licensing to operate, obtention of worker visas and permits, and enrollment in appropriate cámaras.

- The Government's Ventanilla Unica office should be endowed directly by the presidency with the full authority of the presidency to command and secure the coordination and cooperation of all government agencies and bureaucrats whose authorities or activities directly or indirectly affect FDI and foreign investors.

- The organic authority of the Ventanilla Unica office as prescribed by the presidency should provide that regulatory and other agencies and officials of the Ecuadoran Government whose authorities, programs or activities (regardless of level thereof) directly or indirectly affect FDI or foreign investors shall consult in advance of such action and receive the opinion and counsel of the Ventanilla Unica regarding the effects thereof on FDI in Ecuador.

FDI Handbook

Ecuador's current FDI legal regime, consisting of all Ecuadoran constitutional provisions, laws, regulations, official policies, and treaty obligations directly affecting FDI, together with an accurate and adequate explanation of all collateral laws, regulations, or policies that have any direct impact on FDI, should be translated into English and other major foreign investor languages, and aggregated into a single publication and made available gratis to prospective investors on request or incident to FDI promotion activities both within Ecuador and through Ecuadoran embassies, consulates, and trade and other offices abroad. The Ventanilla Unica office in the Executive Office of the Presidency should take responsibility for this project and ensure its prompt publication, and the publication itself should be shown as emanating directly from the Executive Office of the Presidency.

National Treatment Review

The Executive Office of the Presidency should conduct a thorough review and analysis of all Ecuadoran laws, regulations, and official policies (including all collateral regulations and policies) that directly or indirectly affect FDI and foreign investors to identify and eliminate or modify any that do not

provide or require national treatment for FDI and foreign investors or that by letter or in practice via administration, adjudication, or enforcement, discriminate against firms owned by or enterprises constituting investments of foreigners.

Bilateral Investment Treaties

Building on the model of the recently signed Ecuadoran-U.S. bilateral investment treaty, the Government of Ecuador should continue to actively pursue opportunities for the negotiation of bilateral investment treaties with countries that may be sources of significant FDI in Ecuador.

GATT Accession Application

- The Government of Ecuador should vigorously pursue its application to become a Contracting Party of the General Agreement on Tariffs and Trade; should immediately respond substantively to all suggestions of the GATT Secretariat or other contracting parties to perfect its Protocol of Accession and GATT schedule of tariff concessions; should quickly follow up with responses to substantive enquiries posed by other contracting parties for omissions of information or supplementation or documentation thereof; should enter into early negotiations on all conditions and conduct any research or investigation or take corrective measures required to facilitate its accession.

- The Government of Ecuador should request whatever technical expertise or assistance it needs to facilitate the perfecting of a successful accession application from the appropriate sources for such assistance, including the GATT Secretariat and/or the U.S. Agency for International Development.

FDI Promotion Strategy Analysis

- The Government of Ecuador should immediately undertake action, through its Ventanilla Unica office in the Executive Office of the Presidency, with the advice and assistance of the private sector (as hereinafter described), to analyze Ecuador's areas of sectoral comparative advantage and other FDI selling points, and, on the basis of the analysis, conceptualize and develop an aggressive strategy for promoting FDI in Ecuador by identifying and targeting industry sectors and countries most likely to be receptive to the advantages of FDI in Ecuador.

- On the basis of the FDI promotion strategy analysis, the Government of Ecuador, with the cooperation and

assistance of the private sector, should develop and produce attractive promotional brochures describing the attractions and advantages of FDI in Ecuador for presentation to prospective foreign investors in Ecuador and through Ecuadoran embassies, consulates, and other offices abroad. The brochures should be made available to Ecuadoran private sector organizations, tour agencies, and other institutions that might act as multipliers for channeling the message of the advantages of FDI in Ecuador to prospective foreign investors.

Public-Private FDI Promotion Commission

While recognizing the initiative of the Government in establishing, and not impugning the utility of the Comité de Coordinación Nacional para la Promoción de las Exportaciones e Importaciones (CONAPEI) to promote investment in Ecuador, the Government of Ecuador should create and charge with development of FDI promotion and facilitation policy a body exclusively dedicated to FDI. The Government of Ecuador should establish a public-private Ecuadoran Commission for the Promotion of FDI, composed of senior level (no less than subminister) officials of all government agencies whose activities directly relate to or affect FDI and presidents or executive directors of leading private sector business advocacy organizations, including, in particular, the Fundación Ecuador, the binational chambers of commerce, and the Chambers of Commerce of Guayaquil and Quito, to advise and assist the Government—both the executive and legislative branches—in formulating policies to attract FDI and strategies for FDI promotion. Staff of the Ventanilla Unica of the Executive Office of the Presidency should act as Secretariat for the Commission. The commission would be the competent private sector body to cooperate and coordinate with the government in conducting the FDI promotion strategy analysis and developing an FDI promotion program.

Private Sector Working Groups

The Ecuadoran private sector should consider establishing wholly private, binational private sector working groups with representatives of the private sectors of major FDI-source countries, to further FDI by sponsoring the joint discussion of FDI issues of concern and common problems for investment similar to the U.S.-Colombia private sector working group created in May 1991 under the auspices of the Council of the Americas.

Medium-Term Actions

Investment Guarantees

The Government of Ecuador should devise a rubric for encouraging FDI through the granting of assurances to prospective new foreign investors that guarantee them that the FDI legal regime for admission and treatment established under Decree 415 (Ley de Mercado de Valores) and any further liberalizing legislation or regulatory action will not change or be substantially altered in substance or effect so that it diminishes or dilutes the current or any improved FDI regime under which investors may effect new investments. Such guarantee may be incorporated as part of an overall FDI code, by specific enactment of law, or by means of a contractual arrangement entered into by the state (through the Executive Office of the Presidency, facilitated by the Ventanilla Unica) and backed by the full faith and credit of the Ecuadoran state.

Constitutional Revision

The Government of Ecuador should initiate legislation or other effective action to amend Article 18 of the constitution to eliminate restrictions on foreign acquisition and ownership of real property anywhere in Ecuador except within 5 km of its frontiers.

Statutory Revision

- The Government of Ecuador should initiate legislation to amend its Mining Law, Civil Aviation Law, Radio and Television Law, Fisheries Law, and banking and financial regulatory laws to eliminate any sectoral restrictions on foreign acquisition, ownership, use or control of companies involved in such sectors, or foreign participation or ownership of shares or stock in Ecuadoran companies engaged therein.

- The Government of Ecuador should enact a single, comprehensive foreign direct investment code consolidating all existing laws, regulations, or policies (amended as described earlier) and incorporating the investment guarantees described earlier.

11.1.2 Macroeconomic Policy Reform

The basic attractiveness of any country for FDI is determined by its overall investment and business climates. Unless Ecuador makes measurable progress in removing or ameliorating the disincentives described earlier, no amount of

positive investment incentives will induce foreigners to invest in the country. The realities of Ecuador's current policy and political paralysis indicate that any recommendations regarding macroeconomic policy reforms and restructuring are inherently medium term in nature.

Privatization Law

The Ecuadoran Congress should enact the Modernization Law initiative without further limitations or politicization of the privatization process.

Structural Adjustment

The Government of Ecuador should take prompt action to implement the structural adjustment and macroeconomic policy reforms suggested by the IMF in order to avail itself of its stand-by support program as well as implement the macroeconomic policy adjustment conditions applied to multisectoral support lending by the Inter-American Development Bank.

External Debt

The Government of Ecuador should undertake more aggressive efforts to negotiate a rescheduling and/or settlement of its outstanding external debts with its international public and private creditors.

Investment Financing

The Government of Ecuador should promote an integrated financial services and capital markets infrastructure to rationalize the allocation of capital to productive uses and to provide an adequate supply of financing resources for capital investment, including FDI, and to encourage repatriation of Ecuadoran flight capital into productive, rather than speculative, investment.

Competition Law and Policy

The Government of Ecuador should enact a general anti-monopoly competition regime to reduce economic concentrations and oligopolistic manipulation of financial and other markets.

Political Consensus

The Government of Ecuador, Ecuadoran Congress, and Ecuadoran private sector must enter into a meaningful and productive dialogue to end the macroeconomic reform paralysis and develop a consensus approach for pursuing prompt, concerted, and effective

action to address and resolve or ameliorate the FDI negative impacts of the disincentives described earlier.

Private Sector Advocacy

The Ecuadoran private sector, through its representative advocacy organizations such as the Fundación Ecuador and its various cámaras, should develop better channels of communication, involvement, and effective influence on the formulation and effectuation of macroeconomic policy reforms and restructuring needed to renew business and investor confidence and stimulate economic growth.

11.1.3 Government Bureaucracy

Short-Term Action

Antiforeign Discrimination

The Government of Ecuador, through the Ventanilla Unica office of the Executive Office of the Presidency, should investigate and take action to ensure, through administrative action or legislation, that companies or enterprises with foreign shareholdings are not singled out for unreasonable investigations, inspections, enforcement or other administrative or enforcement actions, or penalties imposed on them, in the administrative implementation of any law, regulation, or official policy, solely because of their foreign ownership or foreign participation in their management or operations.

Bureaucratic Reform

- The Government of Ecuador, through self-generated administrative action or, as necessary, through legislation, should identify and eliminate all bureaucratic authorities, responsibilities, agencies, offices, or functions that are not essential to the implementation of laws, regulations, or official policies, or that are inconsistent with or inhibit or unduly delay such implementation.

- The Government of Ecuador should sanction and penalize all activities or actions of public officials that are not specifically authorized by law or regulation or that subvert, unreasonably complicate, or unduly delay the timely implementation of its laws, regulations, or official policies, with penalties therefor including dismissal from public office or employment.

Medium-Term Action

Anticorruption Law

The Government of Ecuador should submit draft legislation to the Congress to enact a comprehensive anticorruption law for the Ecuadoran bureaucracy, administering civil and criminal penalties for acts of corruption undertaken under color of law or the guise of administrative discretion involving the solicitation or receipt of bribes, kickbacks, extortion, informal consideration, gratuities, or retaliation of any kind premised on the failure thereof, in connection with the performance of official duties and responsibilities.

Administrative Procedure Law

The Government of Ecuador should enact a comprehensive administrative procedure law governing all actions taken in the implementation of laws, regulations, or official policies and establishing a coherent, consolidated rulemaking, adjudicative, and administrative procedure requiring elementary concepts of due process, transparency, fairness, and judicial recourse.

Civil Service

The Government of Ecuador should establish and develop a competent, nonpolitical, merit-based and -driven professional career civil service for the administration, implementation, and adjudication of the nation's laws, regulations, and official policies.

11.1.4 Infrastructure and Productivity

Similarly to our macroeconomic policy recommendations, recommendations for infrastructure and productivity are realistic only in the medium term.

Infrastructure

The Government of Ecuador must either invest heavily in new, enhanced public utility and transportation infrastructure designed to accommodate the production and distribution facilities required for increased domestic as well as foreign investment or privatize such services with inducements for the substantial new capital investment required to enhance such services.

Productivity Enhancement

- The Government of Ecuador should reevaluate its secondary and graduate educational system and worker training programs to provide modernized, technically proficient workers oriented to a good work ethic and capable of higher value-added production of goods and services for domestic consumption and export.

- In particular, the Government of Ecuador should consider increased funding for and expansion of its worker training programs, the Servicio Ecuatoriano de Capacitación Profesional (SECAP), charged with worker training, and promote increased private sector professional training opportunities such as the Centro de Formación Empresarial (CEFE). It should also investigate and consider replicating the Colombian government's National Apprenticeship Service (SENA), which provides apprenticeship and technological training programs through 115 training centers around the country, partially funded through employer payments into the service of the equivalent of 2 percent of their payroll.

11.1.5 Labor Reform

The following recommendations also are essentially medium term in nature.

Restrictions on Foreign Workers

- The Government of Ecuador should eliminate its ceiling on the employment of foreigners at least for professional or managerial personnel.

- The Government of Ecuador should liberalize and simplify its requirements and procedures for granting nonimmigrant work visas for foreign professionals and technical workers.

Minimum Wage

The Government of Ecuador should begin reform of its Labor Code and related laws and regulations to rationalize calculation of "minimum salary" such that the term accurately reflects the salary-per-work-unit, whether monthly or hourly, and eliminate the 13th, 14th, 15th, 16th, and other additions to monthly salary and other benefits, so that the resulting minimum wage figure can be used for accurate comparisons of wage rates in other countries and sectors.

Labor Code Reform

- The Labor Code should be reformed generally to protect and vindicate the rights and interests of both workers and employers and to encourage worker ethic and productivity and recognize and reflect the importance of investment to job creation and retention.

- The Labor Code should be reformed specifically to restrict by law any strike or collective action against an employer until the merits of the claim or protest on which such action is based have been adjudicated by a court of first instance, in order to remove the use of the strike as an extortionate form of leverage in labor disputes.

- The Labor Code should be reformed to prescribe a period of time (6 months, 1 year) from the date of initial employment, during which a worker shall be in the status of probationary employee who may be dismissed for cause without imposition on the employer of termination indemnities.

11.1.6 Intellectual Property

Medium-Term Action

IPR Agreement

Ecuador should immediately undertake the legislative and administrative actions necessary to implement the recently signed Ecuador-U.S. IPR agreement.

Paris Convention

Ecuador should accede to the Paris Convention for the Protection of Industrial Property.

Software/Semiconductors

Ecuador should amend its Copyright Law to extend copyright protection to software and semiconductor chip design.

11.1.7 Trade-Related Measures

The following trade measures may all be considered medium term in nature.

Export Taxes

The Government of Ecuador should eliminate all remaining export taxes.

Andean Pact Preferences

The Government of Ecuador should pursue a vigorous policy and strategy of diplomatic and trade initiatives with other member countries of the Andean Pact to accelerate reductions of tariffs and trade barriers in order to achieve realization of the trade preferences scheme and increase export opportunities to the Andean Pact region.

Nontraditional Exports

The Government of Ecuador should continue to encourage the development of nontraditional exports and facilitate increased production and exports thereof in order to attract potential foreign investors to such sectors.

Andean Trade Preference Act

On April 13, 1993, President Clinton designated Ecuador as a beneficiary under the Andean Trade Preference Act (ATPA), a unilateral trade enhancement program that broadens duty-free access for products originating from eligible countries directly entering the United States. The Government of Ecuador should work with USAID/Ecuador to sponsor seminars and distribution of information promoting increased exports to take advantage of the incremental export opportunities to be realized under the U.S. Andean Trade Preference Act. Promotion of Ecuadoran exports under the ATPA would complement the Government of Ecuador's efforts to increase nontraditional exports and could significantly expand its agricultural exports, an area in which it has a clear comparative advantage.

11.1.8 Tourism

Short-Term Action

Tourism Information and Assistance

The Government of Ecuador should emplace Tourism/Visitor Information/Service booths at its international airports and other major ports of entry to provide tourism information and visitor services designed to facilitate tourism.

Tourism Statistics

The Government of Ecuador's official statistics appear to include all foreign visitors as "tourists." For analysis and planning purposes, it should collect data that disaggregates "vacation tourists" from business and other visitors (especially "regional" tourists, who constitute half of all arrivals, 35 percent of whom come from Colombia). Data needed include total number of vacation tourists, country of origin, port of entry, average length of stay, average daily and total expenditures in Ecuador, kind of vacation, and good and bad experiences.

Development of Reserved Areas

Pending constitutional and statutory revisions to permit private investors to acquire and own real property in "reserved" areas, the Government of Ecuador should provide for tourism development in such areas by offering concessions or long-term lease contracts that provide tourism developers and operators with sufficient indicia of rights to use and operate to allow for legal recourse in the event of violation of such rights.

Medium-Term Action

National Tourism Policy and Strategy

The Government of Ecuador—with the substantial assistance and involvement of the Ecuadoran Private Sector, especially FEPROTUR, other tourism-related associations, and the Fundación Ecuador--should develop, establish, and pursue a national tourism policy as well as formulate a national strategy for tourism promotion and development that provides for strategic planning, goals, and benchmarks for governmental and private sector action to support and realize the national tourism policy.

Tourism Ministry

The Government of Ecuador should separate the tourism promotion and development function from the government information and propaganda function and establish a separate Ministry of Tourism with organic legal structure embodying the legal authorities to formulate, conduct, and exercise oversight over implementation of the national tourism policy and formulation of the national strategy for tourism promotion and development.

Policy and Strategy Prioritization

The Government of Ecuador should strive to compete by its strengths in tourism rather than by its weaknesses. Therefore, in formulating its national tourism policy and developing its national strategy for tourism promotion and development, the

government should prioritize toward ecotourism and other forms of specialized tourism that reflect its unique natural endowments.

Tourism Training

The Government of Ecuador/CETUR should privatize or contract out to private sector companies with special expertise and educational facilities its responsibilities under the Tourism Law for the training of its citizens in tourism management, services, and quality control up to internationally recognized standards for the same.

Medium-Term Action

Privatization of Tourism

- The Government of Ecuador, after having formulated its national tourism policy and national strategy for tourism promotion and development, should proceed to privatize most operational aspects of tourism promotion and development, transferring responsibilities to tourism sector operations susceptible of private investment, including FDI.

- In furtherance of the privatization process, the Ecuadoran Congress should enact the government's draft legislation for a new Tourism Law with the enhanced incentives for private direct investment (including FDI) contained in the amendments to the draft propounded by the private sector group described earlier.

Debt-For-Nature Swaps

The Government of Ecuador should amend its laws to encourage and facilitate debt-equity swaps for retirement of Ecuadoran external debt according to the debt-for-nature equity swap mechanism for the purpose of promoting the environmentally sustainable tourism development, especially in the Amazon Region and other environmentally sensitive areas.

Infrastructural Enhancement

The Government of Ecuador should undertake programs to substantially enhance and upgrade basic infrastructure (utilities, transportation, airports, etc.) necessary for or important to the optimum development of tourism in the country.

12.0 RECOMMENDATIONS FOR A.I.D.

The following recommendations describe program possibilities for providing technical assistance and expertise to the Government of Ecuador by the U.S. Agency for International Development, to encourage and facilitate the Government of Ecuador in implementing as many as possible of the recommendations enumerated previously. Most of the recommendations are for technical assistance that could be provided by the LAC/TI Project of the Office of Trade and Investment of A.I.D. Washington's Latin American/Caribbean Bureau upon request of USAID/Ecuador and drawing on other A.I.D. representative offices in Chile and Colombia.

12.1 Macroeconomic Policy Reform and Restructuring

A.I.D. should consider funding assistance to the Government of Ecuador in the form of technical expertise, advice, and services to the Government of Ecuador and the Ecuadoran private sector from officials, private sector business people, or academics from countries such as Chile and Colombia (facilitated through their A.I.D. representative offices) that have successfully pursued macroeconomic reforms, restructuring, and market opening and thereby stimulated and realized sustained, stable economic growth and expanded domestic and foreign direct investment. Such assistance should emphasize privatization, labor reform, competition and antitrust reforms, financial services, and programs to stimulate the return of flight capital and channeling thereof into productive rather than speculative investment.

12.2 Ecuador's GATT Application

A.I.D. should consider providing technical assistance to the Government of Ecuador to assist and facilitate its successful completion of its GATT accession application and negotiation of its Protocol of Accession and GATT schedule of tariff concessions.

12.3 Intellectual Property Rights

A.I.D. should consider providing technical assistance to the Government of Ecuador to enhance the country's IPR regime to international standards and, in particular, to facilitate

Ecuador's implementation of the recently signed Ecuador-U.S. Intellectual Property Agreement.

12.4 Trade-Related Initiatives

- A.I.D. should provide technical assistance and seminars to educate the Ecuadoran private sector in the export expansion opportunities presented Ecuador from the U.S. Andean Trade Preference Act. An intensive effort to promote ATPA opportunities would complement USAID/ Ecuador's Non-Traditional Agricultural Export (NTAE) project and could significantly affect Ecuador's agricultural exports.

- On the macro level, A.I.D. should consider providing policy advice and transactional expertise and services to the Government of Ecuador and the Ecuadoran private sector to encourage Government of Ecuador efforts to influence acceleration of Andean Pact trade preferences and reductions in tariff and nontariff barriers of other member countries and thereby stimulate opportunities for increased Ecuadoran exports to the region and interregional direct investment.

- On the micro level, A.I.D. should consider making available technical expertise and advice of Chilean government officials and Chilean business people to assist the Government of Ecuador and Ecuadoran Private Sector in stimulating, structuring, and effecting interregional trade and direct investment transactions in order to enhance the levels thereof.

12.5 Tourism

- A.I.D. should consider funding technical policy, management, and systems expertise and assistance to the Government of Ecuador/CETUR and/or FEPROTUR for technical investigation and analysis required to support their input into the development of a national tourism policy and development of a national strategy for tourism promotion and development.

- A.I.D. should consider (with reference to the possibility of making such information available to a number of country clients) funding an overall study of successful approaches and strategies used by developing nations for successful development of tourism and tourism promotion, including any positive investment incentives specific thereto.

APPENDIX A

FOREIGN INVESTMENT: BASIC CONCEPTS

A.1 Definitions/Concepts

Investment, whether originating domestically or from abroad, is divided into two basic types: "direct investment" and "portfolio investment." "Direct investment" describes an investment made to acquire and manage a continuing interest in the target entity. When the entity is located in one country and the investor is located in another country, the investment is referred to as "foreign direct investment." FDI is generally defined as ownership of 10 percent or more of the shares or voting power of an incorporated entity or the holding of a right to 10 percent or more of the profits of an unincorporated entity. Both the International Monetary Fund (IMF) and the Organization for Economic Cooperation and Development (OECD) chose the 10 percent threshold as indicative of an ability to control or at least effectively to influence the management of the enterprise. Ownership of less than 10 percent of an entity is referred to as "portfolio investment" and generally implies an essentially passive interest only in the earnings potential of stock in the firm.

Direct investment may be effected through (1) receipt of shares in exchange for capital (whether in cash funds or in kind); (2) reinvestment of earnings of the entity; or (3) certain "non-arms-length" financial transactions between affiliated enterprises. The "value" of a given FDI is generally determined by the actual capital contributed or the book value or recorded historical cost of contributed assets.

A.2 Legal Framework for FDI

The legal context or framework within which FDI is admitted and regulated in a country is known as the "FDI Regime" and includes the whole array within that country of constitutional provisions, laws, regulations, policies, and practices that, taken together, specifically establish and define the rights and obligations of both the foreign investor and the state with regard to FDI. This FDI regime may be supplemented by certain international conventions or treaties (multilateral, such as the Andean Pact Treaty of Cartagena, or bilateral, as in various bilateral investment treaties [BIT]) that confer certain rights or impose certain regulations on the signatory countries that may expand, reduce, or otherwise vary the rights and obligations of foreign investors and the state established under their FDI regimes. Additionally, there nearly always exists a broad spectrum of laws, regulations, policies, or practices in a

country that are not FDI-specific but nonetheless affect FDI and foreign investors in ways that can support or undermine the FDI regime and that are referred to in the aggregate as "collateral regulation."

Included in this spectrum are laws and regulations relating to corporate organization and business establishment, foreign exchange, taxation, technology transfer, protection of intellectual property rights, labor and employment laws and procedures, agency/distribution and licensing arrangements, and environmental regulations. Similarly, "collateral" international treaties or other agreements, such as agreements for the avoidance of double taxation, may also affect FDI.

A.3 Basic Issues in Investment Regimes

In many countries, an effort has been made to codify and encapsulate in a single body of legislation and implementing regulations the nation's basic provisions on the admission and treatment of FDI, known as "investment codes." The purpose of such codes is to encourage FDI by setting forth the legal and regulatory framework governing it; the rights and obligations of both foreign investors and the host country, including guarantees or special incentives the state is willing to accord FDI; the criteria for admission; and the process and procedures for approval or admission, or both.

Whether incorporated into investment codes or less formalized FDI regimes, the underlying context for FDI admission and treatment nearly always addresses four basic issue areas related to FDI: (1) admission, (2) treatment (including specifically standards for treatment and transferability or repatriation of capital and profits), (3) handling of expropriation,; and (4) procedures for the resolution of FDI-related disputes.

A.3.1 Admission

"Admission" refers to the legal regime and regulatory/administrative process through which FDI that already has occurred or may occur is recognized as such and accepted within a nation's sovereignty. Admission may be either "formal" or "informal." Informal admission refers to the entry of FDI as an accomplished fact in countries that have no established, formal process for recognizing or regulating FDI. Formal admission refers to the process by which actual or prospective FDI is recognized, approved, or regulated under legal norms and administrative procedures established in an investment code or other FDI regime.

Generally, the criteria for admission of FDI in a country with formal admission requirements will reflect the desires of the country to relate such FDI to the economic needs and priorities of the nation and to direct it to geographical areas or economic sectors considered to best serve the policy of the state.

A.3.2 Treatment

"Treatment" refers to the manner in which FDI will be received and treated within a country, in particular, the standards of treatment accorded generally to foreign investors. Generally, if specifically provided for, an investment code or FDI regime will accord FDI either "national treatment" or some variant of "fair and equitable treatment." National treatment implies that foreign investors and their investments will be accorded treatment exactly similar to that accorded domestic direct investors, that is, they will receive the same treatment as citizens of the country, or as is often stated, "treatment no less favorable than" that accorded nationals. Fair and equitable treatment constitutes a less specific standard that implies a broad range of possibilities but usually relates to treatment within a defined system of rules and regulations related to established constitutional and legal standards and internationally recognized considerations of due process. These standards of treatment may be expressed explicitly in constitutional form or in laws or may be established for nationals of signatory countries in multilateral or bilateral investment treaties or regional integration arrangements such as the European Community or the Andean Pact, described later. Frequently, however, foreign direct investors and their investments may, in fact, be accorded better treatment than nationals of a country, that is, accorded certain fiscal and other privileges not available to host country citizens under certain so-called "investment incentives" programs designed to encourage and target FDI in the country.

A particular area of concern for investors in the treatment of FDI has to do with the rights accorded or withheld regarding freedom to transfer to an investor's home country (or repatriate) capital and profits from the investment. From the standpoint of foreign investors, the ideal treatment would accord completely unconditional, unregulated transfer rights without limitation of the percentage of investment that may be repatriated or restrictions on the access to and use of foreign exchange to effectuate such transfers in hard currencies. Some countries guarantee the unrestricted right of repatriation for either capital or profits, or both. Others frequently condition it on a degree of reinvestment or subject to the availability of foreign exchange or to other national priorities. Many specifically tax such transfers through withholding on the amounts transferred in addition to

applicable local income taxes on corporate profits. Even where repatriation transfers are explicitly or generally authorized, freedom to effect them may be diluted by collateral regulations imposed in unrelated or non-FDI-targeted laws and regulations.

A.3.3 Expropriation

"Expropriation" refers to taking formally by title or otherwise by asserting ownership or right to control FDI by governments for public purposes, either without color of law or under constitutional or legal provisions that specify the grounds for such action, procedures therefor, and legal rights of investors including, most important, compensation and the method of calculating the value of the investment. Most countries specify that such taking may occur only "in the public interest," and laws or other authorities therefor usually will specify the manner of valuation and the form of compensation, although only a few require that compensation occur before the taking. The standard for assessing value and quantifying compensation may specify "fair and equitable" (usually based in investment treaties) or simply "fair" or "just," with determination in specific situations delegated to a host country court or administrative body.

A.3.4 Dispute Resolution

For "dispute resolution," unless otherwise explicitly governed under an investment code or international treaty, investment disputes between foreign investors and host country governments or their public or quasipublic agencies are subject only to adjudication in a local judicial or administrative system under the laws of the host country. When addressed in investment laws or regulations or in treaties, disputes may be subject to different types of arbitration, specific forums, local or foreign laws and arbitral procedures, or other conditions. Often, codes or FDI regimes will specify that the dispute may be referred to local courts only if arbitration or conciliation has proved unavailing in resolving the dispute.

A.4 Types of Investment Regimes

There are two main types of investment codes, open investment regimes and authorization or approval regimes. Within the second type are two identifiable subtypes.

Open investment regimes contain no stated special restrictions on entry or no special constraints beyond basic, internationally recognized, public order considerations. Open

codes usually provide that investments may be "freely made," subject only to specific provisions intended to safeguard public health, morals, the environment, and standard requirements for business organization and establishment.

Authorization or approval regimes require all or most foreign investors and all or most types of FDI to obtain special authorization for entry of the investment. These requirements may be imposed generally on all investors or investments, or on a selected priority geographical or sectoral basis. Authorization or approval regimes can be divided into two basic subtypes, high discretion and limited discretion, reflecting the degree and parameters of discretion accorded public officials to authorize and regulate FDI.

High discretion regimes impose few or no constraints on the discretion of public officials or provide no criteria to govern or guide such officials in reviewing and determining whether to authorize and approve FDI or impose certain requirements thereon as conditions precedent to such authorization or approval.

In many cases, however, apparently unrestrained discretion may be limited in practice by a provision of law or regulation to the effect that if no authorization or approval is granted within a specified time period, authorization or approval will be presumed; or by general principles of constitutional law or statutory due process that such discretion must be exercised in accordance with law. High discretion regimes typically involve provisions that restrict FDI to certain priority geographical or sectoral areas (or provide positive incentives therefor without excluding FDI from nonpriority areas) or impose certain performance requirements as conditions for authorization or approval, such as export, employment, or domestic content requirements.

Limited discretion regimes confer clearly defined criteria or limits to the exercise of discretion by public officials in administering investment regimes, for instance, specifying narrow terms on which authorization or approval may be deemed or providing for appeals of preliminary decisions reflecting the exercise of discretion.

A.5 Reasons for Foreign Direct Investment

It has been said that investment follows trade and trade follows investment, because the reality of international business is that FDI occurs as a result either of **market offense** or **market defense** strategies. Firms that try to participate in international trade generally follow a clearly defined scenario of foreign market penetration that begins with direct export sales

from the home country, proceeds to contracting of foreign sales representatives (agents, distributors), and eventually blossoms into one or more forms of FDI, beginning with on-shore sales and service capabilities, thence on to warehousing and inventory stores, then on to assembly or processing operations, and, ultimately, to vertically integrated manufacturing facilities.

The impetus and motivation for both trade and investment, and especially for FDI, relate to market penetration abroad and, therefore, to increasing and or protecting market share. Business decision making underlying FDI relates either to creating new markets or expanding existing markets or to market shares from current or likely competitors. When a firm confronts a decision whether to commit its resources to new FDI in a given country or to increase its existing FDI therein, it must address and resolve four basic criteria that together define the attractiveness of the investment and the extent of it. These critical decision making criteria are market size, comparative advantages, positive incentives for investment, and disincentives or contraindications for FDI.

A.5.1 Market Considerations

Market size defines the potential of sales and profits against which the cost of the investment contemplated must be weighed in order to project potential profits. Potential market size may be measured in both direct (population, disposable income, consumption, and level of economic growth of a country) or in indirect terms, for example, the number and size of third country markets that can be accessed and served through operations emplaced in the target country-sales, warehousing, service, or manufacturing. Firms considering whether to attempt to penetrate a given country's markets think about the country's potential and may evaluate the size of the country in terms of the desirability to realize either a large share of a small market or a small share of a large market. Consequently, the size of market potential is appraised in terms of a potential volume of sales and market share, not only in terms of the absolute size. New market opportunities in a country may occur because of population growth, growth of the economy and disposable income, macroeconomic reforms, and market-opening initiatives. An indirect market impulse may be a country's proximity to unprotected or newly opened markets.

A.5.2 Comparative Advantage

Nations, like individuals, are not all equally endowed with natural resources and other factor inputs to produce goods and

services, nor can they be isolated from the consequences of the history they have produced. In matters of international trade, which basically motivates FDI, the theory of comparative advantage can best be summed up in the saying that "nations should compete from their advantages and not from their disadvantages"; for example, a country should export what it can most efficiently and cheaply produce and import from other countries goods and services that it cannot produce as efficiently or cheaply but which other countries can. Whereas the ultimate judgment on the "if" and "where" of FDI is concerned with rate of return on investment, it is often comparative advantages—real (natural) or artificial (constructed)—that most often determine the bottom line aspects of rate of return.

According to a theory first proposed by David Ricardo in 1817, global economic exchanges of goods and services based on comparative advantage increase the wealth and well-being of all nations involved. According to Ricardo, a country has a comparative advantage in the production of goods it can produce more efficiently than other goods. Modern trade theory holds that regardless of the general level of a country's productivity or labor costs relative to those of other countries, the country should produce for export goods in which it has the greatest comparative advantage and import those in which it has the greatest (or a significant) comparative disadvantage. A country with few economic strengths will find it advantageous to its ultimate development to devote its productive energies to goods and services in which it has the fewest disadvantages while earning enough therefrom to support the costs of investment in innovation and technology required to enhance existing comparative advantages or develop new areas of such advantage.

The major areas of differentiation between countries being considered for investment tend to amount to aspects of comparative advantage, whether in local or international markets. A multinational corporation that finds it can more cheaply and efficiently produce locally for a given market as opposed to exporting to that market will choose to do so, absent other constraints. Similarly, a multinational corporation that can regionalize its production from a given locale through other markets more cheaply than producing in each of them will choose to do so. The elements for making these kinds of decisions include (1) comparative advantage, that is, the relative costs of inputs such as raw materials, labor, parts, supplies, transportation, and distribution; and (2) exogenous factors, for example, tariffs, quotas, export taxes, or even more general considerations such as strength of the economy, prospects for growth, business climate, and security of investment. The focus of this study is essentially on the more general, exogenous factors, especially actions that countries may take that result in "artificial" comparative "disadvantages" or to "construct"

artificial forms of comparative advantages through devices such as positive investment incentives.

It should be noted, however, that a country's comparative advantages are not static but can change over time as the country (or competing countries) changes and develops economically. Normally one of the first comparative advantages lost is labor costs, since it is most easily substituted by advancing technology or other factors. Therefore, comparative advantage in the production of a specific good or service must be analyzed continually in order to determine that adverse impacts are not the result of temporary or transient factors such as rapidly changing labor costs, exchange volatility, or resource costs such as energy and petroleum, whose prices vary greatly for economic and, often, noneconomic reasons.

A.5.3 Disincentives for Investment

Unfortunately, positive incentives to attract FDI are frequently used to cover up or offset serious disadvantages to FDI. Among the disadvantages to FDI that may repel it are performance requirements; political instability, a generally unfavorable business and investment climate, government resistance to macroeconomic reforms and restructuring, inflation, volatile exchange rates, poor public sector services and financial management, antiquated or overly legalistic laws and practices, corruption, export taxes or controls, monopolies, lack of investment financing or an active financial services sector, an unfair or highly prejudicial labor-management regime, and poor management culture.

A.5.4 General Incentives for Investment

General reasons that might impel prospective foreign investors to choose one country as opposed to another include a sound, stable economy; continuing progress in macroeconomic reform and restructuring; limited foreign exchange restrictions, especially on capital and profits repatriation; unrestricted use of expatriate managers and technicians; a favorable, supportive business climate; open, accessible, and growing local and regional markets; an effective, fair legal and regulatory regime; and adequate intellectual property rights protection.

A.5.5 Positive Incentives for Investment

Governments make available a broad spectrum of positive incentives to induce foreign investors to invest in their countries. Incentives are offered to attract investment to priority geographical or sectoral areas that would not otherwise meet investor demands or expectations in market size, comparative advantage, or resource mobilization. Sometimes, positive investment incentives are offered to rectify or counterbalance perceived disincentives or to offset risks identified. Even when there might already be good business reasons to invest in a country, a menu of investment incentives may attract investment away from a similarly situated country to the offering nation, thus becoming a deciding factor for FDI.

Tax incentives are frequently employed, especially to help develop burgeoning industries. For example, tax holidays—periods during which investing firms are either exempt from all taxation or offered reduced taxation—are frequently provided in specialized priority areas such as agribusiness, tourism, and various industrial or geographical areas. Exemptions from or reductions in excise, value-added, or other taxes may be offered. Exemption from or reduced rates on profits remission taxes, tax write-offs, accelerated depreciation, or loss carry-forward provisions are often made available. There may also be exemption from import duties on imported resource inputs, especially in free trade zones or maquila-like round-trip assembly and processing operations, as well as export tax exemptions, usually in labor-intensive industries or in countries with unusually low wage rates. Incentives frequently include drawback or recapture of duties paid on imported inputs used in the manufacture, assembly, or processing of goods destined for export.

Some governments provide financial incentives, including direct government loans at below market rates or reduced fees or loan guarantees for capital investment; interest subsidies for investment financing loans; export financing, loan guarantees, or insurance; joint venture investments; or special debt-equity investment possibilities drawing on steeply discounted foreign debts in hard currency exchange. Some governments provide special exemption from foreign exchange restrictions or guarantee the availability of foreign exchange for profits remission, capital repatriation, or current account payments abroad.

Countries may also try to assure investors of a guaranteed supply of resource inputs at favorable prices or volume preferential rates. In a number of import substitution-oriented countries, governments will attempt to insulate sectoral investors from import competition in the domestic economy by imposing higher tariffs, quotas, or tariff rate quotas. Some countries will enter into special incentive joint ventures to provide local

financing or guarantees or contribute land, buildings, or other available resource inputs in return for a share of equity. Often, countries will undertake to ensure availability of foreign exchange at preferential rates for current account payments or even for repatriation of capital and profits. Countries occasionally will act to insulate FDI from rigid labor codes or high labor benefits requirements or from legal sanctions or requirements imposed on worker separation; some provide government-subsidized worker skills training programs. In countries without significant comparative advantages, offering an array of positive investment incentives may itself become a form of artificial comparative advantage.

A.6 Basic Investor Concerns

The primary goal of any investor is to realize the highest possible (reasonable) return on his or her investment at the lowest (acceptable) risk. Thus, any serious investor will consider all reasonable alternatives for equal or greater return and minimize risks before deciding whether and where to invest. For a multinational investor, the rate of return compares the investment's share of the earnings of foreign affiliates (after foreign taxes), plus net receipts of interest on intercompany loans, to the net book value of its equity in, and net outstanding loans to, their foreign affiliates. It is sometimes figured as income receipts divided by the average of the beginning and year-end direct investment totals.

Normally, a basic factor in projecting rate of return is market size, the realizable share thereof, and the comparative advantages present to enable the investor to realize market share at the lowest possible input costs. Generally, the elements of projecting rate of return are quantifiable and can therefore be cranked into the kind of informed decisionmaking that precedes investment.

Risk, another element of investment, is inherent in free market economics. The options are simply to reduce risk to a minimum or insure, when possible, against it. Still, there are uncertainties. Business and commercial risks are always the most uncertain: downturns in the economy translate into higher costs or lower demand; bankruptcy or other impairment of suppliers or customers can sometimes occur without warning; new technology may be developed; competitors may make economic or technical breakthroughs. To the extent these risks cannot either be reduced or insured against, they must be assumed. The possible impacts of some risks can be insured. Political or currency convertibility risk may be insured through national agencies (Overseas Private Investment Corporation [OPIC]) or international agencies (Multilateral Investment Guarantee Agency [MIGA]).

Certain intangibles constitute concerns that must be confronted, evaluated, and weighed. A nation's FDI regime and legal-regulatory system must be evaluated, for example, by the investor's justifiable concerns for transparency, fairness, consistency, and predictability.

Finally, other significant concerns for the potential foreign investor are the effects of local taxes on the parent company's tax liabilities and the capability for remittance without delay of profits and repatriation of capital and taxes or fees applied. Similarly, the foreign investor must consider the procedures for investing in a target country, as well as the collateral requirements for establishing a company, bottlenecks, and delays. For many investment projects, the availability and cost of local financing may be an important risk reduction or sharing concern.

A.7 FDI Standards

Macroeconomic policy reforms in Central and Eastern Europe, South America, and even Africa have increased competition among countries for new foreign capital. Prospective investors have become much more discriminating in their expectations of and demands for standards for a host country. The U.S. Government, in its dialogue with Latin American and Caribbean countries under the Enterprise for the Americas Initiative, has outlined what it believes to be the minimal elements of an open investment climate, including

- Freedom from screening;
- Provision of national or Most Favored Nation treatment (with limited sectoral exceptions) whichever is better;
- Unencumbered transfers (of capital, profits, interest, royalties, fees, etc.);
- Freedom from performance requirements;
- Freedom to employ top management of choice regardless of nationality;
- Adherence to international law standards for expropriation;
- Granting access of investors to binding international arbitration; and
- Adequate and effective protection of intellectual property rights (IPR).

Creating an open investment regime also involves strengthening the general role of private ownership by eliminating monopolies and oligopolies; progressive privatization of parastatals; well-functioning capital markets; and transparent, fair, consistent, and nonburdensome regulatory regimes.

APPENDIX B

COMPARATIVE STATISTICAL INFORMATION FOR ECUADOR, CHILE, COLOMBIA, AND COSTA RICA

Table B-1. Social Indicators

Year	Indicator	Units	Ecuador	Chile	Colombia	Costa Rica	Source
	Geographical Area	000 km^2	271,000	756,945	1.14M	51,032	[1]
	(Land) App.	000 mi^2	109,000	302,778	440,000	19,652	
1991	Population (total)	0	10,503	13,360	32,873	2,875	[2]
1980–1991	Pop. Growth Rate	percent	2.4	1.7	2	2.4	[2]
1991	Urban Population	percent	56.9	86.2	70.5	47.6	[3]
1991	Rural Population	percent					
1991	Fertility Rate (births per woman)	0	3.6	2.5	2.6	3	[2]
1991	Life Expectancy at Birth	years	66	72	69	75	[2]
1991	Infant Mortality Under 5	per 1,000	64	20	43	20	[2]
1991	Population Density	per km^2	40.1	17.7	29.5	60.7	[3]
1989	Daily Calorie Per Capita	0	2,531	2,581	2,598	2,808	[2]
1992	Primary Sch. Enrollment	0	1,940		3,900	453	[4]
1992	Primary Sch. Enrol. Ratio	percent	113	98[3]	106	104	[4]
1992	Primary Completion Rate	percent	31			83	[4]
1989	Secondary Sch. Enrollment	percent	56	75	52	41	[2]
1990	Non-Literacy Rate	percent	14	7	13	7	[2]
	Work Force (year)		3.4M (1990)	4.7M (1989)	13.8M (1988)	1.0M (1990)	[1]
	Agriculture	percent	39	19	26	32	
	Industry/Commerce	percent	11	34	21	25	
	Services (incl. gov't.)	percent	42	30	58		
	Other	percent	8	9			
	Unemployment Rate (year)	percent	13 (1989)	7.3 (1991)	10.6 (1990)	5.0 (1991)	[5]
	Org. Labor/Labor Force	percent	15 (1982)	13 (1990)	8.2 (1989)	15 (1985)	[6]
1992	Net Migration Rate	per 1,000	0 (1992)	0 (1992)	—	1 (1992)	[6]
1992	Freedom House Ranking (free 1 2 3 4 5, not free 12, 13, 14)	0	5	4	6	2	[4]
1992	"Risk Index"		61	72.5	69	72.5	[5]
	Low 100, High 1		Moderate	Low	Moderate	Low	

Sources:

[1] U.S. Dpt. State Background Notes: Ecuador, June 1991; Chile, Nov. 1990; Colombia, Feb. 1990; Costa Rica, June 1992; Venezuela: Economic and Social Progress in Latin America, 1992 Report: Special Section - Latin America's Export of Manufactured Goods, IADB, Oct. 1992.

[2] World Bank Atlas (25th Anniv. Ed.), The World Bank, WDC, 1992, Pgs. 8,9.

[3] Economic and Social Progress in Latin America, 1992 Report, Special Section: Latin America's Exports of Manufactured Goods, IADB, Oct. 1992, WEC, pp. 285ff.

[4] Latin America and the Caribbean Selected Economic and Social Data, USAID, Wash., D.C., May 1993, Pg. 58.

[5] Business Climate Summaries: A.I.D./CDIE, Wash., D.C., Sept. 22, 1992.

[6] World Fact Book, C.I.A., Wash., D.C., 1993.

Table B-2. Macroeconomic Indicators

Year	Indicator	Units	Ecuador	Chile	Colombia	Costa Rica	Source
1990	GDP	US$ mil.	10.336	33,289	46,989	5,081	[1]
1990–1991	Percentage Reg. GDP	percent	1.5	3.9	5.4	0.6	[1]
1980–1987	Real GDP Growth Rate Av.	percent	1.1	1.1	3.2	1.6	[1]
1990	Real GDP Gowth Rate '90	percent	2.3	2.1	4.1	3.7	[1]
1992	Real GDP Growth Rate '92	percent	3.5	6.5	3	5.4	[2]
1990	GDP Per Capita	US$	1,260	2,527	1,425	1,685	[1]
1981–1990	GDP Per Cap. Av. Ann. Growth	percent	-0.9	0.9	1.4	-0.5	[1]
1990–1991	GDP Per Cap. Ann. Growth	percent	0.4	4.3	0.2	-1.3	[1]
1992	GDP Per Cap. Ann. Growth	percent	1.3	4.8	1	3.2	[2]
1991	Agric. as percent of GDP	percent	15	6 to 9	16	18	[3]
1991	Exports as percent of GDP	percent	31	36	18	39	[3]
1991	Invest. as percent of GDP	percent	22	19	16	23	[3]
1991	GNP	US$ mil.	10,772	28,897	41,922	6,156	[3]
1980–1991	Real GNP Growth Rate	percent	2	3.4	3.2	3.4	[3]
1991	GNP Per Capita	US$	1,020	2,160	1,280	1,930	[3]
1980–1991	Real GNP Growth Rate	percent	-0.3	1.7	1.2	1	[3]
1991	Inflation Rate (end of)	percent	49	19	27	25	[4]
1990	Consumer Price Index percent Chg.	percent	48.5	26	29.1	19	[2]
1991	Consumer Price Index percent Chg.	percent	48.7P	21.8P	30.4P	28.7P	[2]
1992	Lending Rate FQ/92	percent	49		45-50	To 49	[4b]
1990	Real Min. Wages/Growth Rate	percent	-10.2	1.8	0.5	-0.8	[1]
1991	Real Min. Wages/Growth Rate	percent	-15.2P	4.9P	-2.4	-5.8	[1]
1992	Exports/FOB [P]	US$ mil.	2,979	9,631	7,059	1,691	[2]
1992	Imports/CIF [P]	US$ mil.	2,260	FOB 8,594	5,569	2,402	[2]
1992	Capital Acct. Bal. [P]	US$ mil.	353	1,039	456	565	[2]
1992	Overall Balance [P]	US$ mil.	-61	293	1422	110	[2]
1992	Current Acc. Balance [P]	US$ mil.	-414	-746	966	-455	[2]
1992	Trade Balance [P]	US$ mil.	716	1,037	1,490	-711	[c]
1992	Outstanding Ext. Debt	US$ mil.	12,960	16,876	17	3,458	[2]
1992	Ext. Debt as percent of GDP	percent	104.7	45.8	32	55.5	[2]
1992	Debt Serv. as percent Exports	percent	20.6	25	46.7	20.3	[2]
1991	Debt Serv. Paid [P]	US$ mil.	1,117	2,973	3,872	512	[1]
1991	For. Exchg. Res (ex Gold)	US$ Bil.	9.24	7.04	4,212	920	[5]
1987–1991	Ann. Rate of Chg. (ex Gold)	percent	17	18	-3.4		

Sources:

[1] Economic and Social Progress in Latin America, 1992 Report Special Section: Latin America's Exports of Manufactured Goods, IADB, Oct. 1992, WDC, Table B-1, Pg. 286.

[2] Latin America and the Caribbean Selected Economic and Social Data, USAID, Wash., D.C., May 1993.

[3] World Bank Atlas, (25th Anniv. Ed.), the World Bank, WDC, 1992, pgs. 18-19.

[4] (a) World Factbook, CIA, Wash., D.C., 1993. (b) Andean & Caribbean Financing Directory, Dept. of Comm./ITA, Oct. 1992, pg. 122.

[5] Business Climate Summaries: A.I.D./CDIE, Wash., D.C., Sept. 22, 1992.

Table B-3. Investment Indicators

Year	Indicator	Units	Ecuador	Chile	Colombia	Costa Rica	Source
1991 [P]	Gross Domestic Invest.	US$ mil.	2,993	7,620	8,450	962	[1]
1971-1980	Av. Annual Growth Rate	percent	10.4	2.8	5.1	9.3	[1]
1981-1990	Av. Annual Growth Rate	percent	-3.4	0.6	0.9	1	[1]
1990-1991	Annual Growth Rate	percent	4.1	1.9	-2.5	-27.1	[1]
1991	GDI as Share of GDP	percent	21.8	18.8	17.2	23.3	[2]
1991 [P]	Private Direct Investment	US$ mil.	81	576	479	109	[1]
1991	Foreign Direct Inv. Net New	US$ mil.	85	576	457	142	[3]
1991	FDI Share/Gross Don. Inv.	percent	3.4	9.8	7.2	11.1	[3]
1991	U.S. FDI Pos. (Acc. Total)	US$ mil.	337	1,555	1,744		[4]
1989	U.S. FDI Position as percent of LAC	percent	0.6	1.5	2.8		[5]
1980-1984	Av. Annual Rate of Growth	percent	6.1	-3	23		[5]
1984-1989	Av. Annual Rate of Growth	percent	1.7	93.1	1.2		[5]
1989	U.S. FDI Position all Industries	US$ mil.	395	1,018	1,900		[5]
1989	U.S. FDI Pos. Wholesale Trade	US$ mil.	42	37	58 (1987)		[5]
1989	U.S. FDI Pos. Banking	US$ mil.	0.5	261	8		[5]
1989	U.S. FDI Pos. Financing	US$ mil.	0.5	282	0.5		[5]
1989	U.S. FDI Serv. & Other Indus.	US$ mil.	1	216	1		[5]
1989	U.S. FDI Pos. Petroleum	US$ mil.	125	51	306		[5]
1989	U.S. FDI Pos. Mfgring.	US$ mil.	168	170	626		[5]
1992	"Risk Index"		61	72.5	69	72.5	
	(Low 100 -- 01 High)		Moderate	Low	Moderate	Low	[6]
1992	Freedom House Ranking (free 1,2 -- 13, 14 not free)		5	4	6	2	[2]
1991	Total Consumption (Mkt.)	US$ mil.	10,216	25160	37,113	4,047	[1]
	Org. Labor percent Total Labor	percent	15 (1982)	13 (1990)	8.2 (1989)	15 (1985)	[7]
	Force Wages (see Part 2)						
1991	Tax Rev. as percent Curr. Rev.	Ppercent	98.4	65.8	88.9	96.9	[1]
1991	Dir. Taxes as percent Curr. Rev.	Ppercent	58	19.6	40.6	16.6	[1]
1991	Income Taxes as percent Curr. Rev.	Ppercent	9.9	19.6	40.6	14.3	[1]
1991	Prop. Taxes as percent Curr. Rev.	Ppercent	0.3	0	0	0.8	[1]
1991	Indirect Taxes as percent Curr. Rev.	Ppercent	40.4	46.1	48.3	80.3	[1]
1991	Prod. & Sales Taxes as percent						
	Curr. Rev.	Ppercent	25.7	37.3	26.7	51.3	[1]

Table B-3 (continued)

Year	Indicator	Units	Ecuador	Chile	Colombia	Costa Rica	Source
	Research/Dev. Expenditures	US$ mil.	14 (1973)	95 (1988)	52 (1988)	12 (1986)	[1]
1989	High-Tech Trade: Imports	US$ mil.	961	3,505	2,720		[1]
1970-1989	Growth Rate: High Tech Imp.	percent	10.8	10	10.5		[1]
1989	High-Tech Trade: Exports	US$ mil.	14		208		[1]
	No. of Scientists/Engineers in R&D	per 1,000	2.6	3.6	0.3	1.7	[1]

Sources:

[1] Economic and Social Progress in Latin America, 1992 Report. Special Section: "Latin America's Exports of Manufactured Goods," IDB, Oct. 1992, WEC, Table B-5.
[2] Latin America and the Caribbean Selected Economic and Social Data, USAID, Wash., D.C., May 1993, Country Profiles.
[3] Global Economic Prospects and the Developing Countries, The World Bank, 1993, pg. 76.
[4] Economic Survey of the United States, 1991, ECLAC, WDC, Aug. 1992, Table 4-1, pg. 49.
[5] Latin American and Caribbean Trade and Investment Relations with the United States in the 1980s, ECLAC, WDC, Nov. 1991.
[6] Business Climate Summaries, A.I.D./CDIE, Wash., D.C., Sept. 22, 1992.
[7] World Fact Book, CIA, Wash., D.C., 1993.

Table B-4. Revealed Comparative Advantage: Manufacturing Exports, 1988-1990

Indicator	Units	Ecuador	Chile	Colombia	Costa Rica
RCA: Apparel	RCA UL	0.86	0.94	5.38	4.39
RCA: Chemicals	RCA HC/T	1.89	5.39	0.70	0.18
RCA: Electric Mach./App.	RCA HC/T	0.56	0.90	0.13	0.83
RCA: Footwear	RCA UL	0.00	1.96	2.75	1.12
RCA: Iron & Steel	RCA HC/T	0.32	1.58	2.88	0.85
RCA: Leather & Leather Manufacturing	RCA UL	0.10	0.36	7.09	6.68
RCA: Non-Electrical Machinery	RCA HC/T	0.15	0.90	0.15	0.12
RCA: Non-Metallic Min. Manufacturing	RCA NR	1.97	0.68	3.85	1.48
RCA: Paper Manufacturing	RCA NR	0.41	4.67	0.50	0.96
RCA: Plastics	RCA HC/T	0.13	0.36	2.25	0.74
RCA: Textiles Yarn & Fabric	RCA UL	3.35	0.62	1.96	1.59

Notes: UL = unskilled labor-intensive. HC/T = human capital/tech-intensive. NR = natural resource intensive.
Source: Appendix Table 7, pp. 266–267, in "Economic and Social Progress in Latin America," 1992 Report, Special Section: Manufacturing Exports, Inter-American Development Bank, Washington, D.C., October 1992. The report cites the following rationale behind the data in the table (pp. 203, 205): "[A country's] objective has been to promote those exports in which the country will be able to compete effectively in the world market. For this to happen under relatively free trading conditions, the products exported . . . must reflect their relative cost advantages in production, marketing, and distribution. . . . The index of revealed comparative advantage (RCA) adjusts a country's exports for the size of the country and the significance of the product in the country's total exports of those types of goods. When the value of the index is greater than 1, it implies a measurable degree of comparative advantage in a product category; when it is less than 1, it suggests a comparative disadvantage."

APPENDIX C

COMPARISON OF FDI REGIMES AND INVESTMENT ARRANGEMENTS IN ECUADOR, CHILE, COLOMBIA, AND COSTA RICA

Table C-1. Comparison of FDI Regimes in Ecuador, Chile, Colombia, and Costa Rica

Category/Subcategory	Ecuador	Chile	Colombia	Costa Rica
Unified FDI Code	No	No	No	No
FDI Regime/Legal Bases				
Int'l Arrangements	Andean Pact Decision 291	N/A	Andean Pact Decision 291	N/A
Constitution	Articles 14, 18, 46	No	No	No
Statute/Decree	Decree 415 (1993) Ley de Mercado de Valores	Decree Law 600 (1974) (as am.)	Law 09 of 1991 (CONPES Res. 51 & 52/1991	No law specific to FDI
Collateral Law/Regulation	Companies Law/Sectoral Laws	Chaps XIV & XIX Central Bank Compendium	Resolutions of Monetary Board & Central Bank Tax Laws Specific to FDI: Decree 624/89 & Law 42/90	Investment incentive laws for tourism, exports, FTZs
FDI Lead Agency(cies)	MICIP	Foreign Investment Committee	CONPES, Nat'l Planning Dept.	None
Form of FDI Permitted				
New (Greenfield)	Yes	Yes	Yes	Yes
Acquisition of Existing Shares	Yes	Yes	Yes	Yes
Foreign-Owned	Yes	Yes	Yes	Yes
Domestic-Owned	Yes	Yes	Yes	Yes
Establishment of Branches	Yes	Yes	Yes	Yes
Sectors Closed to FDI	Defense, Nat'l Security Radio/TV	Defense, Nat'l Security Radio/TV	Defense, Nat'l Security (toxic hazardous waste disposal)	Beaches 50 Meters
Sectors Reserved to State	Water, mining, elec., telecom., (subject to concessions)	Apparently none	Sectors reserved by CONPES (curr. hazardous wastes)	Medical services, radio/TV, some banking, utilities, insurance, oil refining (subject to concessions)
Restrictions on FDI				
Ownership Limitations/General	None	None	None	None
Sectoral Restrictions	Water, mining, domestic air, transport, radio/TV, fisheries	Fisheries, petroleum, radio/TV, cabotage	Sectors reserved by CONPES (curr. waste disposal, mining, petroleum)	Radio/TV, utilities, banking, insurance, oil, pension funds, (subject to concessions)
Geographical	Reserved areas (for environmental, ethnic indians)			

Table C-1 (continued)

Category/Subcategory	Ecuador	Chile	Colombia	Costa Rica
Foreign Ownership of Real Property				
General	Allowed	Allowed	Allowed	Allowed
Restricted Sectors/Areas	Frontiers, beaches, "reserved areas"	Frontiers, beaches	?	Beaches 50 meters - concessions for next 150 meters
Lease/Concessions Permitted	Yes	Yes	?	Yes
FDI Approval Required?		Yes for FDI in excess of $5 mil., public utilities, media	No, generally utilities, nontoxic wastes, insured investments, oil/mining, must be approved by Nat'l Planning Dept.	
All FDI	No	All other no - but required for FDI guarantees/invariability		No (Except for incentives)
Discretion	N/A	Limited	Substantial	Tourism export incentives: moderate
Subject to Limits/Conditions	No	Under Law 600, capital must be invested within 3 years	Yes	Incentives contracts
Time of Approval Process	N/A	N/A	Approval in 45 days or assumed	N/A
Sectors/Areas Only	For incentives - yes		Banks - Superintendency of Banks	As above
Approving Agency	Incentive agencies only	Foreign Investment Committee	General: National Plan. Dept. Banks: superintendency of banks, mining/oil - Ministry of Mines & Energy - Inst. Funds - Superintendency of Securities	Tourism Board (tourism incents) CENPRO (export incentives)
Treatment of FDI	National	Nat'l except for dom. credit	Qualified national	National
Basis	Const. Art. 14, decree 415, art. 05 B.I.T. (USA)	Law 600, art. 09, 11	Const. art. 100, law 09- art. 15, CONPES res. 51/52, art. 03	Const art. 19
Problem Areas	Some bureaucracy discrimination	Access to domestic credit sources		
FDI Registration Requirements	Companies - Superint. of companies FDI, royalties: Central Bank	Negotion of inv. guaran. contract	FDI: Central Bank (within 3 mos.)	Generally registration not required, Tourism Bd (tourism incentives) CENPRO (export incentives) - Free Zones Bd. (FTZ incentives)
Discretion	None	Limited	Moderate	Moderate
Employment Restrictions	None except for oil/mining	Companies over 25 employees: 85% must be Chilean	80% specialists Colombian, 90% ordinary Colombian	?

Table C-1 (continued)

Category/Subcategory	Ecuador	Chile	Colombia	Costa Rica
Income Taxation/Basic Rate	25%	15%	30% + 25% surch. = 37.5% eff. rate	10-30%
Corporate	Same	Same	Same	Same
Branches	Same	15% base + 35% on distributions	Same	Same
Sectoral - Specific Tax Regime?	Mining, petroleum	FDI invariability option for combined 42% tax available	Oil, coal, nickel	
Distributions Taxed	Dividends - no	Dividends - 35%	Yes, corporations 12%, branches 5%-93; later 0	Dividends - 15%
Other Applicable Taxes				
Business Establishment/Incorporation	Yes	Yes	Yes	Yes
Capital Assets	0.15%			Property taxes
V.A.T.	10%	18% FDI exempt from VAT on certain capital goods imports	14%	10%
Export Taxes	Some	No	?	?
Customs Duties/Average	Up to 35% ad valorem	Av 11% ad valorem plus VAT customs duties may be deferred up to 7 years	Up to 35% ad valorem	10% ad valorem
Other	Excise, stamp, etc.	(Law 600 provides "unvariability" of customs duties until investment completed)	Stamp, legalizations	
Repatriation of Capital Abroad				
Taxed: Rate		Remissions in excess of original capital sub. to 35% tax		
Corporate	No	Same		No
Branches	No	Same		No
Restrictions	No	Must be through "formal" mkt.	No	No
Time Periods	N/A	One year after capital invested	None	N/A
Percentage of Registered Capital	N/A	No	No	No

Table C-1 (continued)

Category/Subcategory	Ecuador	Chile	Colombia	Costa Rica
Foreign Exchange Availability				
Guaranteed through Market	Yes	Yes under contract under Law 600 only from proceeds of sale of capital invested or shares	No	No
As Determined by Market	Yes	Yes	Yes	Yes
Remission of Profits Abroad				
Taxed/Rate				
Corporate	No	No	12%-93; 10%-94; 8%-95	No
Branches	No	No	Same	No
Restrictions	Generally no. Mining - 20% of profits	Must be through "formal" mkt & requires certificate from foreign investment committee	No	No
Time Periods	No	No	None	No
Percentage of Registered Capital	N/A	No	Up to 100% of capital registered	N/A
Foreign Exchange Availability				
Guaranteed through Government	No	Yes under FDI contract	No	No
Guaranteed through Mkt.	Yes	Yes through formal market	Yes	No
As Determined by Market	Yes	Yes formal market	Yes	Yes
Other Remittances Abroad	Must be registered with MICIP & with Central Bank	35% tax with 20% in certain cases	12% tax-'93; 10%-'94; 8%-'95	
Royalties: IPR/License etc.	Free market availability if previously registered	35% unless auth. by C.B., then 4% + must be registered with Central Bank	30% technical contracts must be registered with CB conditions & approval required in some cases	10% gross sales
Interest	Foreign loans must be registered with Central Bank		No	5-50% tax
Current Overhead/Acct. Payments	Same	No	No	Not taxed
Exchange Availability	Per free market	Per free market	Per free market	Per free market
Double Taxation Treaties	Brazil, Germany, Andean Pact	Argentina	Various in air transport sector Andean Pact	?

Table C-1 (continued)

Category/Subcategory	Ecuador	Chile	Colombia	Costa Rica
Debt/Equity Swap Availability?	Inactive public sector, nonprofits	Chap. 19, Central Bank compendium - yes	No	No
Preferential FDI Regimes/Incentives	No	Not permitted; Const. art. 02/2	Not permitted; Law 09 art. 15, res. 51/52, art. 03	No
FDI Incentives/Sectoral/Geographical	Agric., tourism, mining, fisheries, (Most incentives to be phased out in 1994)	Forestry, mining	Agroindustry, tourism, mining, oil	Tourism 50% income tax exemption
Fiscal		Reduced income tax, certain exemptions from VAT		Exports: 15% of export revenues credit against taxes
Exchange		Permits some offshore foreign exchange accts. for expenses cap. repatriation	Petroleum/mining exchange exemptions	Exemption from customs charges, capital assets & income taxes
Labor	No	No	?	?
Other	Sectoral incentives for agriculture, fisheries, tourism, mining due to expire 1994	Forestry, oil/atomic materials, some geographic -9% income tax	Financial sector, petroleum, mining	
Performance Requirements	No	No		No
Foreign Trade Zones	Yes - Free Trade Zones Decree Law No. 1 of 1991	Yes	Yes - Incomex res. 2386/92	Foreign Trade Zones Law
Incentives/General				
Fiscal	No	Income tax exempt	Exempt income, capital assets & remittance taxes	8 yr. tax holiday then 4 yrs - 50% exempt
Exchange	Exempt from most exchange restrictions		Exempt from most foreign exchange restrictions	
Labor	Flexible provisions			
Other	Exempted from customs duties and VAT taxes on raw material, machine, equipment	VAT, customs duties exemption	Exempt from customs duties and some VAT on imports	

Table C-1 (continued)

Category/Subcategory	Ecuador	Chile	Colombia	Costa Rica
Maquila Operations	Yes - temporary Importation Law (Law 90 of 1990)	Apparently no	Yes - Incomex res. 2386/92	Provided for in FTZ law
Incentives		N/A		
Fiscal	Exemption from or "drawback" on most customs duties	N/A	Subject to income other taxes, raw materials imports exempt from VAT	Drawback on customs duties
Exchange	Subject to for. exchange laws	N/A	Subject to for. exchange laws	
Labor	"Flexible" provisions	N/A		
Other		N/A	Subject to "drawback" on customs duties - subj. to ceiling limit with import deposits waived, import licenses waived	Requires no less than 35% Costa Rican value added
Expropriation				
Legal Authority	Const. Art. 47	Const. Art. 19	Const. Art. 58	Const. Art. 45
Prior Compensation Required?	No	Yes	Not under certain circumstances	
Subseq. Compensation Required?	Yes	N/A	Not under certain circumstances	
Procedure				
Judicial/Appeal from Adm.	Yes	Yes	Not under certain circumstances	Yes
Judicial/Set Compensation	Yes	Yes	Not under certain circumstances	
International Arbitration?	Available under applicable treaties	Yes	Not under certain circumstances	No
Unresolved/Pending Claims	No recent history of expropriation with one recent resolved intervention case	No	No recent but concerns over adm. exprop. authority without judicial recourse	Yes - 7 unresolved
FDI Dispute Resolution				
Local Judicial only	No	No	No	Yes
Arbitration: Local/Intl.	As agreed by parties	As agreed by parties	As agreed by parties	Local only
Int'l Agreements	ICSID, NY Conv., Panama Conv.	ICSID ratification pending, NY	NY Convention, Panama Conv.	NY Convention & Panama Con. ICSID signed not ratified CR does not utilize Int'l arbitration
Protection of Investment/Ins.	OPIC, Partial MIGA	OPIC, Partial MIGA	OPIC, MIGA ratification pending	OPIC

Table C-1 (continued)

Category/Subcategory	Ecuador	Chile	Colombia	Costa Rica
Bilateral Investment Treaties				
Signed	USA, Switzerland	Argentina, Belgium, France, Germany, Spain, Malaysia, Switzerland	None?	France, Germany, Switzerland, U.K.
In Negotiation	France, Italy, U.K.	Finland, Italy, Netherlands, U.K., Sweden, Venezuela	USA	USA
Intellectual Property Rights				
Patents - Problem Areas	New patent law considered good	15 yr. term, no "pipeline" provision	Compulsory license, no pharmaceuticals	Several problems, poor enforcement
Copyright - Problem Areas	Computer software not protected - lax enforcement	No major problems	No computer software protection, short terms, lax enforcement	No computer software protection, lax enforcement
Trademark - Problem Areas	Short term, unauthorized importation	None	Registration problems	Unauthorized importation, lax enforcement
IPR Conventions/Agreements	Berne, WIPO, UCC, Rome, Geneva	Paris, Berne, WIPO, UCC, Rome, Geneva	Berne, WIPO, UCC, Rome	Berne, WIPO, UCC, Rome

Table C-2. International Trade and Investment Arrangements

Category/Subcategory	Ecuador	Chile	Colombia	Costa Rica	Explanation
GATT	No	Yes	Yes	Yes	General Agreement on Tariffs and Trade
Andean Pact	Yes	No	Yes	No	Treaty of Cartagena
CACM	No	No	No	Yes	Central American Common Market
LAIA	Yes	Yes	Yes	No	Latin American Integration Association
OAS	Yes	Yes	Yes	Yes	Organization of American States
SELA	Yes	Yes	Yes	Yes	Latin American Economic System
Rio Group	Yes	Yes	Yes	No	Permanent mechanism for political consultation and collaboration
OLADE	Yes	Yes	Yes	Yes	Latin American Energy Association
PARLATINO	Yes	Yes	Yes	Yes	Latin American Parliament
Regional Bilateral Free Trade Agreements	None	Argentina, Mexico, Uruguay, Venezuela	Argentina, Bolivia, Venezuela	Mexico	Regional Bilateral Free Trade Agreements
EAI Framework Agreement	Yes	Yes	Yes	Yes	Consultation agreement with USA to implement EAI
BITS	USA, Switzerland	Argentina, Belgium, France, Germany, Spain, Malaysia, Switzerland	USA, others?	USA, others?	Bilateral investment treaties
OPIC Agreement	Yes	Yes	Yes	Yes	Consultation agreement with USA to implement EAI
Multilateral Investment Guaranty Agency (MIGA)/World Bank Arrangements					
Legal Protection	No	No	No	No	
Local Currency	Yes	Yes	No	No	
MIGA Guidelines Signatory	Yes	Yes	No	No	
Double Taxation Treaties	Andean Pact, Brazil, Germany	Argentina	Various for air trans-port operations (incl. USA)	?	Bilateral treaties for the avoidance of double taxation and tax enforcement cooperation

Table C-2 (continued)

Category/Subcategory	Ecuador	Chile	Colombia	Costa Rica	Explanation
International Dispute Resolution					
New York Convention	Yes	Ratification pending	Yes	Signed but does not apply	UN Convention on Recognition and Enforcement of Foreign Arbitral Awards
Panama Convention	Yes	Yes	Yes	Signed but does not apply	Inter-American Convention on International Commercial Arbitration
Washington Convention/ICSID	Yes	Ratification pending	No	Signed but does not apply	Convention on Settlement of Intl. Investment Disputes and International Center for Settlement of Investment Disputes
Intellectual Property Arrangements					
WIPO	Yes	Yes	Yes	Yes	World Intellectual Property organization
Berne Convention	Yes	Yes	Yes	Yes	Industrial Property (patents, trademarks, literary and artistic copyrights)
Paris Convention	No	Yes	No	No	Industrial Property (patents, trademarks, literary and artistic copyrights)
UCC	Yes	Yes	Yes	Yes	Universal Copywright Convention
Patent Cooperation Treaty					
Geneva	Yes	Yes	No	No	Geneva Convention on phonograms

Note: Chile left the Andean Pact in 1976.

APPENDIX D

STATEMENT OF WORK

1. Preliminary gathering of basic information relating to foreign direct investment climates and regimes.

2. Development of basic methodology of approach for assessing and comparing the relative appropriateness, attractiveness, and effectiveness of FDI climates and incentive programs responding to criteria and concerns of prospective foreign investors.

3. Preparation of individual country profiles describing aspects of their macroeconomic and business climates, resource endowments, industrial and sectoral circumstances, FDI statistics, etc.

4. Incorporation into the country profiles of a specific, in-depth analysis of existing investment incentives.

5. Investigation of contraindications for and disincentives for FDI.

6. Personal contacts with USAID staff, government officials, academics and private sector individuals to elicit their practical experience as to the FDI climates in the countries studied, the effectiveness of investment incentives, disincentives for FDI, workable incentives, and legislative/policy recommendations for improvement in the FDI investment climate.

APPENDIX E

PERSONS INTERVIEWED

Ecuador

1.	Luciano Almeida, Price Waterhouse	Quito
2.	Danny Alvarado, Price Waterhouse	Quito
3.	Mary Andrade, DeLoitte & Touche	Quito
4.	Pedro Aguayo, Fundación Ecuador	Guayaquil
5.	Eva de Arboleda, Guayaquil Chamber of Commerce	Guayaquil
6.	Eduardo Armendaris V. CENAPIA	Quito
7.	Basem Bader O., DeLoitte & Touche	Quito
8.	Francisco Borja P., Cyanamid	Quito
9.	Francisco Van Buchwald, Fundación Ecuador	Guayaquil
10.	Guy Burton, USIA/US Embassy	Quito
11.	Danilo Carrera Drovet, Banco de Guayaquil & Presidente Fundación Ecuador	Guayaquil
12.	Guillermo Chang Durango, Abogado & Ex-Ministro	Guayaquil
13.	Miguel A. Costales F., Borden S.A.	Quito
14.	Ernesto Davalos S., City Investing Company Ltd.	Quito
15.	Raul Daza, Banco del Progreso	Quito
16.	Alberto Dorfzaun H., INVESTBAN	Quito
17.	C. Eduardo Enmanuel, Pres. FEPROTUR	Quito
18.	Nicolas Febres-Cordero, ECUSAL	Guayaquil
19.	Fausto Idrobo, Subminister for Industry, MICIP	Quito
20.	Gary Flor Garcia, CENAPIA	Quito

21.	Roberto Illingworth C., Ex. Secty., Guayaquil Chamber of Commerce	Guayaquil
22.	Gustavo Jacome Paredes, Abogado	Quito
23.	Peter Lapera, USAID/Ecuador	Quito
24.	Pascual Loaiza, Banco Consolidado	Guayaquil
25.	José E. Mantilla, Banco Popular	Quito
26.	Richard H. Miller, CIBA Geigy Ecuatoriana	Quito
27.	Roque A. Miño, Ex. Dir. Amcham/Quito	Quito
28.	Guillermo Moreano G., MINDASA	Quito
29.	Pilar Moreno Hidalgo, Amcham/Quito	Quito
30.	Edgar Naranjo J., Ex. Dir, CETUR	Quito
31.	Edison Ortiz, CONSIDE, Ltda.	Quito
32.	Luis Palau-Rivas, Pres. Amcham/Quito	Quito
33.	Sebastian Paredes, Citibanc	Guayaquil
34.	Antonio Perrone, Dir. CETUR	Guayaquil
35.	Eduardo A. Proaño, Metropolitan Touring	Quito
36.	Luis A. Ricciardulli, Schering Plough	Quito
37.	Gustavo Romero Arteta, Romero, Arteta, Ponce	Quito
38.	W. Rafael Romero, Molinos del Ecuador	Guayaquil
39.	José Maria Rumazo Arcas, Perez Bustamante Y Perez	Quito
40.	Anthony Shiels, Fundación Ecuador	Quito
41.	Paul E. Simons, Econ. Attaché, U.S. Embassy	Quito
42.	José Maria Soto, Reckitt & Colman	Guayaquil
43.	Rolf Stern, Stern y Cia.	Quito

44. James Watson, USAID/Ecuador — Quito

45. Segundo Wong Mayorga, Pres. REYBANPAC — Guayaquil

46. Rafael Wong Naranjo, REYBANPAC — Guayaquil

Chile

1. Pedro Aylwin, Foreign Investment Committee

2. Ann Bacher, FCS/US Embassy

3. Juan Pablo Borquez Yunge, Investment & Financial Advisors for Latin America

4. James E. Callahan, Banco de Boston

5. James Dudley, Economic Attaché/US Embassy

6. Paul Ernst Kohling, Inter-American Development Bank

7. Miguel Fonseca Escobar, Banco Central

8. Juan Foxley Rioseco, Dir., Intl. Div., Banco Central

9. Juan Cristobal Foxley, Superintendencia de Valores y Seguros

10. Pedro Mattar Porcile, Superintendencia de Valores y Seguros

11. Thomas Nicastro, USAID/Chile

12. Rafael Pacheco J., Hoteles Kempinski/Lufthansa

13. Alfonso Peró C., Citicorp Chile

14. Hernan Pitto Dalmazzo, Attorney

15. Humberto Rivas O., SERNATUR

16. Barbara Urzúa, Amcham

17. Isabel Margarita Valenzuela, FCS/US Embassy

18. Eugenio Yunis, Dir. Gen'l., SERNATUR

Colombia

1. Consuelo Alarcón G., US DOC/ITA - US Embassy
2. Linda Archer, FCS/US Embassy
3. Joseph Finnin, Ex. Dir., Amcham
4. Yolanda Hané de González, US DOC/ITA - US Embassy
5. Gerardo Hernandez, Department of National Planning
6. Luz Angela Robledo, Coporación Nacional de Turismo
7. Patricia Rodriguez, Department of National Planning
8. Armando Vegalara Rojas, Ex. Dir., COINVERTIR
9. John Wall, USAID/Wash.
10. Armando Zamora, COINVERTUR

Costa Rica

1. José Ignacio Alfaro, Coordinator, LRE Project
2. Jorge Artavia, Director, Development Department CINDE
3. Sebastián Barceló, Barceló Hotels
4. Juan Carlos Chavarria, KMG-Peat Marwick (Amcham)
5. Carlos Echeverria, Exec. Director, PEDEPRICAP
6. Noylen Hidalgo, Exec. Director, Food Industries Chamber
7. John Holder, Advisor, Private Sector USAID/Costa Rica
8. Bernardo Kopper, Vice Minister, Foreign Trade
9. Gabriela Lobo, Exec. Director, CENPRO
10. Carlos Montenegro, Economic Advisor, Industries Chamber
11. Doris Osterloff, Exec. Director, Exporters Chamber
12. José Maria Quiros, Economic Advisor, U.S. Embassy
13. Roberto Quiros C., ASELEX< S.A. (Amcham)

14. Carlos Silva, Advisor, Minister of Tourism

15. Linda Solera, Asst. Director, Amcham

16. James R. Stanley, President, Fuertejidos (ex-Pres. Amcham)

17. Alvaro Valverde, Asst. Manager, Free Zones Corporation

18. Allison Wanamaker, Exec. Director, Amcham

19. Richard Whelden, Director, Private Sector USAID/Costa Rica

20. Carlos Wond, Director, Domestic promotion CINDE

21. Rodolfo Yglesias, Attorney (Amcham)

APPENDIX F

DOCUMENTS REVIEWED

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APPENDIX G

BIOGRAPHICAL INFORMATION ON THE AUTHORS

Biographical information on the consultants who prepared this report follows.

James L. Kenworthy, Team Leader, Director of the Latin American/Caribbean Trade and Investment Development Project, is a lawyer and consultant with more than 20 years' experience in international trade and investment, including legal practice in Colombia and the Dominican Republic. He has served as Assistant Director, Legal, of the National Foreign Trade Council and an attorney for the Foreign Claims Settlement Commission. During some 11 years as an attorney with the U.S. Department of Commerce, he served with the Office of Foreign Direct Investment, and later as Counsel to the Office of Foreign Investment in the United States. For 2 years he was an Adjunct Professor of International Trade Law at the University of Missouri/Kansas City School of Law.

Wesley D. Boles is Project Manager of the Latin American/Caribbean Trade and Investment Development Project and an experienced international business consultant with extensive experience in Latin America. His recent specialization has been as a consultant in international marketing and business development, and investment analysis and planning. Previously he was a senior staff executive at AFM Incorporated and a foreign service officer, including serving as U.S. Council in Monterrey, Mexico and Mexican Desk Officer in the State Department.

Joseph A. Whelan is an independent consultant specializing in international business and investment analysis and trade investment promotion. He has significant experience in Latin America and has served on a number of A.I.D. and World Bank market research studies. Previously he served in trade investment-related positions with the Overseas Private Investment Corporation, the U.S. Department of Commerce/International Trade Administration, and as a foreign service officer with the U.S. Department of State.