Through investment incentives, such as favorable tax policies and investment insurance, the Government has sought to encourage the flow of U.S. direct investment to developing countries. U.S. policy has been to encourage economic integration mechanisms, such as common markets, one of these being the Andean Common Market (ANCOM), whose principal objective is to develop the Andean area. Findings/Conclusions:

The foreign investment code adopted by ANCOM was intended as an investment incentive by providing a uniform set of rules within member countries, but its exception and escape clauses allow members to vary the rules as necessary. Chile, however, could not work within the structure and withdrew, which introduced uncertainties that the U.S. investor must consider. Trade and U.S. economic assistance ties remain strong between the United States and the Andean countries, but U.S. direct investment is diminishing, due to expropriation, divestment, and unfavorable reaction to Andean investment restrictions. Manufacturing and service types of investments predominate because of the possibility of natural resources investments being expropriated. Adequate data were not available for an in-depth assessment of tax preferences as inducements. U.S. firms continue to have an impact on Andean countries, but private capital diminished, causing a need for more borrowing. U.S. firms provide jobs at high wages, and do not, necessarily, purchase materials from U.S. sources. Technology transfer is hindered by safeguards and other impediments. The largest percentage of U.S. investment will probably continue to be in mining and high-technology manufacturing areas. Other foreign investors have received Andean acceptance because of their willingness to engage in
joint ventures and to provide more favorable financing.

Recommendations: There is a need to establish the relationship between U.S. direct investment abroad and the availability of strategic raw materials resources to the United States. This relationship should be studied, and the Administration and the Congress should be advised of procedures to develop cooperative efforts between the Government and U.S. firms in order to assure U.S. access to raw materials. (Author/SS)
U.S. Direct Investment In South America's Andean Common Market

Department of Commerce

Andean Common Market countries' foreign investment policies and controls are causing important changes in the U.S. direct investment position there. These changes, similar to those in other countries, could ultimately affect the U.S. economy.

GAO believes one of these changes, the decreasing U.S. investor presence in foreign raw materials sources, needs to be studied. The Department of Commerce, under authority of the International Investment Survey Act of 1976, agreed to study the relationship between U.S. direct investment abroad and the availability of raw materials to the United States.

GAO also believes this report can assist U.S. policymakers in determining other issues for inclusion in forthcoming studies under the act.

JUNE 7, 1977
To the President of the Senate and the Speaker of the House of Representatives

Because of congressional concern over the potential consequences of U.S. direct investment abroad, we studied the magnitude and impact of direct investment in South America's Andean Common Market. This report confirms the need for accurate and comprehensive information on direct investment abroad. It also highlights important changes in the U.S. direct investment position in the Andean Common Market countries and suggests studies which would assist the Congress in its deliberations on policies relative to energy and non-energy raw materials.

Our review was made pursuant to the Budget and Accounting Act, 1921 (31 U.S.C. 53), and the Accounting and Auditing Act of 1950 (31 U.S.C. 67).

We are sending copies of this report to the Director, Office of Management and Budget, and to the Secretaries of State and Commerce.

Comptroller General
of the United States
This is GAO's first report on U.S. direct investment abroad. The report evolved from domestic and foreign concerns about the impact of such investment on the U.S. and host countries' economies. It focuses on the Andean Common Market countries—Bolivia, Colombia, Ecuador, Peru, Venezuela, and, until October 1976, Chile—because they have sought to control foreign investment inflows and to meld investment into their development plans.

The common market's principal objective is to develop the Andean area through (1) a planned, systematic method of allocating industry, (2) elimination of intraregional tariff and nontariff barriers, (3) a uniform tariff on goods imported from outside the region, and (4) preferential treatment for Bolivia and Ecuador, the region's lesser developed countries. (See pp. 10 to 13.)

The foreign investment code adopted by the Andean Common Market provides for closing certain sectors of the countries' economies to foreign investors, requesting divestiture in some cases to host country interests, and limiting reinvestment and repatriation of profits. The code was intended as an investment incentive by providing a uniform set of investment rules within member countries, but its exceptions and escape clauses allow members to tailor foreign investment regulations to their own political and economic philosophies. (See p. 13 and apps. II to VII.)

For Chile, however, latitude in implementing the code was not enough. Chile's insistence that it could no longer subscribe to the restrictive foreign investment code and to the proposed high external tariff, which ran contrary to its domestic philosophy, culminated in its withdrawal. (See p. 14.)
This weakened the Andean Common Market and introduced additional uncertainties in Andean countries that the U.S. investor must consider, such as the market’s viability without Chile, Chile’s attractiveness now that it is no longer in the common market, and the future of investment restrictions within the market. (See p. 16.)

**U.S./ANDEAN ECONOMIC TIES**

Economic ties between the United States and Andean countries through trade and U.S.-supported economic assistance remain strong, but U.S. direct investment is diminishing.

Department of Commerce figures for four of the six countries show that U.S. direct investment dropped from $4.6 billion in 1965 to $4.2 billion in 1975. However, GAO figures obtained in the countries show recent nationalizations were followed by decreases of U.S. investment in all six countries to a total of $3.7 billion in early 1976.

These declines were due to such actions as expropriation and divestment. In addition, prospective investors have reacted unfavorably to Andean investment restrictions.

U.S. investors traditionally have been interested in Andean natural resources and this interest continues, but expropriations/nationalizations have made them leery of the future. As a consequence, manufacturing and service types of investment have gained a larger percentage of the U.S. investment dollar in these countries. (See pp. 20 to 23.)

Adequate data was not available for an indepth assessment of tax preferences as inducements to investments of U.S. capital. High Andean tax rates may be a disincentive, but are not indicative of actual tax liabilities which would be affected by special incentives or concessions that may be negotiated. (See p. 24 and app. VIII.)
INVESTMENT IMPACT

Although lack of statistical information has made it impossible to measure the impact of U.S. direct investment on the Andean countries and the United States, the following observations are based upon published sources and interviews in Andean countries.

-- U.S. firms, despite reductions in equity ownership, continue to have an impact on key sectors of Andean country economies by supplying technology, management expertise, and capital; providing marketing expertise and sales channels; and producing and supplying agricultural chemicals. Impact on the U.S. economy appears minimal although this could change.

-- Private capital needed to develop natural resources, establish manufacturing operations, and finance imports and exports historically has been provided by U.S. corporate sources. More recently, however, infusions of new capital from corporate sources has decreased, probably contributing to an increased need for funds through borrowing.

-- U.S. firms provide thousands of jobs at higher salaries within Andean countries, support local manufacturers, and provide some employment in the United States via purchases of U.S.-made goods.

-- U.S. firms do not necessarily purchase materials, parts, and equipment from U.S. sources. Cost, compatibility, and reliability of items strongly influence where the items will be purchased.

-- Some technology transfer occurs through U.S. investor presence in the countries, but safeguards and impediments hinder such transfer. (See pp. 28 to 32.)

FUTURE PROSPECTS FOR U.S. DIRECT INVESTMENT

Most U.S. investors have adopted a wait and see attitude as a result of the various uncertainties mentioned.
The largest percentage of U.S. investment probably will continue to be in mining and high-technology manufacturing areas. Andean countries are demanding more from foreign investors and some investors will be accommodating if their investments can be protected.

It appears that other foreign investors have received Andean acceptance because of their willingness to engage in joint ventures and their abilities to provide more favorable financing. Acceptance of investors, according to American businessmen, is determined by who can provide the "best deal." (See p. 33.)

CONCLUSIONS, RECOMMENDATIONS, AGENCY COMMENTS, AND MATTERS FOR CONSIDERATION BY THE CONGRESS

Andean Common Market economic development has provided little in the way of investment incentive. Moreover, the prospective incentive of a uniform foreign investment code has not materialized because countries have chosen to tailor foreign investment regulations to their own political and economic philosophies.

Chile's withdrawal because of differences over trade and investment restrictions lends additional uncertainties to an already uncertain investment climate.

Although Andean investment restrictions run contrary to U.S.-advocated free flows of capital between nations and hinder the attraction of private investment capital, the United States is committed to the principle that each country has the right to regulate investment within its own borders.

The U.S. policy of assisting developing countries, including Andean countries, through economic assistance and support of regional integration movements is sound. GAO offers no conclusions on U.S. support for direct investment in the Andean countries, however, because a lack of information precludes measuring the full costs and benefits. (See p. 36.)
The Andean Common Market situation reflects some of the current issues relative to all U.S. investment abroad. For example, the magnitude of U.S. investment in the raw materials sectors of Andean and other countries is decreasing at the same time that U.S. dependence on raw materials imports is increasing. (See p. 36.)

GAO believes there is a need to establish the relationship between U.S. direct investment abroad and the availability of strategic raw materials resources to the United States. GAO also believes that consideration should be given to the role and importance of U.S. investment abroad in establishing a definitive national raw materials policy. (See p. 37.)

GAO recommends that the Department of Commerce study the relationship between U.S. direct investment abroad and the availability of strategic raw materials resources to the United States. GAO also recommends that the Department consider advising the Administration and the Congress of procedures to develop cooperative efforts between the Government and U.S. firms in order to assure U.S. access to raw materials. Commerce officials have agreed with these recommendations. (See p. 37 and app. X.)

GAO believes the Department of Commerce's studies would assist the Congress in its deliberations on policies relative to energy and non-energy raw materials. GAO also believes its report provides a frame of reference for legislative and executive branch policymakers' use in determining other issues of prime importance for inclusion in forthcoming Federal studies of U.S. direct investment abroad. (See p. 38.)
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ABBREVIATIONS

ANCOM Andean Common Market
GAO General Accounting Office
LDC less developed country
OPIC Overseas Private Investment Corporation
WHTC Western Hemisphere Trade Corporation
CHAPTER 1

INTRODUCTION

Over the past several years considerable attention has been focused on foreign direct investment in the United States and U.S. direct investment abroad. This attention led to the realization that little reliable data exists on the magnitude and effects, both here and abroad, of these investments.

To provide some additional insights, and to assist the Congress with options for new policy directions should the need arise, we made a series of reviews of foreign direct investment in the United States. This study, which focuses on the Andean Common Market countries, is our first report on U.S. investment abroad.

U.S. POLICY TOWARD DIRECT INVESTMENT ABROAD

The United States advocates the free flow of investment capital between nations and follows a virtual "open door" policy toward incoming investment. It also wants to assist friendly developing countries to attract private investment, which it views as an important source of technology, management skills, and capital contributing to economic development.

Through investment incentives, such as favorable tax policies and investment insurance, the Government has sought to encourage the flow of U.S. direct investment to developing countries. U.S. policy has been to encourage economic integration mechanisms, such as common markets, that, according to the Secretary of State "strengthen the growth process of participating countries."

The U.S. Government recognizes each country's right to regulate investment within its own borders and to establish guidelines for the sector and nature of investments considered desirable. Where restrictions and restraints are applied, the Government asks that they be applied equitably to all investors.

1/Ownership of 10 percent or more of a foreign corporation's voting stocks or control of a foreign business organization by a citizen or corporation is considered direct investment.
SOURCE OF INFORMATION ON AND MAGNITUDE OF
U.S. DIRECT INVESTMENT ABROAD

The Bureau of Economic Analysis, Department of Commerce, functions as the domestic source of official information on the magnitude of U.S. direct investment abroad. Its authority for accumulating and publishing data on such investment is Executive Order 10033 of February 8, 1949, issued pursuant to Section 8 of the Bretton Woods Agreement Act. Under the act, the United States collects data on U.S. foreign investment in order to comply with official requests from the International Monetary Fund for balance-of-payments information.

According to Commerce, the book value of U.S. direct investment abroad at the end of 1975 was about $133.2 billion. Without adjusting for inflation, this represents approximately a 12-percent increase over the prior year—and an increase of almost 2,000 percent since 1940. As shown in table 1, a substantial portion of the increase has occurred in the developed countries of Europe. Total dollar value of U.S. investment in Europe has almost doubled in each 5-year period since 1950, with the largest increase, $25.3 billion to $49.6 billion, occurring during 1970-75.

DOMESTIC CONCERNS OVER INVESTMENT

The increasing amount of private investment capital going abroad and its effects on the U.S. economy have long been of interest to the Government and private sector. It wasn't until January 1968, however, that mandatory controls were instituted to curtail the movement of direct investment capital abroad by restricting U.S. parent financing of foreign affiliates. The controls were not intended to discourage direct investment per se, but reflected a desire to shift the financing of investment to foreign capital markets, thus alleviating U.S. balance-of-payments problems. Commerce's Office of Foreign Direct Investments was given responsibility for administering the controls.

Although the controls were removed in January 1974, Government and private sector concerns have persisted that the investors may be exporting jobs, capital, and technology to the detriment of the domestic economy. Conversely, others are concerned that the Government may try to impose new restrictions on investment outflows. They contend that the United States and host countries benefit from investment through increased employment, development of natural resources, and shared technologies.
TABLE I
GROWTH OF U.S. DIRECT INVESTMENT ABROAD BY AREA

<table>
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<tr>
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<tbody>
<tr>
<td>BILLIONS OF DOLLARS</td>
<td>($7.9 b.)</td>
<td>($8.6 b.)</td>
<td>($11.8 b.)</td>
<td>($19.3 L.)</td>
<td>($32.8 b.)</td>
<td>($49.3 b.)</td>
<td>($75.3 b.)</td>
<td>($133.2 b.)</td>
</tr>
<tr>
<td>C.</td>
<td>30%</td>
<td>30%</td>
<td>30%</td>
<td>34%</td>
<td>C.</td>
<td>C.</td>
<td>C.</td>
<td>C.</td>
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<tr>
<td>E.</td>
<td>20%</td>
<td>20%</td>
<td>20%</td>
<td>15%</td>
<td>E.</td>
<td>E.</td>
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</tr>
<tr>
<td>L.A.</td>
<td>40%</td>
<td>L.A.</td>
<td>41%</td>
<td>L.A.</td>
<td>35%</td>
<td>L.A.</td>
<td>17%</td>
<td>L.A.</td>
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<tr>
<td>O.A.</td>
<td>10%</td>
<td>O.A.</td>
<td>9%</td>
<td>O.A.</td>
<td>14%</td>
<td>O.A.</td>
<td>19%</td>
<td>O.A.</td>
</tr>
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</table>

Source: U.S. Department of Commerce
LACK OF CURRENT AND COMPLETE DATA

Existing Commerce statistics are generally recognized to be incomplete, outdated, and of limited value to policymakers. The Bureau of Economic Analysis made its last comprehensive study of direct investment abroad in 1966. The data has been updated partially through a voluntary survey of 500 firms (only 298 responded) in 1971 and by quarterly questionnaire samplings of selected firms in the United States. According to Commerce, questionnaires are currently received from 1,250 firms which have an estimated 18,000 foreign affiliates.

The need for more current and comprehensive data has been recognized over the past several years. In 1974, under the Foreign Investment Study Act (Public Law 93-479), the Departments of Commerce and the Treasury were authorized and directed to undertake comprehensive studies of foreign direct and portfolio investments in the United States. This was the first comprehensive study of foreign direct investment in the United States since 1959 and of portfolio investment since 1941. Results from the studies were reported to the Congress by Commerce on May 3, 1976, and by Treasury on August 4, 1976.

Also in 1974, Commerce submitted for approval to the National Advisory Council on International Monetary and Financial Policies a new and expanded data-gathering form on U.S. investment abroad. The form included a request for information which was not gathered in prior surveys but which Commerce believes necessary to measure the impact of such investment. The form was not approved because of the opinion that the information requested did not specifically relate to U.S. balance-of-payments transactions and could not be authorized under the Bretton Woods Agreements Act.

On September 28, 1976, the Congress approved new legislation (S. 2839) known as the International Investment Survey Act of 1976. It was signed by the President on October 11, 1976, becoming Public Law 94-472. The act provides the

1/Portfolio investment includes ownership of bonds, other U.S. corporate securities, and/or less than 10 percent of the voting stock or equivalent interest.

2/An interdepartmental council consisting of the Secretaries of the Treasury, State, and Commerce; the Chairman, Federal Reserve Board; and the President of the Export-Import Bank.
President with authority to "conduct such studies and surveys as may be necessary to prepare reports in a timely manner on specific aspects of international investment which may have significant implications for the economic welfare and national security of the United States." Among other things, it requires the President, through his designee(s), to conduct:

-- Comprehensive "benchmark surveys" of U.S. direct investment abroad and of foreign direct and portfolio investment in the United States at least every 5 years.

-- A comprehensive "benchmark survey" of U.S. portfolio investment abroad within 5 years of the legislation's enactment and to evaluate the feasibility and desirability of conducting, on a periodic basis, similar surveys.

-- A regular data-collection program to secure current information on international capital flows and other information related to international investment, including, but not limited to, information "necessary for computing and analyzing the United States balance of payments, the employment and taxes of United States parents and affiliates, and the international investment position of the United States."

On January 19, 1977, the President through Executive Order 11961 assigned responsibility under the act for conducting studies relating to direct investment to the Secretary of Commerce and for those relating to portfolio investment to the Secretary of the Treasury.

CHANGING ROLE OF U.S. INVESTMENT ABROAD

The geographical and sectoral distribution of U.S. investment abroad has changed drastically since statistics were first accumulated in 1929. World political and economic conditions have contributed heavily to these changes. Increasingly, however, changes are being caused by foreign governments' awareness and concern over foreign investment impact on their economies.

Distribution

Over the years, there has been a geographical shift in U.S. investment from less to more-developed parts of the world, attributable largely to the appeal of larger and more advanced markets, such as the European Economic Community. There has also been a shift from investment in the mining,
smelting, and service sectors to petroleum and manufacturing, as shown in the following table.

Table 2
Changes in Distribution of U.S. Direct Investment Abroad

<table>
<thead>
<tr>
<th>Amounts</th>
<th>Percent</th>
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<tbody>
<tr>
<td>(billions)</td>
<td>(billions)</td>
</tr>
</tbody>
</table>

Developed areas:
- Canada: $2.0 $3.6 $21.0 $31.2 | 26.7 30.5 27.8 23.4
- Europe: 1.3 1.7 25.3 49.6 | 17.3 14.4 33.5 37.2
- Other (note a): 0.3 0.4 5.5 10.4 | 4.0 3.4 7.3 7.8

Developing areas:
- Latin America: 2.5 4.9 13.0 22.2 | 46.7 41.5 17.2 16.7
- Other: 1.4 1.2 6.2 12.6 | 5.3 10.2 9.2 5.9

Unallocated: 3.9 6.1 19.2 34.8 | 52.0 51.7 25.4 26.2

Total: $7.5 $11.8 $75.5 | $133.2 100.0 100.0 100.0

Sectors:
- Mining and smelting: $1.2 $1.1 $5.4 $5.6 | 16.0 9.3 7.2 5.0
- Petroleum: 1.1 3.4 19.7 34.8 | 14.7 28.8 26.1 26.1
- Manufacturing: 1.8 3.8 31.0 56.0 | 24.0 32.2 41.1 42.0
- Other (note b): 3.4 3.5 19.4 35.8 | 45.3 29.7 25.6 26.9

Total: $7.5 $11.8 $75.5 | $133.2 100.0 100.0 100.0

a/Includes Australia, Japan, New Zealand, and South Africa.
b/Comprises primarily investment in public and private service sectors.

Source: U.S. Department of Commerce

Investment climate

About 50 percent of the total foreign direct investment throughout the world has been made by U.S. companies. It is understandable, therefore, that changes in investment climate would have a major impact on U.S. business enterprises. Recent significant trends in both developed and developing parts of the world show that host countries are:

--Prohibiting foreign investment in such key economic sectors as transportation, communications, banking, and insurance.

--Demanding more participation in managing and controlling foreign operations in their territories.

6
--Establishing mechanisms to screen and monitor foreign investment to ensure maximum benefits to their economies.

--Examining and adopting foreign investment policies promulgated by others.

THE ANDEAN COMMON MARKET: AN EXPERIMENT IN ECONOMIC DEVELOPMENT

The Andean Common Market (ANCOM), currently composed of five Latin American countries—Bolivia, Colombia, Ecuador, Peru, and Venezuela—was established May 26, 1969, to stimulate economic development. It is the only integration group in the world with a common foreign investment code embodied in its development strategy. Provisions within its code close certain sectors of the economies to foreign investors, require divestiture of in-place investments to host country interests, and limit reinvestment and repatriation of profits. The code was intended as an investment incentive by providing a uniform set of investment rules for member countries, but its exceptions and escape clauses have allowed member countries to tailor foreign investment regulations to their governments' political and economic philosophies.

Because of ANCOM's potential impact on U.S. foreign investment and the strong economic ties between its member countries and the United States, we selected this evolving common market as the subject of our first study of U.S. investment abroad.

U.S. policy toward ANCOM

The United States actively supports the ANCOM integration concept and its development objectives. Through the Andean Development Corporation, ANCOM's principal development organization, the United States has provided some $15 million in loan funds for relending to Andean private enterprises for projects designed to stimulate regional integration. The U.S. position on ANCOM, as expressed by the Secretary of State before the sixth General Assembly of the Organization of American States in June 1976, is that "we seek means to support the far-reaching integration plans that have been drawn up in the hemisphere—for the Andean group * * *.*

---

1/On October 30, 1976, Chile officially withdrew its membership in ANCOM, citing irreconcilable differences with ANCOM's foreign investment and tariff restrictions as its primary reason. (See p. 14.)
SCOPE OF REVIEW

We sought to develop information on the nature and magnitude of U.S. investment in ANCOM, identify some effects of the investment, and ascertain the present investment climate and its implications for future investment.

Although Chile withdrew from ANCOM on October 30, 1976, we included it in this review because (1) Chile's development philosophy is embedded in ANCOM and its integration mechanisms, (2) Chile was a member during most of our study and maintains close ties with the other member countries, (3) Chile's withdrawal exemplifies some of the issues and problems confronting ANCOM as a developing common market, and (4) our observations and conclusions apply equally to Chile and the member countries.

We did our preliminary work in Washington, D.C., and New York City, and in-depth work in the five ANCOM countries and Chile. Information was obtained from:


-- Government officials of four ANCOM countries and Chile and ANCOM officials.

-- Representatives of the Association of American Chambers of Commerce in Latin America.

-- Domestic and foreign representatives of U.S. financial institutions.

-- Representatives of U.S. firms operating in the six countries.

-- Foreign business and industrial representatives.

-- Representatives of the Overseas Private Investment Corporation, Inter-American Development Bank, and Business International Corporation, among others.
CHAPTER 2

THE ANDEAN COMMON MARKET

ANCOM is an outgrowth of the Latin American Free Trade Association, a union of 11 Latin American countries established in June 1961 to expand national markets through eliminating barriers to intraregional trade, establish a Latin American Common Market, and integrate the member country economies.

After several years, member countries realized that the Association was not achieving its objectives because of differences in economic development among members and the complex way in which tariff reductions had to be achieved.

Looking to improve their own economic positions, the Andean countries agreed to form a subregional economic bloc. With concurrence from the Association, ANCOM was established on May 26, 1969, with the signing of the Cartagena Agreement by Bolivia, Chile, Colombia, Ecuador, and Peru. Venezuela became the sixth and final member on January 1, 1974.

ORGANIZATION

The Cartagena Agreement established two principal organizations: the Commission and the Junta. The Commission, ANCOM's supreme body, consists of representatives from each member country. It functions as a forum for individual country representation. The Commission's primary responsibilities include the formulation of policies and the adoption of measures necessary for their implementation. Its formal actions are known as ANCOM Decisions.

The Junta is ANCOM's technical organization. It consists of three members, who may be nationals of any Latin American country, and a supporting staff. Located in Lima, Peru, it is ANCOM's headquarters and central planning mechanism. Its primary responsibilities are to carry out the Commission's instructions, formulate proposals for economic integration, and supervise the implementation of ANCOM Decisions. The Junta is committed to preserving and developing economic integration.

Andean Development Corporation

Although the Andean Development Corporation was established on February 7, 1968, prior to the Cartagena Agreement, it is an integral part of the Andean integration movement. Its primary function is to promote industrial projects.
through studies and financial assistance. Funding is provided by member countries and public and private foreign capital sources. As stated previously, the United States has provided the corporation with a $15 million loan.

OBJECTIVES AND MECHANISMS

ANCOM's stated objectives are to promote the development of its area, facilitate its countries' participation in the Latin American Common Market, and raise the standard of living of its people. To achieve these objectives, the Cartagena Agreement provides for joint planning of industry, internal trade liberalization, a common external tariff, and preferential treatment for Bolivia and Ecuador.

Joint planning of industry

Experience in the Latin American Free Trade Association demonstrated to ANCOM members that more developed countries benefit most from a free-market situation. Drawing upon this experience and the fact that economic development in the Andean countries differed considerably, the drafters of the Cartagena Agreement provided for "Sectoral Programs of Industrial Development," a planned systematic method of allocating industries among member countries to avoid duplication of production and unnecessary competition. Only selected industries are to be included as programs, and each program will cover one industry, with products within the industry assigned to member countries. Programs are designed to provide favorable tariff preferences and temporary monopolies or semi-monopolies over the manufacture of the products.

It was hoped that through industrial planning the ANCOM members would develop new specialized industries and improve existing ones, thus reducing the need for imports and increasing the amount of exports and employment to the benefit of overall regional development. These goals are not being realized, however, because (1) approval of sectoral programs has been slow, with only three programs having been approved to date, (2) limited capital within the region has prevented some countries from taking advantage of sectoral allocations, and (3) some countries have changed their development philosophies from encouraging industries that reduce imports to improving their traditional industries for better export possibilities.
Internal trade liberalization

ANCOM hopes to eliminate all tariff and nontariff barriers on products traded between member countries by 1993. These barriers have already been reduced or eliminated on some items, but the majority of products have been temporarily excluded from tariff reductions, including products in the Sectoral Programs of Industrial Development, country lists of excepted products, 1/ and/or ANCOM's list of agricultural products subject to escape-clause action. 2/

According to a recent study made for the U.S. Department of State, entitled "The Andean Integration Movement: An Appraisal":

"* * * only about 27 percent of ANCOM intraregional commerce is subject to the progressive liberalization. Most of these products are unprocessed foods and raw materials. Some fuels and ores are included, 'but no important items of general manufacture are in this trade.'"

Despite limitations, intra-Andean exports increased by more than 450 percent from 1969 to 1974. Although a substantial percentage of the increase is attributable to raw materials, primarily fuels, trade of some manufactured items has increased. For example, as illustrated by a U.S. consulting firm's recent study, 3/ Colombian exports to other Andean countries (including many industrial goods) increased from $44.3 million in 1969 to $202 million in 1974. Also, Ecuadorean exports to other Andean countries (primarily petroleum, but includes manufactured or processed products) increased from $11.5 million in 1969 to $172 million in 1974.

1/Each country is allowed a specific number of goods which it can exclude for a limited period of years from trade liberalization.

2/The escape-clause allows Andean countries to maintain high tariffs on imported agricultural products if imports threaten domestic interests.

Trade has increased—especially in monetary volume—among member countries. But continued restrictions on many agricultural products and manufactured items indicate ANCOM countries' reluctance to forego trade barriers for further increases in intraregional trade. Part of this reluctance can be attributed to the differing economic philosophies among member countries. The more developed countries are seeking to lower tariffs in order to promote trade of their exportable products, whereas the lesser developed seek means to protect domestic markets.

**Common external tariff**

The Cartagena Agreement provides for the establishment of a common external tariff to be applied uniformly throughout the Andean countries by December 31, 1988. Apparently the tariff's purpose was to protect local producers, stimulate efficiency in operations, and create an internal preference for Andean-produced goods.

As with other Andean integration mechanisms, exceptions to the rule are allowed. For example, products that are not produced in the region or are in short supply can be exempted.

Prior to the end of 1975, the Commission was to have approved a schedule leading to the attainment of the external tariff. This has since been changed to December 31, 1978, due to disagreement within the Commission over the rates that should be adopted.

**Preferential treatment for Bolivia and Ecuador**

Central to the Andean integration plan is a commitment to reduce the differences among member countries through an equitable distribution of the benefits of integration. Accordingly, Bolivia and Ecuador, as the two lesser developed countries in ANCOM, were granted special privileges under the Cartagena Agreement, as shown in table 3.
Bolivia and Ecuador are also accorded special consideration under ANCOM's Foreign Investment Code. (See app. I.)

Due to the limited success of industrial programing, trade liberalization, and attaining a common external tariff, it appears that ANCOM's integration mechanisms have had little impact thus far on the development of Bolivia and Ecuador.

**FOREIGN INVESTMENT CODE**

An integral part of ANCOM’s development strategy is its Decision 24, Foreign Investment Code, "Common Regime of Treatment of Foreign Capital and of Trademarks, Patents, Licenses, and Royalties." (See app. I for codified text of the Decision.) Adopted December 31, 1970, the Decision is structured to (1) protect the Andean market from foreign domination, (2) insure that member countries do not try to outbid one another for foreign capital and technology, and (3) insure that national rather than foreign firms benefit from regional integration.
The Code 1/ is a statement of minimal restrictions which national governments are to apply to foreign business, including:

--Registration of all direct foreign investments with a competent national authority (Article 5).

--Divestiture of majority ownership by all new and existing foreign enterprises that want to benefit from ANCOM trade (Articles 30 and 27).

--Limits on annual repatriation of profits to 14 percent of authorized direct foreign investment (Article 37).

--Limits on yearly reinvestments without government approval to 5 percent of capital (Article 13).

--Authority for member countries to reserve certain economic sectors to govern by different rules (Articles 38 to 43).

Although a principal objective of the Code is to bring about uniform treatment of foreign investment, member countries have been less than uniform in implementing Decision 24, as shown in Table 4. See appendixes II through VII for detailed summaries of each country's implementation of some of the Decision's more important provisions.

RATIONALE FOR AND IMPACT OF
CHILE'S WITHDRAWAL

Chile was an original signatory of the Cartagena Agreement and staunch supporter of, and contributor to, the ANCOM development philosophy. In recent years, however, Chile has experienced drastic changes in governments and developmental philosophies. Recent past Chilean governments pursued doctrines directed toward safeguarding domestic products and industries from foreign domination through imports and investments. The current government, faced with severe economic problems and limited foreign capital inflows,

1/Thé Foreign Investment Code was recently modified by Decision 103 which increased the percent of profits which may be remitted each year from 14 to 20 percent, permitted even higher remittances if approved by the host country, and raised the amount of automatic reinvestment allowed from 5 to 7 percent per year.
<table>
<thead>
<tr>
<th>Country</th>
<th>Registration</th>
<th>Divestiture</th>
<th>Profit remittance</th>
<th>Reinvestment</th>
<th>Reserved sectors</th>
<th>General implementation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bolivia</td>
<td>Central Bank of Bolivia</td>
<td>By those who want to participate in ANCOM</td>
<td>Uncertain</td>
<td>Uncertain</td>
<td>Left up to individual countries</td>
<td>Metal smelters, steel mills, and petrochemical complexes</td>
</tr>
<tr>
<td>Chile (note 2,3)</td>
<td>Foreign Investments Committee</td>
<td>Uncertain</td>
<td>Individually determined</td>
<td>Individually determined</td>
<td>Areas reserved by national law</td>
<td>Liberal</td>
</tr>
<tr>
<td>Colombia</td>
<td>Bank of the Republic</td>
<td>By those who want to participate in ANCOM</td>
<td>Limit of 14% of registered value</td>
<td>Maximum of 5% of registered value</td>
<td>Public service, finance, communications, marketing</td>
<td>Mildly conservative</td>
</tr>
<tr>
<td>Ecuador</td>
<td>Ministry of Industry, Commerce and Integration</td>
<td>Varies depending upon whether new or old investment</td>
<td>Limit of 14% of registered capital</td>
<td>Maximum of 5% of registered capital</td>
<td>Extractive, public service, finance, communications</td>
<td>Liberal</td>
</tr>
<tr>
<td>Peru</td>
<td>Government agency which regulates its sector</td>
<td>Through industrial community program</td>
<td>Limit of 14% of registered capital</td>
<td>Maximum of 5% of registered capital</td>
<td>Public service, communications, finance, natural resources</td>
<td>Very conservative</td>
</tr>
<tr>
<td>Venezuela</td>
<td>Ministry of Development</td>
<td>By those who want to participate in ANCOM or are in sensitive areas</td>
<td>Limit of 14% of registered capital</td>
<td>Maximum of 5% of registered capital</td>
<td>Extractive, public service, finance, communications</td>
<td>Very conservative</td>
</tr>
</tbody>
</table>

*Limitation provisions shown are general descriptions of each country's implementation of Decision 24 and are not intended to be all-inclusive. They do not consider the effects of Decision 103.

Provisions in effect prior to Chile's withdrawal from ANCOM.
chose a more moderate position concerning ANCOM's Foreign Investment Code and high external tariff. This caused open disagreement between Chile and the other Andean countries and culminated in Chile's withdrawal from ANCOM in October 1976.

Chile's withdrawal does not signal ANCOM's demise, but it does weaken the already floundering common market and eliminate its strongest proponent for a liberalized investment code. It also further complicates the Andean investment situation by introducing additional uncertainties that the U.S. investor must consider, including:

--ANCOM's viability without Chile: the withdrawal could diminish ANCOM's economic strength and investor attractiveness since it removes from the market Chile's developed manufacturing sector and consumer market. Conversely, it could enhance the attainment of a fully functioning five-nation common market now that the Chilean hindrance has been removed. 1/

--Chile's attractiveness without ANCOM membership: the withdrawal could further diminish manufacturing investor interest in Chile since investments could no longer benefit from lower internal tariffs nor sectoral allocation programs available within ANCOM. Conversely, it could enhance the Chilean investment climate by removing investor apprehensions about ANCOM investment restrictions. The withdrawal most likely will have little impact on extractive investments, however, since mining operations were exempt from ANCOM regulations and most of Chile's raw materials are exported outside of ANCOM countries.

--Future investment restrictions within ANCOM: foreign investment restrictions promulgated by ANCOM are less likely to undergo major reductions without Chile because remaining members are less adamant in seeking reductions. However, minor changes in the code's restrictions could be more readily forthcoming since Chile's opposition to minor reductions in lieu of the total elimination of some restrictions has been removed. ANCOM Decision 103 may exemplify this point.

1/ Chile had insisted that further implementation of ANCOM integration mechanisms be temporarily suspended pending modification of the Foreign Investment Code.
Adopted after Chile's withdrawal, Decision 103 among other things liberalizes the code by increasing the percent of profits which may be remitted and re-invested each year.
CHAPTER 3

U.S. INVESTMENT IN THE
ANDEAN COMMON MARKET

The United States and ANCOM countries have had a long history of strong economic ties through trade, private U.S. investment, and U.S. economic assistance. Although the United States is still a major trading partner with these countries and provides significant amounts of economic assistance, indications are that the private U.S. investment presence is diminishing.

TRADE

In 1975, the United States accounted for approximately 36 percent of ANCOM countries' exports and 39 percent of their imports. Major U.S. imports were petroleum, copper, iron, tin, coffee, bananas, and sugar; major U.S. exports were machinery, transportation equipment, cereals, flour, and chemicals.

Table 5 shows the substantial U.S. share of the ANCOM market trade between 1966-75.

Table 5

<table>
<thead>
<tr>
<th>Year</th>
<th>ANCOM imports from U.S.</th>
<th>ANCOM exports to U.S.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1966</td>
<td>39</td>
<td>41</td>
</tr>
<tr>
<td>1967</td>
<td>37</td>
<td>37</td>
</tr>
<tr>
<td>1968</td>
<td>39</td>
<td>36</td>
</tr>
<tr>
<td>1969</td>
<td>37</td>
<td>33</td>
</tr>
<tr>
<td>1970</td>
<td>39</td>
<td>33</td>
</tr>
<tr>
<td>1971</td>
<td>33</td>
<td>32</td>
</tr>
<tr>
<td>1972</td>
<td>34</td>
<td>34</td>
</tr>
<tr>
<td>1973</td>
<td>34</td>
<td>32</td>
</tr>
<tr>
<td>1974</td>
<td>34</td>
<td>36</td>
</tr>
<tr>
<td>1975</td>
<td>39</td>
<td>36</td>
</tr>
</tbody>
</table>

Sources: U.S. Department of Commerce Trade Statistics and International Monetary Fund Trade Statistics
ECONOMIC ASSISTANCE

From July 1, 1945, through June 30, 1975, the United States provided some $3.88 billion in bilateral economic assistance to ANCOM countries. Although economic assistance has increasingly come from multilateral sources, the United States, as a principal contributor to the multilateral organizations, continues to be an important source of development funds to the countries. Table 6 shows that U.S. bilateral economic assistance dropped from $322.5 million in 1966 to $175.5 million in 1975, but that multilateral assistance increased from $297 million to $383 million during the same period.

Table 6
Sources of Economic Assistance to ANCOM Countries

<table>
<thead>
<tr>
<th>Year</th>
<th>United States</th>
<th>Multilateral</th>
<th>Total amount</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Amount</td>
<td>Percent</td>
<td>Amount</td>
</tr>
<tr>
<td>1966</td>
<td>$322.5</td>
<td>52</td>
<td>$297.0</td>
</tr>
<tr>
<td>1967</td>
<td>204.1</td>
<td>45</td>
<td>254.2</td>
</tr>
<tr>
<td>1968</td>
<td>226.7</td>
<td>53</td>
<td>204.3</td>
</tr>
<tr>
<td>1969</td>
<td>212.3</td>
<td>37</td>
<td>362.0</td>
</tr>
<tr>
<td>1970</td>
<td>210.8</td>
<td>35</td>
<td>392.1</td>
</tr>
<tr>
<td>1971</td>
<td>158.4</td>
<td>25</td>
<td>482.4</td>
</tr>
<tr>
<td>1972</td>
<td>244.1</td>
<td>60</td>
<td>161.0</td>
</tr>
<tr>
<td>1973</td>
<td>155.6</td>
<td>27</td>
<td>416.7</td>
</tr>
<tr>
<td>1974</td>
<td>137.8</td>
<td>20</td>
<td>549.9</td>
</tr>
<tr>
<td>1975</td>
<td>175.5</td>
<td>31</td>
<td>383.0</td>
</tr>
</tbody>
</table>

Source: U.S. Agency for International Development.

DIRECT INVESTMENT

Accurate, complete, and current statistical information on U.S. investment in ANCOM countries is not available in the United States nor in host countries. Mechanisms established by ANCOM countries to register and monitor foreign investment are not fully operational in all countries, and the types and amounts of data being accumulated in the countries are not uniform.
Commerce has not made a comprehensive study of U.S. direct investment abroad since 1966. and current data is recognized as incomplete, outdated, and of limited value. Nevertheless, by using information that was available in the United States and the Andean countries, we developed a profile of U.S. foreign direct investment in ANCOM countries, as discussed in the following sections.

Magnitude

U.S. private investors have been interested in the Andean countries since the late 1800s. Most often, these interests were directed to the extractive or public service sectors which are key sectors in the countries' economies. Changes have occurred in the sectoral distribution of U.S. investment, but at the time of our review in early 1976, U.S. investors held $3.7 billion or over 70 percent of the $5.2 billion in total foreign investment in ANCOM countries.

According to Commerce, the book value of U.S. direct investment in four ANCOM countries declined from $4.6 billion in 1965 to $3.6 billion in 1974 before surging to $4.2 billion in 1975. It should be noted, however, that the 1975 Commerce figure does not reflect the January 1976 nationalization of U.S. oil interests in Venezuela, valued by Commerce at $861 million. Table 7 shows the total book values from 1965 to 1975.
Table 7

U.S. Direct Investment in Chile, Colombia, Peru, and Venezuela (note a)

<table>
<thead>
<tr>
<th>Year</th>
<th>Value (millions)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1965</td>
<td>$4,575</td>
</tr>
<tr>
<td>1966</td>
<td>4,011</td>
</tr>
<tr>
<td>1967</td>
<td>4,095</td>
</tr>
<tr>
<td>1968</td>
<td>4,343</td>
</tr>
<tr>
<td>1969</td>
<td>4,358</td>
</tr>
<tr>
<td>1970</td>
<td>4,327</td>
</tr>
<tr>
<td>1971</td>
<td>4,317</td>
</tr>
<tr>
<td>1972</td>
<td>4,218</td>
</tr>
<tr>
<td>1973</td>
<td>4,161</td>
</tr>
<tr>
<td>1974</td>
<td>3,608</td>
</tr>
<tr>
<td>1975</td>
<td>4,224</td>
</tr>
</tbody>
</table>

a/Commerce does not publish separate investment totals for Bolivia and Ecuador.

Source: U.S. Department of Commerce

During our incountry review, we obtained estimated investment figures for each ANCOM country. Although we could not verify accuracy, the figures appear to parallel information published on U.S. investment concentrations and to reflect recent divestitures and nationalizations. Table 8 presents a sectoral breakdown of investment by country.
Table 8

U.S. Investment by Sector

<table>
<thead>
<tr>
<th>Sector</th>
<th>Bolivia</th>
<th>Chile</th>
<th>Colombia</th>
<th>Ecuador</th>
<th>Peru</th>
<th>Venezuela</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mining and</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>smelting</td>
<td>$14</td>
<td>$15</td>
<td>-</td>
<td>-</td>
<td>$1,050</td>
<td>-</td>
</tr>
<tr>
<td>Petroleum</td>
<td>30</td>
<td>11</td>
<td>-</td>
<td>$334</td>
<td>140</td>
<td>-</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>-</td>
<td>103</td>
<td>(a)</td>
<td>66</td>
<td>(b)</td>
<td>$581</td>
</tr>
<tr>
<td>Other (note c)</td>
<td>5</td>
<td>21</td>
<td>-</td>
<td>-</td>
<td>110</td>
<td>485</td>
</tr>
<tr>
<td>Total</td>
<td>$49</td>
<td>$150</td>
<td>$745</td>
<td>$400</td>
<td>$1,300</td>
<td>$1,066</td>
</tr>
</tbody>
</table>

a/Breakdown by sector not available.
b/Estimate for manufacturing included in "other" category.
c/Includes commerce, services, financial institutions, etc.


Investment levels have declined due to expropriation, divestment, and other host country actions which exhibit strong nationalism and a general mistrust of foreign investors. The following examples help to illustrate this point.

--Copper accounts for 75 to 80 percent of Chile's foreign exchange earnings through exports. Until recent years, a few U.S. companies held the predominant share of Chile's total copper production and U.S. investment in the country. This presence greatly diminished, however, when U.S. copper producers were forced to divest part of their holdings in the mid-1960s and later had their remaining properties expropriated.

--U.S. investment in Peru has been primarily in the mining sector, Peru's major source of export earnings. Over the last few years, however, the U.S. investment position has changed substantially as a result of Peruvian expropriation of U.S. mining interests in copper and iron ore.
Oil accounts for about 97 percent of Venezuela's foreign exchange earnings, 66 percent of its government revenues, and 30 percent of its gross national product. Until the industry was nationalized on January 1, 1976, foreign firms, primarily U.S. corporations, owned and operated most of the oil-producing facilities in the country.

Because of the 1973 downturn in the world economy and such other factors as Andean government instabilities, the extent to which ANCOM investment restrictions have contributed to the decline in investments since 1969 cannot be accurately measured. However, as noted on page 32, they have had an unfavorable impact on investor attitudes.

Geographic distribution

Investments within the region and within each country appear to be distributed based upon two primary criteria (1) the presence of an exploitable natural resource and (2) the availability of an internal consumer market. Colombia, Venezuela, and, to a lesser extent, Chile, the three more developed Andean countries, have been able to attract U.S. investment in the manufacturing, trade, finance, and petroleum sectors. The other three Andean countries, with lesser developed internal markets, have traditionally attracted the majority of U.S. investment to the extractive sectors.

Likewise, the countries' most industrialized and populous cities have been the sites of most U.S. manufacturing, trade, and finance investments, whereas the extractive operations are dispersed to wherever mineral and oil deposits can be found.

Reasons for investing

It is fairly obvious that investors in the mining sector must invest where exploitable resources can be found. But why would manufacturers want to invest in ANCOM countries which have limited markets, uncertain political and economic conditions, and other deterrents? American manufacturers in the Andean countries gave the following reasons:

--A chemical manufacturer could have continued to export to the host country but market potential is greater by having a plant there.
--A pharmaceutical manufacturer's plant was established because the company would not have been able to compete with local producers due to high tariff rates on imported finished goods.

--A motor vehicle assembler wanted to develop expertise on local needs to be in a better position to know about and bid on special projects. High tariff rates on imported finished goods and cheap labor were also inducements.

--A chemical manufacturer estimated plant construction costs would be about 65 percent less if constructed in the Andean country rather than in the United States. High cost of labor and pollution control requirements in the United States were cited as primarily contributing to the cost difference.

--Several companies mentioned market and profit potentials.

Department of State officials cited the possibility of producing for export as another reason for investment in ANCOM countries. This is already true for extractive industries and, according to the officials, it could become increasingly so for manufacturing investments.

The need to avoid discriminatory high tariff rates on imported finished goods was most often mentioned by U.S. manufacturing investors as the reason for establishing operations in the country in lieu of servicing through U.S. exports. Protective high tariff rates, according to informed sources, have historically been common throughout Latin America and indications are that they will continue as part of these countries' developmental philosophies. ANCOM's protective tariff on goods imported from without the Andean areas exemplifies the retention of this protectionist philosophy.

**Tax incentives**

While the preceding factors are no doubt some of the overriding considerations in any investment decision, the tax policies of both the United States and the host countries also tend to encourage expansion of investment. In the absence of actual tax statistics, only limited observations can be drawn on how such policies may act as inducements to furthering U.S. investment abroad. A few fundamental tax principles can be used to illustrate the impact on investment decisions.
In general, the United States taxes the overseas net earnings of subsidiaries of U.S. parent corporations at a rate of 48 percent. However, this tax is not levied until earnings are repatriated as dividends to the U.S. parent. Taxes paid to the foreign government can be used to reduce, within certain limitations, the U.S. tax liability on these repatriations. The amount of such reduction cannot exceed the U.S. tax liability on aggregate foreign earnings. Generally, U.S. parent companies have an incentive to retain earnings in a controlled subsidiary as long as the foreign tax liability is significantly less than the U.S. tax liability on such earnings. For example, if $1 million in earnings of a U.S.-controlled subsidiary were taxed by an Andean government at 30 percent in 1976, and $500,000 was returned to the parent, the parent would owe another $90,000 in U.S. taxes.

U.S. tentative tax prior to credit $240,000 (48% x $500,000)
Tax credit 150,000 (30% x $500,000)
Final U.S. tax liability on repatriated earnings $ 90,000

However, if another subsidiary of the same U.S. corporation was subject to a foreign tax rate of 50 percent, a $10,000 excess foreign tax credit would be generated. This excess credit may be used to offset part of the tax otherwise due on the dividends from the subsidiary in the first example. Such excess credit may also be carried back or forward.

U.S. tentative tax prior to credit $240,000 (48% x $500,000)
Tax credit 250,000 (50% x $500,000)
Maximum allowable credit in current year $240,000
"Excess" tax credit $ 10,000

Obviously, there is an incentive to leave the money abroad if the overall foreign tax rate is lower than the U.S. tax rate. However, the relevant foreign tax rate is the combined tax on profits plus any withholding tax on distributed profits.

---

1/When current year foreign taxes are greater than the U.S. tax liability on such earnings, the U.S. parent is allowed to offset the excess against the U.S. tax on foreign income for the 2 preceding years and for 5 succeeding years.
Andean country statutory income tax rates on corporate earnings retained in-country and additional withholding tax rates imposed on repatriated dividends are shown in table 9. In most cases the combined tax rate will exceed the U.S. 48 percent corporate rate if all after-tax profits are distributed as dividends to the U.S. parent corporation.

<table>
<thead>
<tr>
<th>Country</th>
<th>Percent of tax on</th>
<th>Percent of additional withholding tax on</th>
<th>Percent of combined tax on repatriated dividends</th>
<th>100 percent distribution</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>earnings retained</td>
<td>corporate tax on retained dividends</td>
<td>(note a)</td>
<td></td>
</tr>
<tr>
<td>Bolivia</td>
<td>30</td>
<td>30</td>
<td>51</td>
<td></td>
</tr>
<tr>
<td>Chile</td>
<td>b/15 and 40</td>
<td>42</td>
<td>52.44 to 70.42</td>
<td></td>
</tr>
<tr>
<td>Colombia</td>
<td>40</td>
<td>32</td>
<td>59.2</td>
<td></td>
</tr>
<tr>
<td>Ecuador</td>
<td>30</td>
<td>44.4</td>
<td>61.08</td>
<td></td>
</tr>
<tr>
<td>Peru</td>
<td>20 to 55</td>
<td>40</td>
<td>52 to 73</td>
<td></td>
</tr>
<tr>
<td>Venezuela</td>
<td>c/15 to 50</td>
<td>d/15 or 30</td>
<td>27.75 to 65</td>
<td></td>
</tr>
</tbody>
</table>

a/ There are also special penalty tax rates for interest, royalty, and capital gains payments. (See p. 117.)

b/ Second rate listed represents a surtax on profits remaining after the initial tax deduction.

c/ Does not apply to earnings from oil and mining ventures.

d/ Rate varies according to type of share. Nominative shares are taxed at 15 percent rate and bearer shares are taxed at 30 percent rate.

The effect of U.S. and Andean country tax policies is to encourage new investment or expansion through the retention of foreign source earnings abroad. However, the above rates are statutory and are not necessarily indicative of actual tax liability, which may be affected by tax incentives or special concessions negotiated with the host government. For example, the host country may allow certain preferred noncompetitive industries a 5 to 10 year tax holiday or tax waiver for investment in certain underdeveloped economic or geographic sectors. Unfortunately, adequate data is not available to permit an indepth assessment of the effect of tax preferences on the flow of U.S. capital to ANCOM.
countries, but some form of tax-holiday provision is common. (See app. VIII for additional data and comments concerning taxes.)

**Overseas Private Investment Corporation program incentives**

The stated purpose of the Overseas Private Investment Corporation (OPIC), a U.S. Government corporation created by the Foreign Assistance Act of 1969 (Public Law 91-175), is to:

"**mobilize and facilitate the participation of United States private capital and skills in the economic and social progress of less developed friendly countries and areas, thereby complementing the development assistance objectives of the United States**"

OPIC's three primary activities—financial assistance, insurance, and investment informational services—act as incentives to encourage U.S. direct investment in developing countries. The financial assistance program provides direct loans and loan guarantees to U.S. investors. The insurance program provides insurance against loss from political risks of currency inconvertibility, expropriation, and war.

Although OPIC programs are specifically geared for developing countries, such as ANCOM members, the insurance program, its principal investment incentive, has for the most part been inoperable over the last few years within ANCOM countries. Subrogation rights to disputed property, a prime requisite for the issuance of an insurance policy by OPIC, has been interpreted by some Andean governments as not permitted under ANCOM's Decision 24, article 51. However, OPIC continues to maintain sizeable insurance coverage in the Andean countries, due primarily to policies issued prior to ANCOM's establishment. As of August 31, 1976, the total amount of insurance under the three primary areas of coverage was as follows.

---

1/Contractual arrangements between OPIC and the insured, whereby OPIC assumes the legal rights of the insured in property disputes with host countries.
Insurance coverage by country is included in appendixes II through VII.

Political and nationalistic actions resulting in the expropriation/nationalization of U.S. investment in the Andean countries has, over the last few years, made OPIC insurance a valuable asset to U.S. investors. Several U.S. businessmen, primarily interested in the extractive sectors, indicated during our country interviews that the availability of OPIC insurance would be a very positive factor in attracting U.S. private capital to ANCOM countries. Some ANCOM country government officials also recognized the importance of OPIC insurance in attracting U.S. private investment capital to their countries.

Impact of U.S. investments

Without key statistical information, it is impossible to measure the impact of U.S. investment on labor, capital, and other areas of vital importance to both the United States and ANCOM countries. However, certain observations can be drawn from published sources and interviews with U.S. businessmen and foreign government and business representatives.

Economic

The extractive and agricultural sectors dominate the Andean economies by providing substantial employment and contributing much of their foreign exchange earnings. U.S. private financial institutions are heavily involved in these sectors. U.S. firms are increasingly being removed from direct agricultural and extractive equity investments, but continue to have an impact on these sectors by (1) supplying technology, management expertise, and exploratory and developmental capital for mining and petroleum operations, (2) providing marketing expertise and conduits for mineral, petroleum, and agricultural products, and (3) producing and supplying chemicals used in agricultural production.

The impact of U.S. direct investment in Andean countries on the U.S. economy appears minimal. The investments, according to 1975 Commerce data, represented approximately
3 percent of total U.S. direct investment abroad ($4.2 billion of $133.2 billion). Although an increasing percentage of the investment is represented by manufacturing operations, indications are that the manufactured products, for the most part, are not presently exported to the United States. However, this could change as these operations become more efficient and their products more competitive in the world markets.

**Capital**

The Andean countries, with the possible recent exception of Venezuela, historically have had an investment capital shortage. Over the years, U.S. companies have provided significant amounts of private capital needed to develop natural resources, establish manufacturing operations, and finance imports and exports. Much of this capital came from the United States through corporate and private financial institution financing. Recently, however, new infusions of capital by corporate sources has decreased, thus reducing demands on the U.S. capital market. This, together with the reduction of U.S. investment through expropriations and divestments, has resulted in an overall decrease in the U.S. investment presence in the countries.

Concurrent with the decrease in U.S. direct investment has been a rapid growth in the external debt of some of these countries. For example, the combined external debt for Chile, Colombia, and Peru grew from $5.6 billion in 1970 to $9.6 billion in 1975. Although the decrease in U.S. private equity capital has probably contributed to the need for borrowed funds, a direct causal relationship cannot be established at this time.

**Employment**

U.S. firms provide thousands of jobs at all levels in these high-unemployment countries. We contacted 43 firms in six countries which directly employed about 32,000 persons, approximately 99 percent of them non-U.S. citizens. Some of these firms had no U.S. employees. We were told that U.S. firms also:

--Indirectly support local manufacturers through purchasing locally produced parts and products. Some U.S. manufacturers indicated that parts and products are purchased locally because (1) they can be produced cheaper and a locally available supply is assured, (2) government-imposed local content requirements
dictate that some components be produced locally, and/or (3) if divestiture to majority local ownership is enforced, shares in the U.S. company can be sold to suppliers who have a vested interest in the company.

A U.S. retailer stated that his company had established local manufacturing plants to supply his establishments with locally produced items. The plants had since been sold to local entrepreneurs because the retailer had no continuing interest in maintaining manufacturing operations.

--Usually pay their employees more than do local businesses. U.S. businessmen indicated that the higher salary was commensurate with the higher caliber of people they wanted to employ. Also, U.S. firms are primarily in the extractive, extractive-related, and high-technology manufacturing areas which normally command higher salary levels.

--Provide employment in the United States through their purchases of goods and equipment. Goods and equipment used in manufacturing and extractive operations are, for the most part, imported because they are not available within the local economy. However, as discussed below, only a portion of such requirements are imported from the United States.

**Market for U.S. goods and equipment**

Do U.S. firms in ANCOM countries buy materials, parts, and equipment from U.S. sources? We received mixed responses from American business representatives in answer to that question.

Several manufacturers told us that they purchased a large percentage of parts from the United States but that it was becoming more difficult as ANCOM countries imposed higher local-content requirements. One firm preferred the reliability of U.S. equipment and estimated that 60 to 70 percent of its operations equipment came from the United States. Another acquired materials mostly from the host country and made other purchases from the cheapest available source. Still another firm estimated that half of its plant equipment came from the United States and that its materials for the previous year came from (1) subsidiaries in the United States ($500,000), (2) other U.S. suppliers ($75,000 to $80,000), (3) non-U.S. subsidiaries ($200,000 to $250,000), and (4) non-U.S. companies ($200,000 to $250,000).
Other firms' purchases were made as follows:

-- All materials and equipment purchased from the United States.

-- Finished products assembled from "kits" made in the United States.

-- Most equipment and parts purchased from the company's subsidiaries in other Latin American countries because transportation and equipment costs were lower and the facilities produced similar items not produced in the United States.

-- Materials purchased from the United States and Europe and equipment purchased from Europe because U.S. equipment was considered overpriced.

**Technical and management know-how**

U.S. investment is concentrated in the high-technology areas of manufacturing and in the exploration and exploitation of mineral resources. The countries, we were told, benefit from the technology through better products and new and more efficient mineral extractive operations. Although some technology is transferred as a result of having manufacturing operations in the country, we found U.S. investors had taken measures to safeguard their technology by entering into licensing agreements and management contracts and by restricting the transfer of special formulas abroad. Moreover, as pointed out by Department of State officials, the flow of U.S. technology is impeded by (1) assembly as opposed to manufacturing operations, (2) importation of sophisticated components rather than local manufacture, and (3) informal agreements between members in joint ventures that limit the development of in-country technology. According to the State officials, the latter method of limiting technology flows can result in less-developed countries being left with obsolete technology and dependent on infusions of new technology from abroad.

Business management is recognized as an American forte. Some of the individuals contacted consider the transfer of U.S. management know-how to be one of the more significant U.S. contributions to ANCOM countries. Several U.S. companies had training programs in the United States for key host-country employees who had high advancement potential.
In addition to management know-how, U.S. firms also contributed to the development of a work force through on-the-job education and specialized technical training of employees.

FUTURE FOR DIRECT INVESTMENT

For the most part, U.S. investors throughout the ANCOM countries have taken a wait-and-see attitude. Government regulations have had some effect on investors, but uncertainty over future investment restrictions, economic conditions in the countries, and/or political interventions are the greatest deterrents to future investment.

Governments are interested in investments that benefit their economies. These vary from country to country depending upon economic status and development goals. Most of the governments, however, appear to be interested in obtaining maximum capital and technology with as little foreign equity as possible.

Concentration

The percentage and form of U.S. investor participation is changing. The largest percentage of U.S. investment will most likely continue to be in the extractive sectors and high-technology manufacturing areas. Raw materials and related industries continue to be the mainstay in most of these countries' economies and the areas of prime investor interest. 1/

ANCOM countries are requiring greater host-country equity participation in extractive operations. This is true of many new mining ventures being considered in the region. Countries trying to develop their petroleum sector do not allow equity participation by foreign investors and require guaranteed minimum investments for set percentages of the oil, if discovered.

Most countries are interested in attracting new manufacturing technologies not available domestically. Venezuela is willing to buy this technology; most others would

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1/Continued interest may be partially due to the fact that member countries have, for the most part, exempted extractive sectors from ANCOM's Foreign Investment Code restrictions.
rather attract foreign capital in conjunction with the technology. All, however, prefer local equity participation in the firms.

U.S. investors have been, and to a certain extent continue to be reluctant to participate in joint efforts with host-country governments or private individuals for fear of proliferation of their technologies and dilution of their management controls. Some U.S. companies throughout ANCOM have begun to see the potential benefits of such business unions, however, and have adopted a softer line on local equity participation. But they have demanded strong management and technology contracts to protect their investments. As one U.S. investor said: "We would go in with zero equity if we thought we could make money and protect our interest."

U.S. share of total foreign investment

Although U.S. companies account for more than 70 percent of total foreign investment in ANCOM countries, they appear to be encountering strong competition from Canadian, Japanese, and European investors in the manufacturing and extractive sectors. Other foreign investors seem to be receiving increased acceptance in some ANCOM countries because they are more receptive to joint ventures with local firms or host governments and are better able to provide more favorable financing for import-export trade. Financing, we were told, is often subsidized by the foreign investors' home governments.

Our review of ANCOM's Foreign Investment Code and its implementation by member countries revealed no favorable or unfavorable provisions directed toward any foreign countries' investors. Also, American businessmen knew of no foreign investment provisions implemented by the six countries aimed against U.S. investors or in favor of investors of other countries. As far as the U.S. businessmen were concerned, the countries were out to get the "best deal" from whatever source possible.

Moreover, we were told that past expropriations and similar actions were directed primarily at U.S. business interests simply because the United States had the most foreign investors in the region. Facilities owned by investors of other foreign countries have also been subject to similar expropriation/nationalization actions.
Reliable statistics are not available from either U.S. 
or host government sources on the extent of U.S. investment 
in ANCOM countries. The Department of Commerce has made no 
comprehensive study of U.S. direct investment abroad since 
1966, and many host governments have not completed the reg-
istration of foreign investment as provided in Decision 24 
of the ANCOM agreement.

Available statistics indicate that the value of U.S. 
investment in four of the six countries dropped from 
$4.4 billion in 1969 when ANCOM was established to about 
$3.7 billion at the time of our review in early 1976. To 
what extent is this decline is attributable solely to ANCOM 
investment restrictions is not determinable due to many 
variables, including governmental instability and the down-
turn in the world economy since 1973.

It is clear, however, that changes have occurred in the 
U.S. investment presence over the last decade and further 
changes are indicated as host-country governments demand 
greater control over and participation in foreign business 
enterprises in their countries. For example, the number of 
U.S. investments in the extractive sectors has decreased due 
to host country nationalization/expropriation actions. Cor-
sequently, a much larger percentage of U.S. investments is 
presently concentrated in the manufacturing and services 
sectors.

U.S. businessmen, leery of past controls and fearful of 
future restrictions, have adopted a wait and see attitude, 
except in those instances where their expertise or capital 
has warranted "special consideration" by Andean country gov-
ernments. Despite the changes and apprehensions, U.S. enter-
prises continue to have the largest amount of investment in 
the region. In other words, there is room for U.S. firms to 
negotiate, case by case, the terms for priority investment 
that Andean countries are seeking to attract.

ANCOM is encountering a number of problems with mecha-
nisms adopted to meet the region's development objectives. 
Investment incentives through industrial allocations, internal
import reductions, and import protection have not materialized. Moreover, a uniform foreign investment code has not been realized, because member countries have chosen to tailor foreign investment regulations to their governments' political and economic philosophies.

Chile's recent withdrawal from ANCOM because of irreconcilable differences with the organization's restrictive foreign trade and investment policies exemplifies the dilemma facing ANCOM, its member countries, and other developing countries, i.e., how to maximize benefits and minimize costs of foreign investment while projecting a favorable investment climate. Chile believes that ANCOM's restrictions were detrimental to its own economy by alienating foreign investors and thus reducing badly needed inflows of foreign capital and technology. Other Andean countries are in partial agreement with the Chilean position, having opted to liberalize sections of the Foreign Investment Code after Chile's withdrawal. While it is true that the ANCOM investment restrictions have had an unfavorable impact on the U.S. investor, the degree to which these restrictions have contributed to the decline cannot be accurately measured. It is safe to say, however, that many other factors, including host government political stability and economic viability, contribute just as heavily to a favorable or unfavorable investment climate.

Four basic U.S. policy objectives are involved in U.S. direct investment in the Andean countries. The United States:

1. Advocates international free flows of capital between nations.

2. Desires to assist friendly developing countries to attract private investment which it views as an important source of technology, management skills, and capital.


4. Recognizes each country's right to regulate investment within its own borders.

Andean host-country actions have presented the United States with a dilemma over these objectives. Regulations implemented by Andean countries have restricted foreign investment operating in their countries and have hampered the flow of capital between them and the United States. Although these actions hinder the achievement of some policy objectives,
the United States is committed to the principle that each country has the right to regulate investment within its own borders. This policy is reasonable and advantageous to the United States and lends appropriate recognition to individual country sovereignty. History has shown that U.S. interference in other governments' policies and programs has proven detrimental to the overall interest of the United States. Moreover, investor reactions in the Andean countries indicate that most government investment controls, per se, do not necessarily deter such investments.

The U.S. policy of assisting developing countries' growth through bilateral and multilateral economic assistance and support of regional integration movements—such as the Andean Common Market—is sound. But because of the information void in the United States and host countries, we were unable to draw conclusions on the U.S. policy of supporting direct investment in the Andean countries. Host countries have doubtless benefited through additional jobs, technology and management science transfers, and capital inflows, and the United States has benefited from the resulting access to supplies of raw materials. But information was not available to measure the full costs and benefits to these countries.

We believe that the ANCOM situation reflects some of the current issues relative to all U.S. investment abroad and these issues' impact on the U.S. economy. For example, Andean host countries are demanding that foreign investors incorporate a greater percentage of locally-produced components in finished products. And they are eager to negotiate favorable terms with foreign companies that offer needed technology, complement national industries, and produce exportable products. We believe that this trend may eventually affect the U.S. balance of trade with these countries and, ultimately, can be expected to impact on U.S. exports to other markets.

A more pressing concern for the United States is continued access to vital energy and non-energy raw materials. Expropriation and nationalization actions over the past few years have drastically reduced U.S. investment in the raw materials sectors of ANCOM countries, other developing and developed countries. Investors from other industrialized countries—primarily to assure supplies of raw materials for their home countries—are increasingly competing with U.S. investors for access to natural resources. Moreover, there are indications that non-U.S. investors have been encouraged, if not financially assisted, by their home governments in these ventures.
The United States generally supports U.S. investment abroad through various programs and policies. 1/ But these supports may be insufficient in view of the Nation's increasing needs for strategic raw material imports and the decreasing presence of U.S. investors in foreign supply sources. We believe there is a need to establish the relationship between U.S. direct investment abroad and the availability of strategic raw materials resources to the United States. We also believe consideration should be given to the role and importance of U.S. investment abroad in establishing a definitive national raw materials policy.

The International Investment Survey Act of 1976 is a positive step toward accumulating the data needed to draw conclusions on the magnitude and impact of U.S. investment abroad. It gives the President wide latitude in collecting and analyzing the data for identifying issues affecting the U.S. economic welfare and national security. Thus its purpose is to generate an information base sufficient for policy formulation and decisionmaking.

RECOMMENDATIONS

Because of the strategic importance of raw materials to the U.S. national interest, increasing U.S. dependence on raw material imports, and the decreasing U.S. investor presence in foreign raw materials sources, we recommend that the Secretary of Commerce, under authority of the International Investment Survey Act of 1976, conduct studies to establish the relationship between U.S. direct investment abroad and the availability of raw materials resources to the United States. If such studies confirm that a strong relationship exists, we further recommend that the Secretary advise the Administration and the Congress of the need to develop cooperative efforts between the Government and U.S. firms in order to assure U.S. access to raw materials.

AGENCY COMMENTS

Informal comments from officials at the Departments of the Treasury, State, and Commerce, and the Overseas Private Investment Corporation and Congressional Research Service were used in updating and modifying this report. Also, formal comments were obtained from the Departments of State and Commerce, which oversee U.S. direct investment abroad.

1/In addition to OPIC programs and favorable U.S. tax policies discussed in this report, the U.S. Government offers Export-Import Bank loans and free and unlimited imports on certain raw materials.
State agreed with our conclusions and saw our study as projecting a balanced view of factors influencing American direct investment in Andean countries. Commerce regards our study as an informative, comprehensive, and interesting commentary on the U.S. investment position in six representative less-developed countries. It agreed that it would be highly useful for the Secretary of Commerce, under authority of the International Investment Survey Act of 1976, to gather data that may enable Commerce to determine the extent of the relationship between U.S. direct investment abroad and the availability of raw materials resources to the United States. Also, that if such studies indicate that a strong relationship exists, the Department of Commerce would be pleased to give consideration to advising the Administration and the Congress of procedures to develop cooperative efforts between the Government and U.S. firms in order to assure U.S. access to raw materials. (See apps. IX and X.)

MATTERS FOR CONSIDERATION BY THE CONGRESS

We believe that Department of Commerce studies to establish the relationship between U.S. direct investment abroad and the availability of raw materials resources to the United States would assist the Congress in its deliberations or policies relative to energy and non-energy raw materials. We also believe our report provides a frame of reference for legislative and executive branch policymakers' use in determining other issues of prime importance for inclusion in forthcoming Federal studies of U.S. direct investment abroad.
Ancom’s Foreign Investment Code

December 31, 1970

"Common Regime of Treatment of Foreign Capital and of Trademarks, Patents, Licenses, and Royalties"

Decision 24

The Commission of the Cartagena Agreement

In view of Articles 26 and 27 of the Cartagena Agreement and Proposal No. 4 of the Board;

Whereas in the Declaration of Bogotá it was recognized that foreign capital "can make a considerable contribution to the economic development of Latin America, provided it stimulates capital formation in the country where it is established, facilitates extensive participation of national capital in that process, and does not create obstacles to regional integration."

In the same document the governments proposed the adoption of "standards that will facilitate the use of modern technology, without limiting the market for products manufactured with foreign technical assistance and the coordination of foreign investments with general development plans."

In the Declaration of Punta del Este the Presidents of America stated: "Integration must be fully at the service of Latin America. This requires the strengthening of Latin American enterprise through vigorous financial and technical support that will permit it to develop and supply the regional market efficiently." And they recognized that: "Foreign private enterprise will be able to fill an important function in assuring achievement of the objectives of integration within the pertinent policies of each of the countries of Latin America";

The Ministers of Foreign Affairs of the Member Countries of the Cartagena Agreement, at their first meeting in Lima, confirmed the conviction expressed in the Consensus of Viña del Mar that "economic growth and social progress are the responsibilities of their peoples and that attainment of national and regional objectives depend fundamentally on the effort of each country"; reaffirmed their determined support of "the sovereign right of every country to dispose freely of its natural resources"; adopted as a common policy "to give preference in the economic development of the subregion to authentically national
capital and enterprises of the Member Countries" and recognized that the investment of foreign capital and the transfer of foreign technology constitute a necessary contribution to the development of Member Countries and that they "must receive guaranties of stability in the measure in which they really constitute a positive contribution."

DECLAR ES:

1. The programming of subregional development and the expansion of the market will generate new investment requirements in the various sectors of production. Consequently, it is necessary to establish common rules for foreign investment which will be consistent with the new conditions created by the Cartagena Agreement, in order that the advantages deriving from it may benefit national or mixed enterprises as defined herein.

2. The contribution of foreign capital and technology can play an important part in subregional development and help with the national effort to the extent that it constitutes an effective contribution toward attaining the objectives of integration and reaching the goals indicated in national development plans.

3. The standards of the common regime must clearly set forth the rights and obligations of foreign investors and the guaranties that will protect foreign investments in the subregion. In addition, they must be stable enough to work for the mutual benefit of the investors and the Member Countries.

4. The treatment given to foreign capital may not discriminate against national investors.

5. One of the fundamental objectives of the common regime must be the strengthening of national enterprises, in order to enable them to participate actively in the subregional market.

6. In line with this order of ideas, national enterprises must have the best possible access to the modern technology and new administrative practices of the contemporary world. At the same time, it is necessary to establish efficient mechanisms and procedures for the production and protection of technology in the territory of the subregion and to improve the terms under which foreign technology is acquired.
7. With the purpose of attaining the objectives set forth herein, common standards must contemplate mechanisms and procedures which are sufficiently efficient to make possible a growing participation of national capital in existing or future foreign enterprises in Member Countries, in such a way as to lead to the organization of mixed enterprises in which national capital has the majority interest and in which national interests will have the capacity to participate in determining fashion in the basic decisions of such companies. When the participation of national capital is represented by contributions of the State or of State enterprises, it may be less than the majority interest, provided its determining capacity in decision-making is guaranteed.

8. In compliance with the general spirit of the Cartagena Agreement and with the provisions of Article 92 thereof, the common regime must set standards "that will compensate for the structural deficiencies of Bolivia and cuador and ensure the mobilization and assignment of the resources needed for fulfillment of the objectives contemplated in the Agreement in their favor."

9. The common regime should also tend to strengthen the negotiating capacity of the Member Countries vis-à-vis other countries, enterprises which supply capital and technology, and international organizations which are concerned with these matters.

DECIDES:

To approve the following:

COMMON REGIME OF TREATMENT OF FOREIGN CAPITAL AND OF TRADEMARKS, PATENTS, LICENSES, AND ROYALTIES

CHAPTER I

Article 1. For the purposes of this regime, the following definitions are understood:

Direct Foreign Investment: Contributions, coming from abroad and belonging to foreign individuals or enterprises, made to the capital of an enterprise, in freely convertible currency, industrial plants, machinery, or equipment, and having the right to re-exportation of their value and the transfer of profits abroad.
Likewise, investments in local currency from funds which are entitled to be transferred abroad shall be considered to be foreign investments.

**Foreign Investor:** The owner of a direct foreign investment.

**National Investor:** The State, national individuals, national non-profit entities, and the national enterprises defined in this Article. Foreign nationals with consecutive residence in the recipient country of no less than one year, who renounce before the competent national authority the right to re-export the capital and to transfer profits abroad, shall also be considered to be national investors.

**National Enterprise:** An enterprise organized in the recipient country, more than 80% of whose capital belongs to national investors, provided that in the opinion of the competent national authority, that proportion is reflected in the technical, financial, administrative, and commercial management of the enterprise.

**Mixed Enterprise:** An enterprise organized in the recipient country and whose capital belongs to national investors in a proportion which may fluctuate between 51% and 80%, provided that in the opinion of the appropriate national authority, that proportion is reflected in the technical, financial, administrative, and commercial management of the enterprise.

**Foreign Enterprise:** An enterprise whose capital in the hands of national investors amounts to less than 51% or, if that percentage is higher, it is not reflected, in the opinion of the proper national authority, in the technical, financial, administrative, and commercial management of the enterprise.

**New Investment:** Investment made after July 1, 1971, in either existing or new enterprises.

**Reinvestment:** Investment of all or part of undistributed profits resulting from a direct foreign investment, in the same enterprise which produced them.

**Recipient Country:** The country in which the direct foreign investment is made.

**Commission:** The Commission of the Cartagena Agreement.

**Board:** The Board of the Cartagena Agreement.
Member Country: One of the Member Countries of the Cartagena Agreement.

Article 2. All foreign investors who wish to invest in one of the Member Countries must submit an application to the competent national authority, which, after evaluating it, will authorize the investment when it corresponds to the development priorities of the recipient country. The application must follow the model indicated in Annex No. 1 of the regime.

Upon the proposal of the Board, the Commission may approve common criteria for the evaluation of direct foreign investments in the Member Countries.

Article 3. Member Countries shall not authorize any direct foreign investment in activities which they consider are adequately covered by existing enterprises.

Likewise, they shall not authorize any direct foreign investment of which the purpose is to acquire shares, participations, or rights owned by national investors.

Direct foreign investments made in a national enterprise to prevent its imminent bankruptcy are excepted from the provisions of the preceding paragraph, provided the following conditions are met:

(a) That the agency in charge of supervising corporations in the respective country, or its equivalent, verifies that bankruptcy is imminent;

(b) That the enterprise proves that it has granted an option to purchase preferably to national or subregional investors; and

(c) That the foreign investor agrees to place on sale the shares, participations, or rights that he may acquire in the enterprise for purchase by national investors, in a percentage necessary to constitute a national enterprise, within a period not exceeding 15 years, which period will be established in each case according to the characteristics of the business sector. The authorization issued by the competent national authority shall specify the period of time and the conditions under which that obligation will be met, the way in which the value of the shares, participations, or rights will be determined at the time they are sold, and, if pertinent, the systems by which the transfer of the latter to national investors will be ensured.
Article 4. Authorization for foreign investors to participate in national or mixed enterprises may be given, provided that it signifies increasing the capital of the enterprise and that the participation in question does not change the enterprise's national or mixed nature.

Article 5. All direct foreign investments shall be registered with the competent national authority, together with the agreement specifying the terms of the authorization. The amount of the investment shall be registered in freely convertible currency.

Article 6. The authority which registers the investment, in coordination with the competent state divisions or bureaus in each case, shall be responsible for supervising the fulfillment of the obligations contracted by foreign investors.

In addition to the functions indicated in other provisions of this regime and those established in the regulations, the competent national authority shall:

(a) Supervise fulfillment of the commitments for national participation in the enterprise's technical, administrative, financial, and commercial management, and in its capital;

(b) Authorize in exceptional cases the purchase of shares, participations, or rights of national or mixed enterprises by foreign investors, in accordance with the provisions of Articles 3 and 4 of the present regime;

(c) Establish an information and price control system of the intermediate products that may be furnished by suppliers of foreign technology or capital;

(d) Authorize the transfer abroad, in freely convertible currency, of all amounts which enterprises or investors are entitled to transfer in accordance with this regime and with the national laws of the country concerned;

(e) Centralize the statistical, accounting, information, and supervisory records connected with direct foreign investments; and

(f) Authorize licensing contracts for the use of imported technology, trademarks, and patents.

Article 7. Foreign investors shall be entitled to re-export the invested capital when they sell their shares, participations, or rights to national investors or when liquidation of the enterprise occurs.
The sale of shares, participations, or rights, of a foreign investor to another foreign investor must be previously authorized by the competent national authority and will not be considered as re-exportation of capital.

**Article 8.** Re-exportable capital is understood to be the capital formed by the total of the original direct foreign investment which is registered and actually made, plus the reinvestments made in the same enterprise in accordance with the provisions of this regime and minus the net losses, if any.

In cases of participation of national investors, the foregoing provisions shall be understood to be limited to the percentage of direct foreign investment in connection with the reinvestments made and with the net losses.

**Article 9.** In the case of liquidation of the enterprise, the difference between the real value of the net assets and the re-exportable capital as defined in the previous article shall be considered as capital gain and may be transferred abroad after payment of the pertinent taxes.

**Article 10.** Foreign investors shall have the right to transfer abroad the amounts obtained from the sale of their shares, participations, or rights, after payment of the pertinent taxes.

**Article 11.** Conversion of the amounts that a foreign investor may have the right to transfer abroad shall be made at the rate of exchange prevailing at the time of drawing the draft.

**Article 12.** Reinvestment of profits earned by foreign enterprises shall be considered to be new investments and may not be made without previous authorization and registration.

**Article 13.** Governments of the Member Countries may permit reinvestment of the profits received by a foreign enterprise without any special authorization, up to an amount not exceeding 5% per year of the company's capital. In these cases, the obligation to register is still in force.

**Article 14.** Foreign credits contracted by an enterprise require previous authorization by, and must be registered with, the appropriate agency.

Global limits on foreign indebtedness may be authorized for specified periods. Credit contracts concluded within the authorized global limits must be registered with the appropriate authority.
Article 15. Governments of the Member Countries shall refrain from endorsing or guaranteeing in any form, either directly or through official or semi-official institutions, external credit transactions carried out by foreign enterprises in which the State does not participate.

Article 16. Transfers abroad made by enterprises covering amortization or interest because of the use of foreign credits shall be authorized in accordance with terms of the registered contract.

For foreign credit contracts concluded between the parent company and its affiliates or between affiliates of the same foreign enterprise, the real rate of annual interest may not exceed by more than three points the rate of interest of first class securities prevailing in the financial market of the country of origin of the currency in which the transaction is registered. For external credit contracts other than those indicated above, the real rate of annual interest to be paid by the enterprises will be determined by the competent national authority and it must be closely related to the prevailing conditions of the financial market of the country in which the transaction has been registered.

For the purposes of this article, real interest is understood to be the total cost that must be paid by the debtor for the use of the credit, including commissions and expenses of all kinds.

Article 17. In regard to domestic credit, foreign enterprises shall have access to short-term credit only, in accordance with the terms and conditions specified in the regulations which the Commission may issue on the matter upon the recommendation of the Board.

Article 18. All contracts on the importation of technology and on patents and trademarks must be examined and submitted for the approval of the competent authority of the Member Country, which must appraise the effective contribution of the goods incorporating the technology, or other specific forms of measuring the effects of the imported technology.

Article 19. Contracts on importation of technology must contain, at least, clauses on the following subjects:

(a) Identification of the terms of the transfer of technology;

(b) Contractual value of each of the elements concerned in the transfer of technology, expressed in a form similar to that followed in the registration of direct foreign investments; and
(c) Determination of the time period involved.

Article 20. Member Countries shall not authorize the conclusion of contracts for the transfer of foreign technology or patents which contain:

(a) Clauses by virtue of which the furnishing of technology imposes the obligation for the recipient country or enterprise to acquire from a specific source capital goods, intermediate products, raw materials, and other technologies, or of permanently employing personnel indicated by the enterprise which supplies the technology. In exceptional cases, the recipient country may accept clauses of this nature for the acquisition of capital goods, intermediate products or raw materials, provided that their price corresponds to current levels in the international market;

(b) Clauses pursuant to which the enterprise selling the technology reserves the right to fix the sale or resale prices of the products manufactured on the basis of the technology;

(c) Clauses that contain restrictions regarding the volume and structure of production;

(d) Clauses that prohibit the use of competitive technologies;

(e) Clauses that establish a full or partial purchase option in favor of the supplier of the technology;

(f) Clauses that obligate the purchaser of technology to transfer to the supplier the inventions or improvements that may be obtained through the use of the technology;

(g) Clauses that require payment of royalties to the owners of patents for patents which are not used; and

(h) Other clauses with equivalent effects.

Save in exceptional cases, duly appraised by the competent authority of the recipient country, no clauses shall be accepted in which exportation of the products manufactured on the basis of the technology is prohibited or limited in any way.

In no case shall clauses of this nature be accepted in connection with subregional trade or the exportation of similar products to third countries.
Article 21. Intangible technological contributions shall grant the right to payment of royalties, upon authorization by the competent national authority, but they may not be computed as capital contributions.

When these contributions are furnished to a foreign enterprise by its parent company or by another affiliate thereof, no payment of royalties shall be authorized and no deductions will be allowed in this connection for tax purposes.

Article 22. National authorities will undertake a continuous and systematic task of identification of available technologies on the world market for the various industrial fields, in order to have available the most favorable and advisable alternative solutions for the economic conditions of the subregion, and will forward the results of their work to the Board. This action will be carried on in coordination with the action adopted under Chapter V of this regime in connection with the production of national or subregional technology.

Article 23. Before November 30, 1972, the Commission, upon the recommendation of the Board, will approve a program directed toward promoting and protecting the production of subregional technology, as well as the adaptation and assimilation of existing technologies.

This program shall contain, among other elements:

(a) Special tax or other benefits to encourage the production of technology and especially that connected with the intensive use of input items of subregional origin or those designed to make efficient use of subregional productive factors;

(b) Development of exports to third countries of products manufactured on the basis of subregional technology; and

(c) Channeling of domestic savings toward the establishment of subregional or national research and development centers.

Article 24. The governments of the Member Countries shall give preference in their purchases to products that include technology of subregional origin in such form as the Commission may consider advisable. On the recommendation of the Board, the Commission may propose to the Member Countries the establishment of charges on products which use trademarks of foreign origin for which royalties have to be paid, when generally known or easily accessible technology is used in their production.
Article 25. Licensing contracts for the utilization of trademarks of foreign origin in the territory of the Member Countries may not contain certain restrictive clauses such as:

(a) Prohibition or limitation on the exportation or sale in certain countries of the products manufactured under the trademark concerned, or similar products;

(b) Obligation to use raw materials, intermediate goods, and equipment supplied by the owner of the trademark or his affiliates. In exceptional cases, the recipient country may accept clauses of this nature provided the prices correspond to current levels on the international market;

(c) Fixing of sale or resale prices of the products manufactured under the trademark;

(d) Obligation to pay royalties to the owner of the trademark for unused trademarks;

(e) Obligation permanently to employ personnel supplied or indicated by the owner of the trademark; and

(f) Other obligations of equivalent effect.

Article 26. At the proposal of the Board, the Commission may indicate production processes, products, or groups of products, with respect to which no patent privileges may be granted in any of the Member Countries. Likewise, it may decide on the treatment of privileges already granted.

CHAPTER II

Article 27. The advantages deriving from the duty-free program of the Cartagena Agreement shall be enjoyed only by products produced by national or mixed enterprises of the Member Countries, as well as by foreign enterprises which are in the process of being transformed into national or mixed enterprises, pursuant to the terms of this Chapter.
Article 28. Foreign enterprises that currently exist in the territory of any Member Country and that wish to enjoy the advantages deriving from the duty-free program of the Cartagena Agreement for their products must agree with the competent authority of the recipient country, within three years following the date the present regime enters into force, to their gradual and progressive transformation into national or mixed enterprises, in accordance with the provisions of Article 31.

At the end of the aforesaid three-year period, there must be in all cases a participation of national investors in the capital of the enterprises of no less than 15%.

The time period in which this transformation must be carried out may not exceed 15 years in Colombia, Chile, and Peru, and 20 years in Bolivia and Ecuador, from the date on which this instrument enters into force.

Upon completion of two-thirds of the time period agreed for the transformation, there must be a participation of national investors in the capital of the said enterprises of no less than 45%.

Foreign enterprises that currently exist will be understood to be those that are legally organized in the territory of the country on June 30, 1971.

Article 29. The national authorities responsible for issuing certificates of origin of merchandise shall grant such certificates to products produced by currently existing foreign enterprises which, within the period of three years referred to in the first paragraph of Article 28, formally express to the government of the recipient country their intention to transform into national or mixed enterprises.

The products of currently existing foreign enterprises which do not enter into the agreement to transform themselves into national or mixed enterprises within the aforesaid three-year period may not enjoy the advantages deriving from the duty-free program of the Agreement, and consequently they shall not be issued a certificate of origin by the competent authority.
Article 30. Foreign enterprises that may be established in the territory of any Member Country after July 1, 1971, shall agree, in representation of their shareholders, to place on sale for purchase by national investors, gradually and progressively, in accordance with the provisions of Article 31, the percentage of their shares, participations or rights necessary for the transformation of such enterprises into mixed enterprises, within a period which may not exceed 15 years in Colombia, Chile, and Peru, and 20 years in Bolivia and Ecuador.

In the case of Colombia, Chile, and Peru, the agreement must stipulate a participation of national investors in the capital of the enterprise of no less than 15% at the time production begins, no less than 30% upon completion of one-third of the agreed period, and no less than 45% upon completion of two-thirds of that period.

In the case of Bolivia and Ecuador, the progressive participation of national investors in the capital of the enterprise must be no less than 5% three years after production begins, no less than 10% upon completion of one-third and no less than 35% upon completion of two-thirds of the agreed period.

In figuring the percentages referred to in this Article, any participation of subregional investors or of the Andean Development Corporation shall be counted as national investors.

In all cases the period of 20 years with respect to Bolivia and Ecuador shall start to be counted two years after production begins.

Article 31. Agreements on the transformation of foreign enterprises into mixed enterprises must stipulate the following items, among others:

(a) The period of time for compliance with the obligation to transform the foreign enterprise into a mixed enterprise;

(b) The gradual scale for the transfer of shares, participations, or rights to national investors, including in that gradual scale, at least, the rules on minimum percentages referred to in Articles 28 and 30;

(c) Regulations that will ensure the progressive participation of national investors or their representatives in the technical, financial, commercial, and administrative management of the enterprise, at least as of the date on which the enterprise begins production;
(d) The method of determining the value of the shares, participations, or rights at the time of their sale; and

(e) The systems that will ensure the transfer of shares, participations, or rights to national investors.

Article 33. The products of foreign enterprises shall enjoy the advantages deriving from the duty-free program of the Cartagena Agreement during the period of time agreed for their transformation into mixed enterprises under the conditions agreed to in the pertinent agreement. If the enterprise should fail to fulfill the obligations of the agreement or if at the end of the agreed period the transformation of the foreign enterprise into a mixed enterprise has not been carried out, its products will cease to enjoy the advantages of the duty-free program, and consequently they will not be covered by certificates of origin.

Article 33. With respect to the matters covered by this regime, the rights established herein for foreign and mixed enterprises are the maximum which may be granted to them by the Member Countries.

Article 34. Foreign enterprises, of whose production 80% or more goes into exports to the markets of third countries, shall not be obligated to abide by the provisions of this Chapter. In that case, the products of such enterprises may not enjoy in any way the advantages deriving from the duty-free program of the Cartagena Agreement.

Article 35. The obligation upon foreign enterprises to place on sale certain percentages of the shares, participations, or rights of foreign enterprises in favor of national investors referred to in Articles 3, 28, and 30 shall be controlled by the competent national authority concerned. This obligation shall be fulfilled by sale to private individuals, to the State, or to State enterprises of the recipient country.

Article 36. Mixed enterprises shall be considered to be those in which the State or State enterprises participate, even if the participation is less than 51% of the capital, provided that the State representation has a determining capacity in the decisions of the enterprise. It shall be the duty of the Commission, on recommendation of the Board, to establish the minimum percentage of participation of the State or of the State enterprises referred to in this article, within three months following the date on which the present regime enters into force.
Article 37. Upon authorization by the competent national authority, foreign investors shall have the right to transfer abroad, in freely convertible currency, the verified net profits resulting from the direct foreign investment, but not in excess of 14% of that investment annually.

In special cases, the Commission may, upon the request of any Member Country, authorize higher percentages than that provided in this Article.

CHAPTER III
SPECIAL REGULATIONS BY SECTORS

Article 38. Each Member Country may reserve sectors of economic activity for national, public, or private enterprise and determine whether the participation of mixed enterprises in those sectors shall be admitted.

Without prejudice to the provisions of other articles of this Chapter, the Commission, on the recommendation of the Board, may determine the sectors which all the Member Countries shall reserve for national, public, or private enterprises and determine whether participation of mixed enterprises shall be admitted in them.

Article 39. Foreign enterprises in the sectors referred to in this Chapter shall not be obligated to abide by the provisions of the previous Chapter regarding the transformation of foreign enterprises into national or mixed enterprises. However, they shall be subject to the other provisions of the common regime and to the special provisions specified in Articles 40 to 43, inclusive.

Article 40. During the first ten years of the life of this regime, the activities of foreign enterprises in the sector of basic products under the concession system may be authorized, provided the duration of the contract does not exceed 20 years.

For purposes of this regime, the basic-products sector is understood to mean the one comprising the primary activities of exploration and exploitation of minerals of any kind, including liquid and gaseous hydrocarbons, gas pipelines, oil pipelines, and exploitation of forests.

Member Countries shall not authorize deductions on account of depletion to be made for tax purposes by enterprises investing in this sector.
The participation of foreign enterprises in the exploration and exploitation of liquid and gaseous hydrocarbons shall be authorized preferably in the form of contracts of association with State enterprises of the recipient country.

Member Countries may grant foreign enterprises established in this sector treatment different from that provided in Article 37.

Article 41. The establishment of foreign enterprises or new direct foreign investment shall not be permitted in the sector of public services. Investments which had to be made by currently existing foreign enterprises in order to operate under technically and economically efficient conditions are excepted from this rule.

For these purposes, public services are considered to be those that provide drinking water, sewers, electric power and lighting, cleaning and sanitary, telephone, postal, and telecommunications services.

Article 42. New direct foreign investment shall not be permitted in the sector of insurance, commercial banking, and other financing institutions.

Foreign banks which currently exist in the territory of the member countries shall cease receiving local deposits in current accounts, savings accounts, or time deposits within a period of three years from the date on which this regime enters into force.

Currently existing foreign banks which desire to continue accepting local deposits of any kind must convert into national enterprises, for which purpose they must place on sale shares representing at least 80% of their capital to be purchased by national investors within the period of time indicated in the previous paragraph.

Article 43. New direct foreign investment shall not be permitted in domestic transportation enterprises, advertising enterprises, commercial radio stations, television stations, newspapers, magazines, or enterprises engaged in domestic marketing enterprises of products of any kind.

Foreign enterprises which currently operate in these sectors must convert into national enterprises, for which purpose they must place on sale at least 80% of their shares for purchase by national investors within a period not exceeding three years from the date on which this regime enters into force.
Article 44. When, in the opinion of the recipient country, special circumstances exist, that country may apply other regulations than those provided in Articles 40 to 43, inclusive.

The products of foreign enterprises included in the sectors of this Chapter which do not agree to convert into national or mixed enterprises, or with respect to which the Member Countries apply different regulations than those referred to in the previous paragraph, shall not enjoy the advantages of the duty-free program of the Cartagena Agreement.

CHAPTER IV

Article 45. The capital of Stock companies must be represented in registered shares.

Bearer shares that currently exist must be converted into registered shares within a period of one year from the date on which this regime enters into force.

Article 46. When projects are concerned that pertain to products reserved for Bolivia or Ecuador by application of Article 50 of the Cartagena Agreement, the four remaining countries agree not to authorize direct foreign investment in their territories, except as stipulated in contracts signed before December 31, 1970.

Article 47. Upon the proposal of the Board, the Commission shall approve, no later than November 30, 1971, an agreement to avoid double taxation among the Member Countries.

Within the same period of time, the Commission, acting on the recommendation of the Board, shall approve a model agreement for the conclusion of arrangements on double taxation between the Member Countries and other states outside the subregion. In the meantime, the Member Countries shall refrain from concluding agreements of this nature with any country outside the subregion.

Article 48. The Member Countries agree to keep each other informed and to inform the Board regarding the implementation of this regime in their territories, particularly regarding the rules of Chapter II. Likewise, they agree to establish a continuing system for the exchange of information regarding authorizations for foreign investment or the importation of technology that they may grant in their territories, in order to facilitate a growing harmonization of their policies and to improve their negotiating capacity in order to obtain conditions no less favorable for the recipient country than those that have been negotiated in similar cases with any other Member Country.
Likewise, they agree closely to coordinate their action in the international organizations and forums which consider subjects relating to foreign investments or the transfer of technology.

**Article 49.** Without prejudice to the provisions of Articles 79, 81, and 99 of the Cartagena Agreement, any Member Country which considers that it is being harmed by imports of products from foreign enterprises made under the duty-free program of the Agreement, may apply to the Board for authorization to adopt the necessary corrective measures to prevent the damage.

**Article 50.** Member Countries shall not grant to foreign investors any treatment more favorable than that granted to national investors.

**Article 51.** In no instrument relating to investments or the transfer of technology shall there be clauses that remove possible conflicts or controversies from the national jurisdiction and competence of the recipient country or allow the subrogation by States to the rights and actions of their national investors.

Differences between Member Countries of this regime in regard to its interpretation or implementation shall be resolved by following the procedure indicated in Chapter II, Section D, "on the settlement of controversies," of the Cartagena Agreement.

**CHAPTER V**

**Article 52.** In accordance with the provisions of this regime and of Chapter II of the Cartagena Agreement, the Committee and the Board shall have the following powers and duties:

**The Commission**

(a) Decides on recommendations submitted by the Board for its consideration with respect to the treatment of foreign capital, industrial property, and the system of the production and marketing of technology, in compliance with this regime;

(b) Approves, on the recommendation of the Board, the regulations necessary for effective implementation of the common regime; and

(c) Adopts other measures which tend to facilitate the attainment of its objectives.

**The Board**

(a) Supervises the implementation and fulfillment of the regime and of the regulations approved by the Commission on this subject;
(b) Centralizes statistical, accounting, and other types of information relating to foreign investments or the transfer of technology, coming from Member Countries;

(c) Compiles economic and legal information regarding foreign investments and transfers of technology and furnishes it to Member Countries; and

(d) Recommends to the Commission necessary measures and regulations for the effective implementation of this regime.

Article 53. In adopting decisions on the matters covered by this regime, the Commission shall follow the procedures established in Article 11(a) of the Cartagena Agreement.

Article 54. Member Countries shall establish a Subregional Industrial Property Office, which shall have the following functions:

(a) To serve as liaison between the national industrial property offices;

(b) To compile information on industrial property and distribute it to the national offices;

(c) To prepare model licensing contracts for the use of trademarks and patents in the Subregion;

(d) To advise national offices on all matters connected with the implementation of common regulations on industrial property adopted in the regulations referred to in Provisional Article G:

(e) To carry out studies and to submit recommendations to the Member Countries on invention patents.

Article 55. Upon the recommendation of the Board, the Commission shall establish a subregional system for the development, promotion, production, and adaptation of technology, which shall also have the duty of centralizing the information referred to in Article 22 of this regime and distributing it among the member countries, together with the information it obtains directly on the same subjects and on the conditions for the marketing of technology.
TEMPORARY PROVISIONS

**Article A.** This regime shall enter into force when all the Member Countries have deposited in the Office of the Secretary of the Board the instruments by which they put it into practice in their respective territories, in accordance with the provisions of the second paragraph of Article 27 of the Cartagena Agreement.

**Article B.** Foreign investments existing in the territory of the Member Countries on the date this regime enters into force must be registered with the competent national authority within the following six months.

These investments shall continue to enjoy the benefits granted by the provisions currently in force in every respect that is not contrary to this regime.

**Article C.** Until the regulations called for in Temporary Article G hereof enter into force, the Member Countries shall refrain from signing unilateral agreements on industrial property with third countries.

**Article D.** Within the three months following the date on which this regime enters into force, each Member Country shall designate the authority or authorities that are competent to authorize, register, and supervise foreign investments and the transfer of technology, and shall inform the other member countries and the Board of such designation.

**Article E.** All contracts on the importation of technology and licenses for the use of trademarks and patents of foreign origin signed prior to the date on which this regime enters into force must be registered with the competent national authority within six months following that date.

**Article F.** Within six months following the date on which this regime enters into force, the Commission, at the recommendation of the Board, shall approve the regulations of the Sub-regional Industrial Property Office.

**Article G.** Within six months following the date on which this regime enters into force, the Commission, at the recommendation of the Board, shall adopt regulations for implementing the rules on industrial property, which shall cover, among others, the subjects listed in Annex No. 2.
Article H. The Member Countries agree not to establish incentives for foreign investment other than that contemplated in their industrial development legislation at the time this regime enters into force, as long as the obligation referred to in Article 28, second paragraph, of the Cartagena Agreement, on the harmonization of industrial development legislation, has not been fulfilled.

Likewise, before November 30, 1972, the Commission, on the recommendation of the Board, shall adopt the necessary measures to harmonize the system of incentives applicable to the other sectors.

Article I. Within three months following the date on which this regime enters into force, the Commission, on the recommendation of the Board, shall determine the treatment applicable to capital belonging to national investors of any Member Country other than the recipient country.

Within the same period of time, the Commission, on the recommendation of the Board, shall determine the rules to be applied to investments made by the Andean Development Corporation in any of the Member Countries.
ANNEX No. I

GUIDE LINES FOR THE AUTHORIZATION, REGISTRATION, AND SUPERVISION OF FOREIGN INVESTMENTS

Every application for foreign investment must contain:

I. Identification of the investor.

(a) Name or firm name;
(b) Nationality;
(c) Membership of Board of Directors;
(d) Composition of personnel and management;
(e) Economic activity;
(f) Copy of articles of incorporation.

II. Details of the investment.

(a) Financial resources in foreign exchange or credit;

   Currency in which the investment is made;
   Capital of national origin;
   Capital of foreign origin;
   Credit from parent company;
   Credit from other sources;
   Actual interest to be paid on credits.

(b) Physical or tangible resources, such as:

   Industrial plants;
   New and reconditioned machinery;
   New and reconditioned equipment;
   Spare parts;
   Loose parts and pieces;
   Raw materials;
   Intermediate products.
(c) Resources derived from technology or intangibles, such as:

- Trademarks;
- Industrial designs;
- Management capacity;
- Technical know-how, patented or not patented;
- Possible alternative know-how.

Technical know-how may be presented in the following forms:

1. Objects:
   - Samples;
   - Nonregistered models;
   - Machinery, apparatus, pieces, tools;
   - Working devices.

2. Technical documents:
   - Formulas, estimates;
   - Plans, drawings;
   - Unpatented inventions.

3. Instructions:
   - Notes on preparation, manufacture, and functioning of the product or the process;
   - Explanations or practical advice for use;
   - Technical booklets;
   - Supplementary explanations of patents;
   - Manufacturing diagrams;
   - Supervisory methods;
   - Amounts to be paid for royalties;
   - Identification of the recipient of royalties.

III. Requirements which are satisfied:

(a) Shortage of domestic savings;
(b) Shortage of foreign exchange;
(c) Lack of directive or administrative capacity;
(d) Need of access to scarce technological knowledge;
(e) Lack of capacity or of commercial contacts for the
sale of merchandise in international markets;
(f) Lack of local entrepreneurial spirit.

IV. Plan for progressive national participation;

(a) Percentage of shares to be placed in the hands of
national investors;
(b) Operating capacity;
(c) Exportable production;
(d) Additional employment generated;
(e) Importation of raw materials or intermediate
products in annual protection;
(f) Use of national input items.

ANNEX No. 2

PROVISIONS OF THE REGULATIONS FOR THE APPLICATION
OF STANDARDS ON INDUSTRIAL PROPERTY

(a) Determination of the signs, words, symbols, or names
that may be registered as trademarks;
(b) Provisions on ownership of the trademark, procedures
for acquiring it, persons holding the right, etc.;
(c) Standard classification of products for trademark
purposes;
(d) Publication and terms of opposition to the registration;
(e) Priority or right to opposition;
(f) Use of the privilege;
(g) Lapse for failure to use;
(h) Term of the privilege;
(i) Negotiation of the trademark;
(j) Standard causes on nullity, failure to renew, can-
celation by previous registrations, etc.;
(k) Classification of patents;
(l) Determination of the industrial products and processes
that may be patented according to the objectives of
the global strategy for development of the subregion;
(i) Conditions of patentability and, particularly, standard criteria to establish the innovation and the industrial application of the patent;

(n) Owners of the patent;

(o) Procedure for registration, opposition, method of putting the invention into practice, etc.;

(p) Term of the privilege; and

(q) Standards on industrial models and designs.

Source: U.S. Department of State
APPENDIX II

INVESTMENT PROFILE

BOLIVIA

I. STATISTICS (note a)

General

Area: 424,162 square miles
Population: 5.5 million
Capital cities: Administrative - La Paz (pop. 700,000), Constitutional - Sucre (pop. 48,000)
Major industrial centers: La Paz, Cochabamba (pop. 160,000), Santa Cruz (pop. 130,000)
Geographic location: Landlocked in the center of South America
OPIC insurance: Inconvertibility ($0.8 million), expropriation ($4.2 million), war ($1.0 million), as of August 31, 1976

Economy

Gross national product: $1.75 billion
Per capita income: $315
External debt: $315 million
Monetary reserve: $156.2 million
Inflation rate: 12 percent
Trade:

<table>
<thead>
<tr>
<th>Exports</th>
<th>Imports</th>
</tr>
</thead>
<tbody>
<tr>
<td>Value</td>
<td>Value</td>
</tr>
<tr>
<td>Principal products</td>
<td>Machinery and equipment, iron</td>
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<tr>
<td>$451 million</td>
<td>and steel, motor vehicle parts,</td>
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<tr>
<td>Tin ores and concentrates, other metals,</td>
<td>wheat, chemicals</td>
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<tr>
<td>coffee, crude petroleum</td>
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</tr>
<tr>
<td>Major partners</td>
<td>United States (26%)</td>
</tr>
<tr>
<td>United States (20%)</td>
<td>Latin American Free Trade Assn. (34%)</td>
</tr>
<tr>
<td>Latin American Free Trade Assn. (44%)</td>
<td>Japan (16%)</td>
</tr>
<tr>
<td>United Kingdom (11%)</td>
<td></td>
</tr>
</tbody>
</table>

a/Estimates are for 1975 unless otherwise stated.
Labor

Work force: 2.5 million
Major sectors: Recent work force estimates by sector unavailable, but 1972 estimates place 69 percent of the work force in agriculture.
Unemployment: 15 percent
Wages: Information not available.

II. CHARACTERISTICS OF U.S. INVESTMENT

Number and value

U.S. investment in Bolivia is relatively small. Unofficial sources list 43 U.S. firms as having investments there.

The U.S. Embassy roughly estimates that U.S. investors account for about $49 million, or 66 percent, of total foreign investment. The Embassy estimate of August 1975 is a compilation of estimates for some 20 U.S. companies and shows that about 60 percent of U.S. private investment dollars are for oil exploration costs rather than fixed investment.

Geographic distribution

Most U.S. firms in the service sector are located in the La Paz area. Mining and petroleum exploration investments are dispersed throughout the country.

Sectoral distribution

Mining

U.S. companies currently do little mineral mining in Bolivia. U.S. firms there are exploring new mining ventures that could result in substantial future investments.

Petroleum

Some eight U.S. oil companies have joined several other foreign oil companies in the search for new oil deposits, and all operate under performance contracts with the state-owned oil company. Contracts specify that companies will commit a minimum amount of money for exploration—$4 million to $5 million—over a period of
about 3 years. If oil is found, production is divided between the government and the companies according to percentages specified in the contracts. All contracts have a maximum life of 30 years, with the government taking ownership of the facilities at that time.

Finance

Three U.S. financial institutions operate as full service banks. Two are heavily involved in private sector loans to small and large businesses and in import/export financing. The other is primarily involved in governmental loans.

Manufacturing

The reason for so few U.S. manufacturing companies in Bolivia can largely be attributed to the lack of an internal market—about 2 million consumers—and the lack of transportation systems to other parts of Latin America and the world. Only one American \(^1\) and one Swedish manufacturing plant have agreed to comply with ANCOM Decision 24 regulations in order to participate in the common market.

Intensity

Firms operating in Bolivia can be described as capital-intensive. Although little money has been invested in the country to date, exploration undertaken by mining and petroleum companies could signify substantial dollar investments in the future.

III. FOREIGN INVESTMENT POLICY

ANCOM has granted Bolivia and Ecuador special treatment designed to aid the establishment of specific industries, open Andean markets to their products, protect their internal markets from competition from other Andean nations, and allow prolonged tariff protection against imports from outside ANCOM.

\(^1\)An informed source in the United States told us that the U.S. company is in the process of withdrawing from Bolivia because exports have not developed as expected and the Bolivian market cannot support the operation.
Bolivia has had difficulty in attracting the type of investment it wants to speed its economic development and to capitalize on the special ANCOM treatment. Consequently, the government has been lenient in applying Decision 24 regulations and receptive to foreign investment in general.

In December 1971, the government passed the Bolivian Investment Law, which created the National Investment Institute. The law applies to industry, mining, agriculture, livestock, renewable natural resources, construction, and tourism; guarantees equal treatment to foreign and domestic investors; and provides incentives for investors who register with the Institute. Among the incentives are "tax-holidays," exemption from import taxes for machinery and fixed assets, accelerated depreciation, exchange guarantees, and exemption from withholding taxes. Specific incentives by sector are shown on the following page.

Registration

Under Supreme Decree No. 11774 issued in September 1974, the Central Bank of Bolivia was designated as the competent body for applying Decision 24. Companies desiring to export to ANCOM countries are required to sign transformation contracts with the Central Bank.

Divestiture

Divestiture requirements in Bolivia are uncertain. A government official indicated that Bolivia intends to apply the divestiture provision of Decision 24 only to firms who want to participate in ANCOM. Firms that produce for local consumption or export markets would be exempt from the provision. The period of divestiture to minority ownership in Bolivia is 20 years.

Profit remittance

Government policy concerning the 14-percent profit remittance ceiling as specified in Decision 24 was uncertain. (ANCOM's profit remittance ceiling is now 20 percent.) Officials in the government recognized that Bolivia's free exchange of currency system would make it extremely difficult to administer such a limitation.
# BENEFITS AND INCENTIVES GRANTED BY BOLIVIA'S LAW OF INVESTMENTS

## NEW INDUSTRY

<table>
<thead>
<tr>
<th>BENEFITS AND INCENTIVES</th>
<th>A/ First Category</th>
<th>B/ Second Category</th>
<th>C/ Third Category</th>
<th>Existing Industry</th>
<th>Mining</th>
<th>Furniture Natural Resources</th>
<th>Construction</th>
<th>Tourism</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 - Exception from import duties and related additional fees, except charges for customs warehousing services and customs fees on machinery and equipment imported and used in the process of production (taxes paid only)</td>
<td>100% a/e</td>
<td>100% a/e</td>
<td>100% a/e</td>
<td>100% a/e</td>
<td>100% a/e</td>
<td>100% a/e</td>
<td>100% a/e</td>
<td>100% a/e</td>
</tr>
<tr>
<td>2 - Exception from customs duties and related additional fees and surcharge imposed by the Decree No 06400 of Jun 27/82 on imports of raw material and supplies not produced in the country except customs warehousing services and customs fees</td>
<td>100% a/e</td>
<td>75% a/e</td>
<td>5% a/e</td>
<td>100% a/e</td>
<td>100% a/e</td>
<td>100% a/e</td>
<td>100% a/e</td>
<td>100% a/e</td>
</tr>
<tr>
<td>3 - Refund of customs duties on raw materials and supplies imported and incorporated to the products exported if this benefit has not been already granted</td>
<td>100% a/e</td>
<td>100% a/e</td>
<td>100% a/e</td>
<td>100% a/e</td>
<td>100% a/e</td>
<td>100% a/e</td>
<td>100% a/e</td>
<td>100% a/e</td>
</tr>
<tr>
<td>4 - Tax exemption on transfers of capital and credits either domestic or foreign which have been already invested in the approved project</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>5 - Exception of national departmental and municipal taxes and university surcharges on production and sales of manufactured goods exported</td>
<td>100% a/e</td>
<td>100% a/e</td>
<td>100% a/e</td>
<td>100% a/e</td>
<td>100% a/e</td>
<td>100% a/e</td>
<td>100% a/e</td>
<td>100% a/e</td>
</tr>
<tr>
<td>6 - Option to adhere to the annual depreciation granted to fixed assets</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>7 - 40 year national departmental and municipal tax exemption on new constructions of the companies except charges on municipal public service. Exemption for a period of five years on real estate incorporated as capital of the company</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>8 - Proportional tax exemption on profits of Bolivian companies that invest in such projects for the purchase of new shares issued by companies on which they do not have capital participation. Such exemption will be granted until capital gains per participation reach 5% a/e</td>
<td>100% a/e</td>
<td>100% a/e</td>
<td>100% a/e</td>
<td>100% a/e</td>
<td>100% a/e</td>
<td>100% a/e</td>
<td>100% a/e</td>
<td>100% a/e</td>
</tr>
</tbody>
</table>

---

In the Department of Beni, Pando and Tarija and other areas of lesser economic and social development a 10 years tax exemption on profits and total income derived from an approved investment will be permitted.

The re-investment of profits will have an exemption from the total income tax, according to Articles 9th and 10th of Decree No 8819 of January 8 1969. Furthermore it will be entitled to the benefits corresponding to the category under which they are rated. Tax exemption will be granted temporarily on the basis of technical-economic studies made by the Ministry of Industry and Commerce.

OTHER BENEFITS NOT RELATED TO TAXATION

- Land for the establishment of industries will be supplied by the Government, even though they may not be a part of industrial complexes. State owned land concessions for investments and agricultural development, within legal limitations.

1° Subject to special legal regulations.

a/ First category—mining-metallurgical industrial Complex: iron ore mining, metal-mechanics basic chemistry, pharmaceutics, iron work, motor vehicles and electric equipment, industry and electronics.

b/ Second category—manufacturing of component parts and machinery: industrial machinery, agronomic, consumer goods and explosives and related materials.

c/ Third category—All industrial activities not included above.

Source: Government of Bolivia.
Reinvestment

The application of Decision 24 reinvestment limitations in Bolivia was uncertain. Recent legislation indicated that the 5-percent limit might be applied to firms interested in participating in ANCOM. (ANCOM's profit reinvestment ceiling is now 7 percent.)

Reserved sectors

Metal smelters, steel mills, and petrochemical complexes in their basic stages are considered strategic industries, subject to development by the government through its state-owned enterprises. However, foreign and national private capital can participate in these industries with the government if it is deemed in the national interest.

The hydrocarbon industry is also considered a basic and strategic industry. Exploration and exploitation of hydrocarbon deposits is available only through performance contracts with the government.

Other

Supreme Decree No. 13050 issued in November 1975 sets out specific guidelines and incentives applicable to assembly plants. Bolivia's objective in fostering this type of industry is to develop local industrial plants for component items by gradually enforcing greater local content in the finished products. Incentives offered include exemptions from customs, internal revenue, and other taxes; tariff protection; and accelerated depreciation.

IV. IMPACT OF INVESTMENT CONTROLS

ANCOM investment controls have had little impact on the U.S. investor, since most investments are in sectors excluded from ANCOM restrictions. Lack of specific guidelines was mentioned by some U.S. business representatives as a deterrent to future foreign investment. However, more frequently mentioned deterrents were (1) lack of adequate transportation systems for moving goods within and through the country, (2) absence of a consumer market, (3) absence of a skilled labor force, and (4) history of political turbulence and government intervention in industry.
V. FUTURE FOR U.S. INVESTMENT

Aided by recent political and economic stability, Bolivia has begun to attract increasing amounts of domestic and some foreign investments. Below are recent statistics published by its National Investment Institute.

Approved Projects (note a)

December 1971 to December 1975

<table>
<thead>
<tr>
<th>Year</th>
<th>Number of projects</th>
<th>Amount of investment (000 omitted)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1972</td>
<td>39</td>
<td>$18,185</td>
</tr>
<tr>
<td>1973</td>
<td>32</td>
<td>30,676</td>
</tr>
<tr>
<td>1974</td>
<td>52</td>
<td>52,536</td>
</tr>
<tr>
<td>1975</td>
<td>63</td>
<td>127,391</td>
</tr>
<tr>
<td>Total</td>
<td>186</td>
<td>$228,788</td>
</tr>
</tbody>
</table>

a/Does not include investments in the hydrocarbon industry.

According to an Institute official, approximately $35 million of the $229 million of approved investment is from foreign sources. The amount applicable to the United States could not be determined but is probably less than half of the $35 million.

U.S. investors have apparently adopted a wait and see attitude. It is generally agreed, however, that if investments are made they will continue to be in the extractive sector. According to U.S. businessmen, ANCOM does not hold much promise for success in the immediate future and the Bolivian market is too small to warrant manufacturing operations.
INVESTMENT PROFILE

CHILE (note a)

I. STATISTICS (note b)

General

Area: 292,258 square miles
Population: 10 million
Capital city: Santiago (pop. 2.7 million)
Major industrial centers: Santiago, Valparaíso (pop. 292,847), Concepción (pop. 196,317)
Geographic location: Southwest coast of South America
OPIC insurance: Inconvertibility ($26.4 million), expropriation ($30.6 million), war ($28.5 million), as of August 31, 1976

Economy

Gross national product: $6.59 billion
Per capita income: $659
External debt: $3.7 billion
Monetary reserve: $109.0 million
Inflation rate: 375 percent

Trade:

<table>
<thead>
<tr>
<th>Exports</th>
<th>Imports</th>
</tr>
</thead>
<tbody>
<tr>
<td>Value</td>
<td>$1.5 billion</td>
</tr>
<tr>
<td>Principal</td>
<td>Raw materials</td>
</tr>
<tr>
<td>products</td>
<td></td>
</tr>
<tr>
<td>Major</td>
<td>United States (9%)</td>
</tr>
<tr>
<td>partners</td>
<td>Japan (11%)</td>
</tr>
<tr>
<td></td>
<td>United Kingdom (8%)</td>
</tr>
<tr>
<td></td>
<td>West Germany (15%)</td>
</tr>
<tr>
<td></td>
<td>Argentina (10%)</td>
</tr>
</tbody>
</table>

a/Investment profile was prepared prior to Chile's withdrawal from ANCOM. We expect little immediate change in its investment policy or its ability to attract investments, however, since its policy bordered on total disregard for ANCOM's Foreign Investment Code and inability to attract U.S. investments appeared to be based on economic and political factors rather than its membership in ANCOM.

b/Estimates are for 1975 unless otherwise stated.
APPENDIX III

Labor

Work force: Countrywide statistics not available. Work force for the greater Santiago area estimated at 1.1 million.
Major sectors: Information not available.
Unemployment: 16.5 percent for the greater Santiago area.
Wages: Annual minimum wage as of September 1975 was about $295. Fringe benefits amount to 80 to 100 percent of payroll.

II. CHARACTERISTICS OF U.S. INVESTMENT

Number and value

There are approximately 125 U.S. firms with subsidiaries in Chile.

The U.S. Embassy estimates that U.S. investors account for about 33 percent, or $150 million, of total foreign investment, as shown below.

<table>
<thead>
<tr>
<th>Sector</th>
<th>Amount (million)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mining and smelting</td>
<td>$15</td>
</tr>
<tr>
<td>Petroleum</td>
<td>11</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>103</td>
</tr>
<tr>
<td>Other</td>
<td>21</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$150</strong></td>
</tr>
</tbody>
</table>

Geographic distribution

Most of the U.S. firms are in Santiago, Chile's capital city and largest industrial center. As a result of prior government attempts to disperse industry and population, some U.S. industrial plants are located in less developed parts of the country.

Sectoral distribution

Mining

There is little remaining U.S. investment in mining and smelting. Extractive companies are exploring new
mining ventures that could result in significant future dollar investment. However, such companies would be required, on a case by case basis, to accept the government of Chile as a partner in the venture. The exact equity distribution between partners is subject to negotiation.

**Petroleum**

U.S. investments in petroleum are concentrated in one company which distributes oil and petroleum by-products. A local distributor, Compania de Petroleos de Chile, has about half of the market with the U.S. company having 25 percent.

**Finance**

Included within the sector are two U.S. banks. Both have finance companies and one operates as a full service institution. Most of their loans are to the government.

**Manufacturing**

U.S. firms in the manufacturing sector can aptly be described as mixtures of small- to medium-sized enterprises. Many have been operating in Chile for several years. The highest concentration of U.S. firms is in the highly competitive pharmaceutical industry. A government-owned company has about 20 percent of the market. A U.S. firm is the largest foreign-owned manufacturer of pharmaceuticals and cosmetics and has about 7 percent of the market.

**Intensity**

Many of the U.S. firms can be categorized as technology intensive. This is especially true of the pharmaceutical and chemical firms. Many organizations that market U.S. technology and know-how are represented in the service sector.

**III. FOREIGN INVESTMENT POLICY**

Chile has a positive, virtually open-door, attitude toward foreign investment. It recognizes a need for foreign investment capital to complement national investment in order to get through its present severe economic straits.
Chile's current economic situation is the result of (1) a badly distorted price system inherited from the previous government, (2) the quintupling of oil prices and the higher price of other imports, and (3) a sharp decline in copper prices during the second half of 1974.

To attract needed foreign and domestic capital, Chile has:

-- Adopted a foreign investment statute defining its position vis-à-vis foreign investment.

-- Reduced tariff rates on imported items in order to stimulate competition and increase productivity.

-- Allowed increased interest rates to reflect the true cost of money, thus providing an incentive for greater domestic savings.

These measures placed Chile at odds with other ANCOM countries. For example, Chile's recently reduced tariffs on imported goods from other than ANCOM countries are lower than those agreed to by ANCOM countries. Also, its Foreign Investment Statute, Decree Law 600, is significantly more liberal than ANCOM's Decision 24.

Decree Law 600 establishes a policy of nondiscrimination between Chilean and foreign firms in such areas as taxes and regulations governing imports, exports, foreign exchange, depreciation, etc. It also totally or partially exempts from import duties or other charges the import of capital goods for projects that have more than 20 percent foreign capital.

Registration

Foreign companies are required under Decree Law 600 to register with the Foreign Investment Committee.

Divestiture

It was unofficially stated that Chile would require divestiture of majority ownership only of those firms that wanted to export to other ANCOM countries. Since Chile has withdrawn from ANCOM, it remains unclear whether and under what conditions divestiture will be required.
Profit remittance

Decree Law 600 does not specify limits on profit remittances but does provide guidelines for contracts between individual investors and the government. Contracts specify the rules governing foreign exchange, remittance abroad, taxation, etc., and duration of contract terms, which is normally 10 years but can be extended if authorized by the Committee.

Reinvestment

Decree Law 600 stipulates that reinvestment up to 10 percent of the original investment may be provided for in each contract. Higher reinvestment percentages must be negotiated with the Committee.

Reserved sectors

Only those areas reserved by law to national investment are excluded to foreign investors. Hydrocarbon deposits, although under state ownership, may be explored and exploited through operations contracts. The maximum term of the contract cannot exceed 5 years for exploration or 30 years for exploitation. Foreign investors may also engage in refining petroleum and any other industrial activity related to hydrocarbons.

Other

Chile is making a concerted effort to attract foreign investment. Decree Law 600 provides assurances to foreign firms that their investments will be dealt with in the same manner as local firms. Properties expropriated during prior governments have been returned or compensated. Although the government will most likely retain the copper operations, new investments in this sector are welcomed. Chile had exercised its option under article 44 of Decision 24 to exempt mining from ANCOM regulations. Banks and financial institutions were also excluded from ANCOM regulations.

IV. IMPACT OF INVESTMENT CONTROLS

Chile's liberal interpretation of ANCOM's Foreign Investment Code has been favorably received by U.S. investors in the country. Despite this favorable opinion, however, there appears to be a general reluctance to
invest further in the economy. Past history of government expropriations, present economic and political problems, and uncertainty over AN:COM regulations have no doubt served to reduce the number and amount of investments.

V. FUTURE FOR U.S. INVESTMENT

A good indication of how U.S. investor interests compare with those of other countries is the list of registered investments published by Chile's Foreign Investment Committee. The following table illustrates this comparison. (Excluded from the information are all copper mining projects, petrochemical and automotive industries, and petroleum exploration.)

Registered Foreign Investment by Country (note a)

<table>
<thead>
<tr>
<th>Country of origin</th>
<th>Number of investments</th>
<th>Per-cent</th>
<th>Total investment (000 omitted)</th>
<th>Per-cent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Holland</td>
<td>5</td>
<td>4.6</td>
<td>$78,964</td>
<td>27.7</td>
</tr>
<tr>
<td>Japan</td>
<td>3</td>
<td>2.8</td>
<td>61,463</td>
<td>21.5</td>
</tr>
<tr>
<td>United States</td>
<td>35</td>
<td>32.1</td>
<td>51,117</td>
<td>17.9</td>
</tr>
<tr>
<td>Germany</td>
<td>9</td>
<td>8.2</td>
<td>40,587</td>
<td>14.2</td>
</tr>
<tr>
<td>Switzerland</td>
<td>7</td>
<td>6.4</td>
<td>12,537</td>
<td>4.4</td>
</tr>
<tr>
<td>Other (note b)</td>
<td>50</td>
<td>45.9</td>
<td>40,532</td>
<td>14.3</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>109</strong></td>
<td><strong>100.0</strong></td>
<td><strong>$285,200</strong></td>
<td><strong>100.0</strong></td>
</tr>
</tbody>
</table>

a/Over the last few years, registered investments have significantly exceeded actual investments. Hence, the figures shown above are anticipated investments which may not be realized for several years.

b/Includes registered investments by firms from 20 countries and one international investment company.

Although estimates are not available, indications are that significant investment could take place in the copper and petroleum extractive sectors. Renewed interest is due to the vast amount of copper resources, government willingness to develop a petroleum industry, and present favorable political and pro-foreign investment.
Climate. The nature of these investments will be different from the past, however, as the government has made it known that it will take equity participation in mining ventures and will allow petroleum exploration under performance contracts.

Apart from possible investment in the extractive industries, U.S. investment will be spread among several sectors, as shown below.

**Registered Foreign Investment by Sector**

October 1974 to December 1975

<table>
<thead>
<tr>
<th>Sector</th>
<th>Total</th>
<th>U.S. Share</th>
<th>U.S. share as a percent of total</th>
</tr>
</thead>
<tbody>
<tr>
<td>(000 omitted)</td>
<td>(000 omitted)</td>
<td>(000 omitted)</td>
<td></td>
</tr>
<tr>
<td>Minerals</td>
<td>$175,271</td>
<td>$10,700</td>
<td>6.1</td>
</tr>
<tr>
<td>Industry</td>
<td>58,628</td>
<td>14,137</td>
<td>24.1</td>
</tr>
<tr>
<td>Services</td>
<td>17,815</td>
<td>9,877</td>
<td>55.4</td>
</tr>
<tr>
<td>Energy and combus-</td>
<td>14,903</td>
<td>14,903</td>
<td>100.0</td>
</tr>
<tr>
<td>tibles</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Finance</td>
<td>9,683</td>
<td>1,440</td>
<td>14.9</td>
</tr>
<tr>
<td>Transportation</td>
<td>7,522</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Agriculture</td>
<td>1,378</td>
<td>60</td>
<td>4.4</td>
</tr>
<tr>
<td>Total</td>
<td>$285,200</td>
<td>$51,117</td>
<td>17.9</td>
</tr>
</tbody>
</table>

Source: Foreign Investment Committee, Chile.
APPENDIX IV

INVESTMENT PROFILE

COLOMBIA

I. STATISTICS (note a)

General

Area: 439,621 square miles
Population: 23.5 million
Capital city: Bogota (pop. 3.2 million)
Major industrial centers: Bogota, Medellin (pop. 1.2 million), Cali (pop. 1.0 million)
Geographic location: Northwest corner of South America

OPIC insurance: Inconvertibility ($10.4 million), expropriation ($55.4 million), war ($43.8 million), as of August 31, 1976

Economy

Gross national product: $13.01 billion
Per capita income: $553
External debt: $2.9 billion
Monetary reserve: $522 million
Inflation rate: 24 percent

Trade:

<table>
<thead>
<tr>
<th>Exports</th>
<th>Imports</th>
</tr>
</thead>
<tbody>
<tr>
<td>Value</td>
<td>Value</td>
</tr>
<tr>
<td>Principal products</td>
<td>Principal products</td>
</tr>
<tr>
<td>$1.520 billion</td>
<td>$1.481 billion</td>
</tr>
<tr>
<td>Coffee, metals, agricultural products, apparel, chemicals</td>
<td>Machinery, equipment, chemicals, metal products</td>
</tr>
<tr>
<td>Major partners</td>
<td>Major partners</td>
</tr>
<tr>
<td>United States (39%)</td>
<td>United States (43%)</td>
</tr>
<tr>
<td>West Germany</td>
<td>West Germany</td>
</tr>
<tr>
<td>Japan</td>
<td>Japan</td>
</tr>
<tr>
<td>ANCOM</td>
<td>ANCOM</td>
</tr>
</tbody>
</table>

Labor

Work force: Countrywide statistics not available.
Major sectors: Agriculture (about 50 percent of work force).
Unemployment: Estimated to be over 10 percent.
Wages: Minimum daily wage about $1.30.

a/Estimates are for 1975 unless otherwise stated.

b/Export-import data on other countries unavailable.
II. CHARACTERISTICS OF U.S. INVESTMENT

The registration of foreign direct investment has been required in Colombia since Decree 444 was passed in March 1967. All existing and new investments must be approved by the National Planning Board (the Ministry of Mines and Petroleum must also approve investments in mining and hydrocarbon deposits) and registered with the Office of Exchange, Bank of the Republic. For this and other reasons, foreign direct investment data in Colombia is somewhat better than that found in other ANCOM countries.

Number and value

According to unofficial sources, approximately 230 U.S. firms have investments in Colombia.

Value of foreign investments registered with the Bank of the Republic as of December 1974, excluding petroleum and natural gas, was $584.5 million. 1/ If the estimated value of petroleum and natural gas investments, including pending registrations, were included, the amount of all foreign investments would total $969.5 million. The following table breaks this down by sector.

<table>
<thead>
<tr>
<th>Sector</th>
<th>Registered investments (millions)</th>
<th>Percent of total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Manufacturing</td>
<td>$395.5</td>
<td>40.8</td>
</tr>
<tr>
<td>Petroleum and natural gas</td>
<td>385.0</td>
<td>39.7</td>
</tr>
<tr>
<td>Retail and wholesale trade</td>
<td>59.0</td>
<td>6.1</td>
</tr>
<tr>
<td>Banks, finance, and insurance</td>
<td>89.0</td>
<td>9.1</td>
</tr>
<tr>
<td>Transportation</td>
<td>11.3</td>
<td>1.2</td>
</tr>
<tr>
<td>Mining</td>
<td>14.4</td>
<td>1.5</td>
</tr>
<tr>
<td>Agriculture</td>
<td>5.9</td>
<td>0.6</td>
</tr>
<tr>
<td>Miscellaneous</td>
<td>9.4</td>
<td>1.0</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$969.5</strong></td>
<td><strong>100.0</strong></td>
</tr>
</tbody>
</table>

1/Registered value is calculated as initially imported capital plus additional foreign capital contributions and eligible profit remittances less capital remitted.
U.S. firms account for about $745 million, or 77 percent, of total foreign investments. Although a breakdown of U.S. investments by sector is not available, indications are that it would closely parallel the breakdown shown for all foreign investment.

**Geographic distribution**

U.S. investments are mostly concentrated in the large industrial cities of Bogota, Cali, and Medellin. Bogota, the capital and most populous city, has the highest percent of firms. This could change, however, as the Colombian Government has decreed that all new foreign investments and major expansions to existing foreign investments must locate outside the country's three large industrial cities.

**Sectoral distribution**

**Mining**

As evidenced by the registered value of investments in the mining sector, there has been little foreign interest in this sector over the past few years. Renewed interest by two U.S. companies and other foreign investors, however, could significantly increase the amount of foreign direct capital in mining.

Nickel and coal projects could result in hundreds of millions of dollars of new investments. Negotiations between the government and prospective foreign investors, including the two U.S. firms, are in process.

**Petroleum and natural gas**

During 1955-70, there was considerable interest in petroleum production. Since 1970, however, the production of crude oil has decreased to a point where, by mid-1974, output did not cover domestic demand. Production is concentrated in two U.S. companies and the state-owned company. Reasons given for the general lack of interest in this sector are the rugged terrain of large sections of Colombia and a history of government-imposed price controls. 1/

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1/A Department of State official advised us that during the 2d quarter of 1976, a two-tier pricing system similar to that in the United States was established in Colombia to make petroleum exploration and development more attractive.
Unlike petroleum, natural gas has attracted considerable interest over the last few years. A substantial find by one U.S. oil company, together with a relaxation of price controls, could result in considerable foreign investments in this area.

Finance and insurance

Until recently, there were seven branches of foreign commercial banks, including two fully-owned U.S. branches, among 25 commercial banks operating in Colombia. As a result of a December 1975 decree requiring divestiture to local majority ownership, four foreign branches have since divested and the remaining three are in the process of divesting to minority ownership. Divestment must be accomplished by July 1978.

Although the foreign branches have only about 8 or 9 percent of the commercial bank business, they have considerable impact on the economy. For example, the two U.S. banks have total outstanding loans of about $450 million, over 75 percent of it outstanding to the government and private sources. Also, both are heavily involved in export/import financing; one finances about 10 percent of Colombia's exports and 15 percent of its imports.

In addition, several U.S. finance organizations participate in local finance corporations and commercial banks and/or operate representative offices.

Several foreign companies are involved in the insurance business, but handle only an estimated 20 percent of total business. Some of the businesses operate as branches of foreign companies, others participate in Colombian-owned companies.

Manufacturing

Chemicals, pharmaceuticals, and rubber products comprise about 46 percent of foreign investments in manufacturing. Registered value of direct foreign investments in manufacturing as of December 31, 1974, is as follows.
APPENDIX IV

<table>
<thead>
<tr>
<th>Product</th>
<th>Registered value (millions)</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Chemicals, pharmaceuticals, and rubber products</td>
<td>$182.5</td>
<td>46</td>
</tr>
<tr>
<td>Metalworks, electrical and non-electrical machines, and transport equipment</td>
<td>64.8</td>
<td>17</td>
</tr>
<tr>
<td>Pulp, paper, and printing</td>
<td>44.5</td>
<td>11</td>
</tr>
<tr>
<td>Food and beverages (mostly canned foods and soft drinks)</td>
<td>35.7</td>
<td>9</td>
</tr>
<tr>
<td>Non-metallic minerals (mostly glass and portland, and asbestos cement products)</td>
<td>28.7</td>
<td>7</td>
</tr>
<tr>
<td>Textiles (mostly synthetic fibers)</td>
<td>21.9</td>
<td>6</td>
</tr>
<tr>
<td>Basic metals (mostly aluminum)</td>
<td>8.7</td>
<td>2</td>
</tr>
<tr>
<td>Miscellaneous</td>
<td>8.6</td>
<td>2</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$395.5</strong></td>
<td><strong>100</strong></td>
</tr>
</tbody>
</table>

Source: Bank of the Republic

Although the preponderance of total manufacturing operations and goods are Colombian, foreign-owned firms dominate the production of selected items, primarily through a high concentration of investments within certain product lines. For example:

--One Canadian and three U.S. firms produce a substantial percentage of the pulp, paper, and cardboard.

--Three U.S. companies produce 100 percent of the tires.

--About 60 firms, primarily from the United States and Europe, control 90 percent of pharmaceutical production; 240 Colombian firms control 10 percent.

--One U.S. company produces most of the window glass.

Several U.S. firms also produce basic chemicals and fibers; others control products through patents and licenses to Colombian producers.

82
Wholesale and retail trade

The wholesale and retail trade is primarily in the hands of Colombian merchants. The majority of retail business is conducted by "Mom & Pop" stores. The largest foreign-owned retail establishment—a U.S. subsidiary—has about 5 percent of the local market.

Intensity

U.S. firms in Colombia are a mixture of technology and labor intensive companies, primarily due to the large portion of investment in the manufacturing and service sectors.

III. FOREIGN INVESTMENT POLICY

Colombia welcomes foreign investments that complement its development plan and comply with its investment regulations. Decree 444, approved March 22, 1967, Colombia’s first comprehensive attempt to regulate foreign investments, formed the basis for some of ANCOM’s Decision 24 restrictions on foreign investments. For example, Decree 444 requires that all investments (1) be approved by a competent national agency, (2) have a 14-percent profit repatriation limit, and (3) have limited payments for royalty and technical service contracts. Decision 24 and Decree 444 work as a system of control, analysis, prior approval, and registration of foreign investments in Colombia.

Although Colombia was at the forefront of ANCOM countries in monitoring and regulating foreign investments, its stance on Decision 24 has been somewhat less certain. Decision 24 was initially approved and implemented by presidential decree in November 1971, only to be turned down by the Supreme Court of Colombia because of a technicality. It was finally put into effect after much judicial and political struggle by Decree 1900 of September 15, 1973, almost 3 years after the initial implementing decree.
Registration

All new foreign investments and reinvestments over 5 percent of registered value, 1/ except for exploration and exploitation of petroleum and natural gas, must be approved by the National Planning Board. Investments in petroleum and natural gas must be approved by the Ministry of Mines and Petroleum. Foreign investment in mining and minerals and the refining, transport, and distribution of hydrocarbons require the approval of both the National Planning Board and the Ministry of Mines and Petroleum.

All new foreign investments and reinvestments since 1967 must be registered with the Bank of the Republic.

Divestiture

Foreign firms incorporated in Colombia beginning January 1, 1974, must agree to divest themselves of 51 percent foreign ownership over a 15-year period. Existing firms that want to participate in ANCOM trade must also agree to divestiture. 2/ The National Planning Board, however, has placed no time limit on when firms must sign transformation contracts in order to participate in ANCOM.

Under recent legislation, foreign-owned banks and insurance companies must also divest themselves of 51-percent ownership. Although the legality of this action was contested in the courts, the Colombian Supreme Court ruled the legislation constitutional.

Profit remittance

The ANCOM 14-percent limit on profit remittances was applicable in Colombia. The 14-percent limit was calculated upon registered value of the investment after taxes. It is anticipated that ANCOM's new 20-percent limit will be applied.

1/The limitation may be increased to 7 percent to conform to recent ANCOM Decision 24 modifications.

2/A mid-1976 decree established a fund authorizing up to $50 million in financing to facilitate the local buyout of foreign investment.
Reinvestment

Reinvestments over 5 percent of registered value had to be approved by the National Planning Board. It is anticipated that ANCOM's new 7-percent limit will be administered in the same manner.

Reserved sectors

New direct foreign investments are not permitted in the following sectors.

--Public services--drinking water, sewer, electric power and lighting, cleaning and sanitary services, telephones, mail, and telecommunications.

--Finance--insurance, commercial banking, and other financing institutions.

--Others--internal transportation, advertising, commercial radio stations, television stations, newspapers, magazines, journals.

Other

Colombia is interested in attracting foreign investments that will (1) offer a real contribution to its technology, (2) relocate to lesser developed areas of the country, (3) accept local participation in ownership, (4) benefit its balance of payments, and (5) have a favorable impact on employment. Colombia is not interested in developing new industries that simply produce presently imported items. It is primarily interested in firms that can produce exportable products.

IV. IMPACT OF INVESTMENT CONTROLS

The investment climate can be appropriately described as uncertain. Colombia began to monitor and control foreign investments in 1967 with the issuance of Decree 444. Hence, when ANCOM adopted its Foreign Investment Code in December 1970, Colombia had already been following some of the code's regulatory provisions. However, Decision 24 requirements went beyond those in effect in Colombia and this caused disagreement in the country. It was only after a considerable legal battle that the Colombian Government was allowed to implement Decision 24 requirements.
More recently, the foreign-owned banks in Colombia, after initially being exempted from ANCOM's divestment rule, were told that they would have to sell 51 percent of their shares to Colombians. Banks unwilling to comply with this requirement were to start liquidating their activities by December 31, 1976. Although this mandate was contested in the courts, the Colombian Supreme Court recently ruled it constitutional.

A direct correlation between the uncertain investment climate and investor reaction cannot be drawn, but as the chart on the following page indicates, investor interest decreased during periods of uncertainty.

The following were cited as additional problems with doing business in Colombia.

--Companies are actively encouraged to sign divestment agreements with the government, yet the scarce available local capital is invested for a higher rate of return than U.S. business can provide.

--Price controls on selected items have cut drastically into profits and made it difficult to operate in the country. The controls are especially prevalent in sectors controlled by foreign enterprises.

--New and additional production facilities must locate outside the three large industrial cities because of government efforts at population and industrial dispersion.

--Inflation and exchange losses from devaluation severely cut into profits.

V. FUTURE FOR U.S. INVESTMENT

For the most part, U.S. investors have adopted a wait and see attitude pending further amplification of Colombia's foreign investment position. Potential significant investments could occur in the extractive sector (coal, nickel, natural gas) if current negotiations are successful.
ANNUAL FLUCTUATIONS IN THE AMOUNT OF GOVERNMENT APPROVED INVESTMENTS (note a)

Events:
- Decree 444 approved March 1967
- Decision 24 implemented in Colombia November 1971
- Implementation invalidated by Supreme Court January 1972
- Decision 24 reimplemented April 1973
- Foreign banks told to divest February 1975

MILLIONS OF DOLLARS

18.4 20.0 27.4 9.3 33.6 16.8 128.1 56.2

a) Does not include petroleum and gas related investments.
Source: Colombia's Departamento Nacional de Planeación
Colombia is being very selective in the types of investments it will allow in the country. The investor must be able to demonstrate positive effects from the investment, preferably in the form of export earnings, employment, technology, population dispersion, and local investor participation.
INVESTMENT PROFILE

ECUADOR

I. STATISTICS (note a)

General

Area: 104,506 square miles
Population: 6.7 million
Capital city: Quito (pop. 550,000)
Major industrial centers: Quito, Guayaquil (pop. 900,000)
Geographic location: Upper Pacific coast of South America
OPIC insurance: Inconvertibility ($5.9 million), expropriation ($13.2 million), war ($7.3 million), as of August 31, 1976

Economy

Gross national product: $4.2 billion
Per capita income: $625
External debt: $429 million
Monetary reserve: $285.7 million
Inflation rate: 16 percent
Trade:

<table>
<thead>
<tr>
<th>Exports</th>
<th>Imports</th>
</tr>
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<tbody>
<tr>
<td>Value</td>
<td>$912 million</td>
</tr>
<tr>
<td>Principal products</td>
<td>Bananas, cocoa, coffee, crude</td>
</tr>
<tr>
<td></td>
<td>petroleum</td>
</tr>
<tr>
<td>Major partners</td>
<td>United States (50%) ANCOM</td>
</tr>
<tr>
<td>(note b)</td>
<td>European Economic Community</td>
</tr>
<tr>
<td></td>
<td>Latin American Free Trade Association</td>
</tr>
</tbody>
</table>

a/Estimates are for 1975 unless otherwise stated.

b/Export-import data on other countries unavailable.
Labor

Work force: 2 million
Major sectors: Agriculture (56%), manufacturing (13%), services (17%).
Unemployment: Unemployment and marginal employment affect some 1.5 million persons. Illiteracy and lack of professional skills are widespread.
Wage: Minimum wage at the beginning of 1976 was about $54 a month. Accurate labor statistics are difficult to obtain because the government does not accumulate this data and statistics developed by other sources are generally misleading due to the high underemployment rate. Employment problems are compounded by a paucity of skilled labor, low educational standards, and scarcity of manufacturing jobs outside the Quito and Guayaquil regions.

II. CHARACTERISTICS OF U.S. INVESTMENT

Number and value

There are a total of 1' firms with U.S. ownership in Ecuador.

The U.S. Embassy estimated the value of U.S. direct investments at about $400 million as of March 1976, over $300 million of it in the petroleum industry. Unofficial estimates in the business community range as high as $750 million to $800 million. An Ecuadorean government official estimates that U.S. investment interests, including petroleum investments represent 80 percent of total foreign investment and foreign investment comprises an estimated 50 percent of the total investment in the country.

Geographic distribution

Except for the petroleum industry, U.S. investments are concentrated in the areas of Quito, the capital and industrial center, and Guayaquil, the major commercial and banking center. The petroleum industry is located in the eastern jungle, a largely undeveloped region.
Sect oral distribution

Petroleum

A joint investment by two U.S. oil companies represents 50 to 75 percent of all U.S. investment in-country. The consortium operates in partnership with the government and is the only major producer of crude petroleum.

Recent disagreements between one member of the consortium and the government has led to negotiations for the company's withdrawal from Ecuador. Indications are that the final settlement will result in full compensation, including substantial cash payment for the company's 37.5 percent interest in the partnership. If withdrawal terms follow through as indicated, the Ecuadorean Government would become the majority stockholder and the remaining U.S. company a junior partner with 37.5 percent of the equity.

Finance

Two major U.S. banks serve both as representatives for their U.S. parents and as commercial banking enterprises in the country.

Manufacturing

Manufacturing is the second largest sector for U.S. investment, most of it concentrated in subsidiaries of U.S. corporations. These investments are relatively small and involve such activities as paperboard, tires, metalworking, and pharmaceuticals.

Other

U.S. interests are also in such diverse areas as food-processing, transportation, agriculture, merchandising, fishing, and personal services. Although many in number, these firms represent a minority share of U.S. investment. Many of them are sales or service representatives of U.S. companies, others reflect direct investments by individuals.
Intensity

U.S. investments are high in capital intensity and technology. The oil-producing and manufacturing firms offer a degree of technology previously non-existent in the country, which gives them a competitive advantage. There are few U.S. investments in labor-intensive industries, such as textiles and agriculture.

III. FOREIGN INVESTMENT POLICY

Government officials have publicly stated that Ecuador welcomes foreign investment and is willing to work with prospective firms. The government, however, has been slow in establishing definitive investment regulations. Although general guidelines have been developed, most investments are considered on a case-by-case basis. Generally, however, investments which bring in new technology are the most welcomed.

Registration

All foreign investors are now required to register with the Ministry of Industry, Commerce, and Integration and the Central Bank. Investments made before June 30, 1971, had to be registered only with the Central Bank. The government is now developing an agency within this ministry to coordinate all official treatment of foreign investment activities. Registered value generally represents the actual value of assets at the time the investment was made.

Divestiture

Divestiture requirements effective as of June 30, 1974, differ according to whether the company was formed before or after July 1, 1971, as shown below.
Firms formed before July 1, 1971, were required to divest only if they wished to enjoy the benefits of the preferential tariff. Firms formed after that date were not given this choice. Due to its status as an underdeveloped member of the Andean community, Ecuador was given a special 20-year divestiture period instead of the customary 15. The 20-year period begins 2 years after the beginning of a firm's operations.

**Profit remittance**

Ecuador permitted a foreign firm to remit profits up to 14 percent of its registered capital each year. The 14 percent was a net amount after taxes. All profit remittances were required to be registered with the Central Bank. It is anticipated that the new ANCOM 20-percent limit will be administered in the same manner.

Although profit remittance is limited by law, government officials have indicated that the limit would present no problem due to Ecuador's free currency exchange.

**Reinvestment**

Foreign firms were allowed to reinvest profits in an amount up to 5 percent of registered capital. This was in addition to the 14 percent remittable. The 5 percent was based on income after taxes. It is anticipated that the new ANCOM 7-percent limit will be administered in the same manner.
Reserved sectors

Ecuador has exercised its rights under articles 38 to 44 of Decision 24 to reserve certain sectors of the economy for Ecuadorean regulation. In Supreme Decree No. 1029 of July 13, 1971, it exempted natural resources, public services, insurance, commercial banks and other financial institutions, internal transport, publicity, commercial radio broadcasters, television, newspapers, magazines, and entities devoted to internal marketing from Decision 24 guidelines. At the same time, it granted certain companies having investments in some of these areas special privileges relative to divestiture and profit remittances. For example, the U.S.-owned petroleum consortium is not limited in the amount of profits it can remit and is not subject to divestiture, and divestiture is not required by the banking sector.

Other

In general, the government wants to select foreign investments. Government officials say they want more investment in manufacturing, but less in merchandising. Investment in the more highly technological areas is encouraged, since the government recognizes the country must have foreign technology to develop.

Other government restrictions include:

--No new foreign investments in the banking sector, although current banks may continue operations and will not have to divest.

--No foreign investments in building construction companies unless the companies are at least 80 percent Ecuadorean-owned.

--No new foreign investments in merchandising unless the companies are 80 percent Ecuadorean-owned. Exceptions are made where the investments are considered necessary to advance sales technology in domestic marketing.

Ecuador obviously intends to protect its domestic firms through these controls. Generally, foreign investment must be considered on the level of the individual
firms, as the government has expressed a willingness to consider exceptions case-by-case.

IV. IMPACT OF INVESTMENT CONTROLS

A major problem with Ecuador's foreign investment policy is that the government is too indecisive and has not laid down definitive investment guidelines. Guidelines covering divestiture, new investments, and reinvestment requirements are not being uniformly enforced. Government officials say that much of this was by design, as they do not want to discourage potential investors with hard and fast rules which could not be waived for needed investments.

Since the eventual implementation of Decision 24 in Ecuador is not clear, U.S. investors refrained from commenting on specific regulations, but did comment on other difficulties encountered, as follows.

-- The government has reserved certain sectors of the economy and has instituted special procedures for controlling them. One of the most significant of these is merchandising, where new foreign firms are prohibited and existing firms must become 80 percent Ecuadorian-owned. Another is the extractive sector, where the petroleum companies are required to work in partnership with the government.

-- Labor is generally unskilled and formal training is almost nonexistent; therefore, each company must invest heavily in training. Organized labor is quite powerful, and the government is usually receptive to labor demands.

-- Eventually, the limits on reinvestment and profit remittances could pose a problem, as these levels are not high enough to encourage new investors.

V. FUTURE FOR U.S. INVESTMENT

Generally, Ecuador will not approve a new investment in a sector in which it feels Ecuadorian companies can be competitive, primarily commercial areas. The basic question asked when a new firm requests entry is: What can it do for Ecuador? In this light, the more desirable firms usually receive a warm welcome, with the government
willing to negotiate on an individual basis. The less desirable firms may be rejected.

Ecuador is anxious to obtain extractive and manufacturing firms. Firms engaged in the marketing of local goods are permitted if they bring in new systems which contribute to the expansion and diversification of local production.

At the present time, most investors are taking a wait and see attitude toward the investment situation. One investor summed up the feelings of U.S. businessmen by saying that businessmen can invest and operate under any conditions as long as they can calculate the risk, but at present that risk cannot be calculated in Ecuador. Thus, new investment will probably be slow in coming until the governmentformulates definitive guidelines.
INVESTMENT PROFILE

PERU

I. STATISTICS (note a)

General

Area: 496,222 square miles
Population: 16 million
Capital city: Lima (pop. 4 million)
Major industrial center: Lima
Geographic location: Central Pacific coast of South America
OPIC insurance: Inconvertibility ($9.5 million), expropriation ($0), war ($0), as of August 31, 1976

Economy

Gross national product: $10.7 billion
Per capita income: $786
External debt: $3.0 billion
Monetary reserve: $466.6 million
Inflation rate: 24 percent
Trade:

<table>
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<tr>
<th>Exports</th>
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<tr>
<td>Value</td>
<td>Principal products</td>
</tr>
<tr>
<td>$1.4 billion</td>
<td>Sugar, copper, fish products, iron ore</td>
</tr>
<tr>
<td>Major partners</td>
<td>United States (29%)</td>
</tr>
<tr>
<td>(note b)</td>
<td>European Economic Community</td>
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<tr>
<td></td>
<td>Japan</td>
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<td>ANCOM</td>
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<tr>
<td></td>
<td>United States (36%)</td>
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<tr>
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<td>European Economic Community</td>
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<td></td>
<td>ANCOM</td>
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</tbody>
</table>

a/Estimates are for 1975 unless otherwise stated.

b/Export-import data on other countries unavailable.
Labor

Work force: 5.0 million

Major sectors: Agriculture (41%), services (23%), manufacturing (16%)

Unemployment: The government does not release official statistics, so it is not possible to determine actual unemployment. Both unemployment and underemployment are high. The U.S. Embassy estimated in October 1975 that 1.149 million workers, or 23.5 percent of the work force, were not fully employed. A Lima University study on the 1972 census estimated that almost half of the "economically active population" was underemployed, with two-thirds of this underemployment in the agricultural sector. A Peruvian Labor Ministry official estimated that unemployment was 4 to 10 percent of the labor force, while 30 to 40 percent were underemployed.

Wages: Information not available.

II. CHARACTERISTICS OF U.S. INVESTMENT

Number and value

Unofficial sources list about 220 U.S. firms as having investments in Peru.

The U.S. Embassy estimates that U.S. investors account for about 90 percent, or $1.3 billion, of total foreign investment—$1.050 billion in mining, $0.140 billion in petroleum, and $0.110 in other areas. Other sources estimate U.S. investment at $2 billion, or 79 percent, of total foreign investment—$1.400 billion in mining, $0.300 billion in petroleum, $0.200 billion in manufacturing, $0.060 billion in commerce, $0.010 billion in finance, and $0.030 billion in other areas.

Geographic distribution

Most U.S. investments are in the vicinity of Lima, the commercial and manufacturing center of Peru. Two major exceptions are the petroleum and mining interests, which are centered in northern and southern Peru, respectively.
**Sectoral distribution**

**Mining**

Mining, Peru's major source of export earnings, is also its major recipient of U.S. investment. The bulk of these investments are in copper, where one consortium of four U.S. corporations accounts for a large percentage of production.

**Petroleum**

There are four major petroleum-producing companies, three of which are U.S. firms. Peru has invested heavily in oil exploration in the northeast jungle and, until early 1975, anticipated a rapidly expanding production base. Discoveries did not justify the high hopes. Unfortunately, only one firm found marketable quantities of oil and hopes to have the fields in production by early 1978.

**Manufacturing and commerce**

Many U.S. firms engage in manufacturing and commerce, but none are near the size of those U.S. firms in copper mining and petroleum. Major product lines of U.S. manufacturers include chemicals, pharmaceuticals, and metal work.

**Intensity**

U.S. investments are highly capital and technology intensive, especially in petroleum and mining.

**III. FOREIGN INVESTMENT POLICY**

Peru is a charter member of ANCOM and supports the limits on foreign investment set out in Decision 24 of the Cartagena Agreement. In implementing Decision 24, Peru has taken a very conservative approach. Publicly, the government welcomes direct foreign investment, but
its strict controls over profit remittances, reinvestment, and divestiture do not support this public claim. 1/

Registration

Peru established dual procedures for registering foreign investment. Each company must register its foreign ownership with the government agency which regulates its sector of the economy (industry, mining, fishing, etc.); individual investors must declare their investments to the Ministry of Economy and Finance.

Divestiture

The overriding factor in divestiture requirements is Peru's "industrial community" program, which requires a firm to use 15 percent of its annual pre-tax profits to purchase stock in the company for its employees or the industrial community. Eventually, the employees will own 33.3 percent of the firm and will share in its directorship and management. One unusual aspect of this type of divestiture is its direct relationship to a firm's profitability. Higher profits result in a faster rate of divestiture.

The industrial community concept has not been fully defined but may affect all types of industry (including extractive) and commercial activities, except where the government makes specific exceptions. Foreign branch banks and petroleum-producing companies operating under service contracts are not currently affected.

Profit remittance

Legally, foreign firms were allowed to remit profits up to 14 percent of registered foreign capital annually. This remittance was net of taxes and could come from current or prior year earnings. Due to tight currency controls, the firms had to apply for remittance rights through the Central Reserve Bank. In practice, the government has been slow to act on these applications, and

1/A shift in Peruvian policy appears to be underway. Recent ministerial and policy changes indicate that the government, faced with severe economic problems, is willing to postpone or abandon some of its socialist programs and practices.
many firms have been waiting 2 years or more to make remittances. A system is being developed to expedite remittance while maintaining their exchange value prior to final approval and transfer.

It is anticipated that ANCOM’s new 20 percent limit will be administered in the same manner.

Reinvestment

Technically, law permits a firm to reinvest profits up to 5 percent of its registered foreign capital annually without authorization and to reinvest an unlimited amount with government authorization. However, determining whether the 5 percent is net of taxes and obtaining authorization for additional amounts has caused problems. In practice, firms have found reinvestment to be difficult and to involve considerable delays.

It is uncertain at this time whether ANCOM’s new 7 percent limit on reinvestment will result in as many problems for investors.

Reserved sectors

The government has reserved the right to take over any activity it considers a basic products industry, including all natural resources, which are the basis for most foreign investment. It has also precluded new foreign investment in commercial banking, insurance, and commerce, and reserved the right to control companies engaged in public services, internal transport, communications, publicity, and internal commercialization of products. The long-term government role in these sectors remains uncertain.

IV. IMPACT OF INVESTMENT CONTROLS

Peru’s economy is depressed, inflation is rampant, and there is a severe capital shortage. Until recently, most policy decisions favored labor over industry and divestiture, reinvestment, and profit remittance practices did little to attract additional investments. As noted earlier, the government appears to be softening its socialistic position. However, the impact on future investor decisions is uncertain at this time.
The following were cited as problems with doing business in Peru.

--The "industrial community" program is unrealistic, as no business can function efficiently with a high percent of the stock and management decision-making responsibility entrusted to laborers.

--The government's slow response to requests for approval of reinvestments and profit remittances and its strict currency controls preclude normal remittances and reinvestments.

--Labor is unskilled, causing problems for technically oriented investors. Labor is also well organized and has the backing of the government.

V. FUTURE FOR U.S. INVESTMENT

At the time of our review, the future for U.S. investment in Peru was uncertain, but the immediate trend appeared negative. The government had taken few actions to encourage investments and had actually discouraged them, although this was contrary to its stated policy. Except for the extractive industry, no new investment had taken place and few new foreign investments were anticipated except where the government actually encouraged them.

In February 1977, a major U.S. consulting firm stated that because of the severe capital shortage and deficient internal savings, the government appeared likely to encourage more foreign investment especially in tourism and agro-industry. Also, investors that provide capital, technology, export possibilities, import substitutes, employment, and/or are willing to relocate to less developed areas may also be favorably looked upon.
INVESTMENT PROFILE

VENEZUELA

I. STATISTICS (note a)

General

Area: 352,143 square miles
Population: 12.4 million
Capital city: Caracas (pop. 2.5 million)
Major industrial centers: Caracas, Maracaibo
(pop. 900,000)
Geographic location: Northern coast of South America
OPIC insurance: Inconvertibility ($10.5 million),
expropriation ($31.9 million), war ($23.4 million),
as of August 31, 1976

Economy

Gross national product: $27.3 billion
Per capita income: $2,000
External debt: $756 million
Monetary reserve: $8.9 billion
Inflation rate: 10.3 percent

Trade:

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<th>Exports</th>
<th>Imports</th>
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<tbody>
<tr>
<td>Value</td>
<td>$8.9 billion</td>
</tr>
<tr>
<td>Principal</td>
<td>Petroleum, petroleum products, iron ore</td>
</tr>
<tr>
<td>products</td>
<td></td>
</tr>
</tbody>
</table>

Major partners

- United States (41%)
- West Germany
- Japan
- Netherland Antilles
- Italy

a/Estimates are for 1975 unless otherwise stated.

b/Export-import data on other countries unavailable.
Labor

Work force: 3.7 million (1974)
Major sectors: Extractive (0.5%), agriculture (22%), commerce (18%), manufacturing (17%), transportation and communications (7%), construction (6%), other services (29%)

Unemployment: A 1974 government survey showed an unemployment rate of about 6 percent; however, this is probably inaccurate. The President of Venezuela publicly stated that 32 percent of the labor force is unemployed or underemployed. Underemployment is obviously high, and unbalanced distribution of income concerns the government. Actual unemployment tends to be structural and seasonal in nature.

Wages: Wages are high by Latin American standards. In 1974, blue collar workers averaged $348 a month, white collar workers $802 not including substantial fringe benefits. Petroleum workers are the highest paid in Venezuela. Minimum wage is about $3.49 a day not including fringe benefits.

II. CHARACTERISTICS OF U.S. INVESTMENT

Number and value

The Superintendency of Foreign Investments has not finished registering foreign investments, but 1,367 firms were registered as having some foreign ownership as of March 1, 1976. These were subdivided as follows.

| National firms (more than 80 percent Venezuelan-owned) | 620 |
| Mixed firms (51 to 80 percent Venezuelan-owned) | 175 |
| Foreign firms (less than 51 percent Venezuelan-owned) | 572 |
| Total | 1,367 |

Registered value of these firms totaled about $1.4 billion, which represents their total value, not just the value of the foreign investment. Also, no statistics showing that portion allocable to U.S. firms were available.

The Central Bank estimated the value of U.S. investment in 1973 at about $1.1 billion, or 61 percent of total foreign investment excluding petroleum and iron ore mining, which were later nationalized. These investments were subdivided by sector as follows.
Since there have been no major changes in U.S. investment patterns in Venezuela over the past 2 years, these estimates should be fairly representative of the current situation.

**Geographic distribution**

Most foreign investments are centered around Caracas and Maracaibo, the major industrial and commercial cities. These two cities also represent the bulk of the Venezuelan market.

**Sectoral distribution**

Historically, U.S. investments in Venezuela have been dominated by petroleum companies. On January 1, 1976, however, Venezuela nationalized the petroleum industry, thereby reducing the value of U.S. investments in the country by about 47 percent. This followed the nationalization of the iron ore industry on January 1, 1975, which represented about 7 percent of U.S. investments. Currently, U.S. firms are concentrated in industry and commerce, as shown below.
Intensity

Foreign firms are highly capital and technology intensive. Firms generally invest in areas in which they are able to provide advanced technology.

III. FOREIGN INVESTMENT POLICY

Venezuela became the sixth member of ANCOM on January 1, 1974, and has since become a major proponent of its development goals. Basically, its policy on foreign investment is that of Decision 4 of the Cartagena Agreement. Government officials maintain there is still a place for foreign investors in Venezuela, but emphasize they will be required to abide by all the controls outlined in Decision 24.

Registration

The competent body established to monitor foreign investment is the Superintendency of Foreign Investments, an agency of the Ministry of Development.

Firms already in existence at January 1, 1974, were required to register their foreign capital with the Superintendency if they wanted to benefit from ANCOM tariff reduction provisions. Exceptions to this were firms in the automotive industry, which were required to register in all cases. Foreign firms entering Venezuela were required to seek investment approval for and to register with the Superintendency, regardless of whether they wished to enjoy the special tariff reductions.

The Superintendency has been slow to process registration applications. Also, many firms disagree with its valuation criteria, which basically sets the registered value as the value of assets actually brought into the country plus reinvestment of profits. This would not consider any expansions financed locally; consequently, firms stand to lose in negotiating nationalization cases.

Divestiture

All foreign-owned firms wishing to participate in ANCOM must become 51 percent Venezuelan-owned by 1989, the end of Venezuela's divestiture period. Foreign firms already active in sensitive areas reserved to
national companies must become 80 percent Venezuelan-owned by May 1977.

Divestiture is taking place very slowly, and many firms have not divested any stock as yet. Government officials say that divestiture will be accomplished on schedule, with government rather than private financing and ownership in some areas if necessary.

**Profit remittance**

Venezuela restricts the amount of profits that can be distributed to foreign investors to a maximum 14 percent a year (net after dividend tax, for an effective rate of 16.47 percent) of the value of the registered foreign investment. This amount can apparently be remitted without prior approval.

It is anticipated that ANCOM's new 20-percent limit will be administered in the same manner.

**Reinvestment**

The government allows foreign-owned firms to reinvest 5 percent of their registered investments each year. This allowance is automatic and is in addition to the 14 percent profit remittance. The 5 percent reinvestment can be accumulated for 5 years.

Firms which have agreed to divest at least 51 percent of their stocks are permitted to reinvest in excess of the 5 percent ceiling as long as national investors reinvest a proportionate amount. Other firms can reinvest beyond 5 percent only if they obtain permission from the Superintendency. The Superintendency has also indicated that profits unremitted and not reinvested may be freely used as working capital; however, this will not be used to raise the registered value unless permission for reinvestment is granted by the government.

It is anticipated that ANCOM's new 7-percent limit will be administered in the same manner.

**Reserved sectors**

Venezuela has reserved the following economic sectors to national companies and no new foreign investments will be allowed.
--Public services, including telephones, mail, telecommunications, potable water, sewers, electricity, and internal security.

--Television and radio, publications in Spanish (with the possible exception of technical journals), publicity, and commercialization of goods and services (except those manufactured by the merchandising firms in Venezuela).

--Professional and consulting activities regulated by national laws.

As previously noted, foreign firms in these areas are required to divest at least 80 percent of their ownership to Venezuelans. The government has also decreed that all foreign insurance companies, commercial banks, and financial institutions will be subject to special legislation.

Probably the most significant areas reserved to the country are in the extractive sector, where foreign petroleum and iron mining firms have been nationalized. These areas accounted for over 50 percent of total U.S. investment in Venezuela in 1973.

IV. IMPACT OF INVESTMENT CONTROLS

The current climate for new investments by U.S. firms is uncertain as there are considerable indecisiveness and bureaucratic delays in arriving at the government's eventual attitude toward and controls over foreign investment. Government officials state publicly that there is still a need and a place for foreign investment, but that investors must be willing to abide by the controls which implemented Decision 24. Moreover, the government wants investment only in sectors for which Venezuela does not have the necessary technology.

U.S. businessmen feel that the government really doesn't care whether new foreign investment is obtained or not. The country is wealthy by Latin American standards, due to its position as a major exporter of petroleum. The huge increase in petrodollar inflows in recent years has actually given Venezuela a capital surplus (highly unusual in Latin America), with a corresponding measure of financial independence. This has helped to spur a new sense of national pride, which many people
feel explains Venezuela's new role as a spokesman for the Third World and its ambivalence toward foreign investment.

In spite of its current attitude, the government recognizes that foreign capital will be necessary if the country is to realize its long-term development goals. Venezuela has no strong technological base, yet investment plans are concentrated in highly technological areas. Thus it must obtain this technology from other countries. This presents an interesting paradox. At the moment, Venezuela needs foreign technology but not foreign capital. However, foreign firms traditionally have been reluctant to invest their current technologies in enterprises in which they have little or no proprietary interests. U.S. iron and petroleum service contracts show that profits can still be had without this interest.

Undoubtedly, the most significant change in the Venezuelan foreign investment climate in recent years has been the nationalization of the petroleum and iron-mining sectors. These actions reduced the book value of U.S. investments in the country by more than 50 percent.

U.S. investors are very concerned with Venezuela's implementation of Decision 24, which is probably the purest and harshest interpretation or any of the ANCOM countries. In effect, Decision 24 is now Venezuelan law, and foreign firms are required to adhere strictly to its provisions. U.S. businessmen in Venezuela cite the following problems with the new controls:

--There is no way to predict what is going to happen in the area of foreign investment. The government has implemented controls which show little concern for the profitability or longevity of existing firms. Also, the rules are changing so fast, it is impossible to determine the future climate.

--Registration of foreign capital is proceeding very slowly and there have been disagreements on the determination of registered value. The Superintendency of Foreign Investments is very conservative in its determination, which is usually considerably lower than the book value. Cases have already been presented in the courts.
--Divestiture requirements are unrealistic. Most firms are not willing to give up 51 percent ownership. This attitude is changing somewhat as it appears that Venezuela is inflexible on this point, however, a secondary problem exists in finding buyers for this stock. Many U.S. investors feel there is not enough available capital in the country to assume this ownership. This is compounded by government attempts to discourage large blocs of ownership among the Venezuelans themselves. There is speculation that the government might have to assume temporary ownership to accomplish divestiture. Currently, most U.S. firms in Venezuela have not begun divestiture.

--The low profit remittance and reinvestment ceilings deter new investments, particularly in view of the high interest rates in the country.

--The country has placed a very low priority on certain types of activities for which new technology is not considered to be essential. Examples of this are food chains and department stores, where new investments are prohibited and existing firms must divest 80 percent ownership.

--Patent protection is poor and firms are allowed exclusive use for a period of only 5 years, which makes them reluctant to bring advanced technology into the country.

--The government is trying to reduce dependence on imports by encouraging manufacturers previously limited to assembly operations to also engage in fabrication. This would limit the involvement of the parent firm in the United States.

U.S. investors also cited the following problems which act as deterrents to new foreign investment:

--Wages and fringe benefits are quite high compared with other Latin American countries, and skill levels are low, causing problems in staffing the plants of the high-technology firms the country is seeking. Absenteeism is high, and productivity is declining. Management has difficulty in disciplining employees, as it is almost impossible and usually quite costly to dismiss an employee. Most firms are overstaffed.
APPENDIX VII

--The government has instituted price and production controls in certain sectors. The most notable is in the motor vehicle sector, where firms are required to produce a set percentage of price-controlled vehicles.

--Personal credit (credit cards) is discouraged, and interest rates on such operations are controlled. For the most part, the extension of personal credit by merchandising firms is a very costly service.

V. FUTURE FOR U.S. INVESTMENT

U.S. investors are quite concerned about the current investment climate. Their concern is not so much over the controls which implement Decision 24 as it is over the uncertainties involved. They say that the current government position is unrealistic, as it acts as a deterrent to the new investment the country needs. This is borne out by the fact that there have been no new major foreign investments in the past 2 years.

Both the government and U.S. investors agree that Venezuela will need foreign investment to meet its development goals. The question now is: Can Venezuela secure the technology it needs under its existing controls? According to U.S. investors, it probably can, but with limitations. First, new technology will probably come into the country through firms engaged in mixed ownership with Venezuelans and through technological contracts with existing firms rather than new, wholly-owned, U.S. subsidiaries. Secondly, this technology may not be the most up-to-date, as firms will be less willing to risk their technology in companies in which they have no proprietary interests.
TAX BENEFITS AS INDUCEMENTS FOR U.S.
DIRECT INVESTMENT IN ANCOM COUNTRIES

For U.S. direct investment, securing raw materials sources, overcoming tariff barriers, exploring new markets or maintaining old ones appear to be stronger considerations, singly or in combination, than tax benefits. Unfortunately, statistics are not available to permit an in-depth examination of the effects of U.S. and ANCOM country tax policies on U.S. direct investment in ANCOM countries. Further, we do not know to what extent ANCOM legal restrictions on foreign direct investment neutralize the incentive of tax preferences granted by U.S. or host country laws. It is, nevertheless, useful to examine the tax rules to learn how they are intended to affect foreign investment.

INSTITUTIONAL FRAMEWORK OF THE
TAXATION OF INCOME FROM MULTINATIONAL TRANSACTIONS
(JURISDICTIONAL RULES)

Two basic tax jurisdictional rules have been developed by the trading countries of the world—the source rule and the residence rule—and they are fundamentally inconsistent. Many countries use a combination of both approaches, taxing their residents on worldwide income and nonresidents on income from domestic sources. A foreign tax credit is then required to avoid double taxation of residents.

The source rule was developed in European countries which have a schedular income tax system (one in which the rates vary with the type and source of income). Under the source rule, jurisdiction to tax is asserted over all income having its source in the taxing state, without regard to citizenship or residence of the income recipient. If all countries adopted the source rule and applied the same rules for determining the source of income there could be no double taxation. But countries which tax their residents on worldwide income maintain that the source rule alone is defective in not taking into account the ability to pay out of total income net of deductions and personal exemptions. Moreover, conflicting source rules among countries make the source principle difficult to apply in practice.

Under the residence rule, jurisdiction to tax is based on residence (and sometimes citizenship) without regard to the source of the income. That is, worldwide income is regarded as the measure of the ability to pay for residents.
(and in the case of the United States, nonresident citizens) of the taxing state. Although simple in concept, the residence principle also is difficult to administer because countries cannot agree on a definition of residence for tax purposes. Citizenship, domicile, physical presence for a fixed period of time, or some combination of these factors are variously applied as criteria in different countries. And more importantly, few countries will agree to exempt from tax the income derived within their borders by nonresidents.

Generally, two major rules are used to determine the residence of a corporation—place of incorporation and seat of management. Under the first rule, a corporation is regarded as a resident of the country of incorporation; under the second, it is deemed to be a resident of the country from which its policy is controlled. With certain exceptions, the United States follows the place of incorporation rule. This means that a foreign subsidiary of a U.S.-incorporated parent company is not regarded as a resident of the United States; therefore U.S. taxation to the parent company of foreign-source profits earned by the subsidiary is postponed until the profits are repatriated. This is commonly referred to as "deferral" of unrepatriated earnings.

Under the seat of management rule, the income of foreign subsidiaries may be taxed currently (i.e., on an accrual basis) in the home country of the parent corporation if the requisite control is exercised by the parent over the affairs of the foreign subsidiary. The United States follows the seat of management concept to a limited extent in order to prevent tax evasion. Foreign source earnings retained abroad in a controlled foreign subsidiary of a U.S. parent may, in certain circumstances, be taxed to the parent on an accrual basis if little or no foreign tax is paid on such earnings. This is the so-called tax haven exception to the place of incorporation rule.

As mentioned above, in practice, most countries using the residence principle also impose a tax on income derived by nonresidents from sources within the taxing country. This extension of tax jurisdiction to nonresidents by countries following the residence rule may result in double taxation (the same income is taxed by both the country of source and by the country of residence).

Bolivia, Ecuador, and Venezuela follow the source principle, which means that foreign-source income is not taxed to domestic corporations and resident individuals. Chile,
Colombia, and Peru assert tax jurisdiction over the worldwide income received by a domestic corporation (defined in terms of residence or domicile). Chile makes no provision for the relief of double taxation of foreign source income. Colombia allows a deduction from income for foreign taxes paid on foreign source income. Peru follows the foreign tax credit method but reduces its tax on dividends remitted abroad if the home country taxes the dividends received at a rate of 30 percent or more. The tax jurisdiction rules of each country are summarized on the next page.

All ANCOM countries levy an additional tax on dividends paid by a subsidiary to its foreign parent and on branch profits remitted to the home office abroad. Although called a "withholding tax", this tax is quite different from most withholding taxes in that it constitutes the final determination of tax liability by the levying country. It is not a prepayment of the domestic income tax but a tax in addition to the domestic income tax payable with respect to domestic source income.

The United States follows the residence (resident taxpayers and all U.S. citizens whether or not U.S. residents) plus source (nonresident taxpayers) principle and allows a tax credit against U.S. tax for foreign taxes paid. Prior to the Tax Reform Act of 1976, two methods could be used to calculate the maximum amount of the credit—a per-country limitation and an overall limitation. Under both methods, the tax credit ceiling limited the amount of creditable foreign taxes to a pro rata share of the U.S. tax attributable to the foreign source taxable income. Under the per-country limitation, the tax credit ceiling was calculated on a country-by-country basis. Under the overall limitation, the tax credit ceiling was calculated on an aggregate basis. Under either method, if foreign taxes exceeded the calculated ceiling, they could be carried back 2 years and forward to the 5 succeeding taxable years. There was no carryback or carryover from a "per country" year to an "overall" year or vice versa. Under the overall method, now mandatory for taxable years beginning after December 31, 1975, foreign source income and losses from all countries are combined and expressed as a percentage of U.S. taxable income to determine the limitation on the credit.

The foreign tax credit covers both foreign income taxes paid directly by the U.S. taxpayer (e.g., taxes paid by a U.S. firm on foreign source branch profits) and foreign income tax paid by the subsidiary of a U.S. parent company with respect
<table>
<thead>
<tr>
<th>Country</th>
<th>Jurisdictional basis</th>
<th>Method for avoiding double taxation</th>
<th>Collection of additional tax on remittances</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bolivia</td>
<td>Domestic source income taxed to domiciled companies and branches and agencies of nondomiciled companies. Foreign-source business profits exempt.</td>
<td>Income derived from sources partly within and partly without Bolivia allocated as a percentage of gross income. Foreign-source income not taxable to corporations.</td>
<td>Withholding at source on income paid to nonresidents.</td>
</tr>
<tr>
<td>Chile</td>
<td>Worldwide income taxes to resident companies.</td>
<td>No unilateral measure to avoid double taxation.</td>
<td>Withholding at source on income paid to nonresidents.</td>
</tr>
<tr>
<td>Colombia</td>
<td>Worldwide income taxes to domiciled companies.</td>
<td>Foreign tax deduction but not in excess of Colombian taxes paid on same foreign earnings.</td>
<td>Withholding at source on income paid to nonresidents.</td>
</tr>
<tr>
<td>Ecuador</td>
<td>Domestic-source income taxed to resident corporations whether or not domiciled in Ecuador. Foreign source income is exempt, except 80% of foreign-source service income is taxable.</td>
<td>Only domestic-source income is taxable.</td>
<td>Withholding at source on income paid to nonresidents.</td>
</tr>
<tr>
<td>Peru</td>
<td>Worldwide income taxed to domiciled or resident companies.</td>
<td>Double taxation of non-Peruvian source income avoided by Peruvian foreign tax credit.</td>
<td>Withholding at source on income paid to nonresidents.</td>
</tr>
<tr>
<td>Venezuela</td>
<td>Domestic-source income taxed to both domiciled and nondomiciled entities.</td>
<td>Foreign-source income is not taxed.</td>
<td>Withholding at source on income paid to nonresidents at rates applicable to residents, plus 15% withheld remittance tax on branch profits and dividends.</td>
</tr>
</tbody>
</table>

to the foreign source income from which dividends are paid to the U.S. parent. The result is that combined U.S. and foreign tax on the repatriated earnings of a foreign subsidiary is the same as the U.S. corporation income tax on the undistributed earnings of a domestic corporation as long as the foreign tax rate (including withholding tax) is equal to or lower than the U.S. tax rate. For ANCOM countries, the statutory income tax rate on remitted branch profits and dividends is in most cases higher than the rate on earnings retained in country.

<table>
<thead>
<tr>
<th>Country</th>
<th>Dividends</th>
<th>Branch profits</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bolivia</td>
<td>51</td>
<td>51</td>
</tr>
<tr>
<td>Chile</td>
<td>52.44 to 70.42</td>
<td>18 to 49</td>
</tr>
<tr>
<td>Colombia</td>
<td>59.2</td>
<td>59.2</td>
</tr>
<tr>
<td>Ecuador</td>
<td>61.08</td>
<td>37</td>
</tr>
<tr>
<td>Peru</td>
<td>52 to 73</td>
<td>44 to 68.5</td>
</tr>
<tr>
<td>Venezuela</td>
<td>a/27.75 to 57.5</td>
<td>27.75 to 57.5</td>
</tr>
<tr>
<td></td>
<td>b/42.5 to 65</td>
<td></td>
</tr>
</tbody>
</table>

See next page for further details.

g/Percent of nominative shares.

b/Percent of bearer shares.
### APPENDIX VIII


*In percent of taxable income on remittance*

<table>
<thead>
<tr>
<th>Statutory income tax rate on income retained in host country (creditable against U.S. tax)</th>
<th>Statutory withholding rates on income remitted to United States (creditable against U.S. tax)</th>
<th>General sales or turnover tax (not creditable against U.S. tax)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Home country</strong></td>
<td><strong>Subsidiary</strong></td>
<td><strong>After-tax branch profit</strong></td>
</tr>
<tr>
<td><strong>United States</strong></td>
<td>.48</td>
<td>-</td>
</tr>
<tr>
<td><strong>Host country</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Bolivia</strong></td>
<td>.30 (investment incentives may reduce rate to .15)</td>
<td>.30</td>
</tr>
<tr>
<td><strong>Chile</strong></td>
<td>.15, .40</td>
<td>-</td>
</tr>
<tr>
<td><strong>Colombia</strong></td>
<td>.40</td>
<td>.10 to .15 (variable on amount of capital)</td>
</tr>
<tr>
<td><strong>Ecuador</strong></td>
<td>.30</td>
<td>-</td>
</tr>
<tr>
<td><strong>Peru</strong></td>
<td>.20 to .55</td>
<td>-</td>
</tr>
<tr>
<td><strong>Venezuela</strong></td>
<td>.15 to .50 (except oil and mining)</td>
<td>.15 to .50</td>
</tr>
</tbody>
</table>

- \(a\)/ Temporary rate for calendar year 1976 is .18; additional levy of .40 on after-tax profits of resident corporations and limited liability companies.
- \(b\)/ Withholding at .40 plus .11 surcharge. Effective withholding rate .444.

U.S. TAX INCENTIVES

1. Tax incentives for foreign branches of domestic corporations.

Western Hemisphere Trade Corporation deduction (note a)


The WHTC deduction allows a corporation to reduce its U.S. tax rate by 14 percentage points. The reduction is available to a domestic corporation which derives at least 95 percent of its gross income from Western Hemisphere countries (other than the United States) and 90 percent or more of its gross income from the active conduct of trade or business in the Western Hemisphere (outside of the United States). The effective rate of tax on net income if a WHTC is 34 percent. Under the 1976 act, the WHTC tax reduction will be phased out over a 4-year period.

2. Tax incentives for foreign subsidiaries of domestic corporations.

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a/The provision was originally enacted in 1942 during a period of high wartime taxes and generally low taxes in other Western Hemisphere countries. It was aimed at insuring that U.S. corporations did not operate at a disadvantage in competing with foreign corporations within the Western Hemisphere. The goal was to retain U.S. ownership of foreign investment which, if placed in a foreign corporation, might end up being owned by foreign interests. Western Hemisphere country taxes have been substantially increased since 1942, with the result that many U.S. companies which qualify as WHTCs receive little or no benefit from the deduction after taking the foreign tax credit into account. There has been a substantial volume of litigation and administrative difficulty generated by the WHTC deduction. Companies have set transfer prices so as to maximize income derived from sources within the Western Hemisphere. Further, companies have generally been successful in obtaining WHTC treatment for income derived from the sale of goods manufactured outside of the Western Hemisphere by providing that title to the goods sold be passed within the Western Hemisphere.
Dividends from less developed country corporations

The Tax Reform Act of 1976 amends the Internal Revenue Code to provide that dividends received by a qualifying U.S. parent corporation from a controlled less developed country (LDC) subsidiary shall be taxed in the same manner as dividends received from other foreign corporations. This means that for purposes of computing U.S. taxable income, dividends paid by all foreign corporations must be grossed up by the amount of foreign taxes deemed paid with respect to such dividends. The amount of foreign taxes deemed paid is the same proportion of the total taxes paid as the dividend bears to the accumulated after-tax profits of the dividend-paying corporation.

This uniform treatment is effective for taxable years beginning after December 31, 1975. However, the act does not apply to dividends received from an LDC corporation before January 1, 1978, and attributable to earnings and profits accumulated in taxable years beginning before January 1, 1976.

The gross-up requirement can be illustrated as follows:
Assume foreign source earnings of $10,000, foreign tax on such earnings of $4,000, accumulated profits net of foreign tax of $6,000, dividend to the U.S. parent of $1,000, and a U.S. corporate tax rate of 48 percent. Under the gross-up requirement, the combined U.S. and foreign tax liability of the U.S. parent for the repatriated earnings is $800, computed as follows.

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gross profits of subsidiary</td>
<td>$10,000</td>
</tr>
<tr>
<td>Foreign tax</td>
<td>$4,000</td>
</tr>
<tr>
<td>After-tax profits</td>
<td>$6,000</td>
</tr>
<tr>
<td>Dividend paid to parent</td>
<td>$1,000</td>
</tr>
<tr>
<td>U.S. gross income of parent:</td>
<td></td>
</tr>
<tr>
<td>Dividend received</td>
<td>$1,000</td>
</tr>
<tr>
<td>Foreign tax deemed paid</td>
<td></td>
</tr>
<tr>
<td>$4,000 x 1,000 = 667</td>
<td></td>
</tr>
<tr>
<td>U.S. tax (tentative) ($1,667 x 48%)</td>
<td>$800</td>
</tr>
<tr>
<td>Foreign tax credit</td>
<td>667</td>
</tr>
<tr>
<td>U.S. tax liability</td>
<td>$133</td>
</tr>
</tbody>
</table>
Prior to the 1976 act, the combined foreign and U.S. tax liability of the parent company for the repatriated earnings would have been $480 computed as follows.

Gross profits of subsidiary $10,000
Foreign tax 4,000
After tax profits $ 6,000
Dividend paid to parent $ 1,000
U.S. gross income of parent $ 1,000
U.S. tax (tentative) ($1,000 x 48%) $ 480
Foreign tax credit: 4,000 x 1,000 = 400

U.S. tax liability $ 80

Deferral of tax on retained profits

To the extent that foreign corporate taxes are lower than U.S. corporate taxes, the deferral of U.S. tax on foreign subsidiary profits is an incentive to retain foreign source earnings abroad. As shown below, most ANCOM country corporate tax rates on corporate earnings retained in the source country and not remitted to the United States are lower than the 48 percent U.S. corporate tax rate.

<table>
<thead>
<tr>
<th>Country</th>
<th>Percent of corporate tax</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bolivia</td>
<td>.30 (investment incentives may reduce rate to .15)</td>
</tr>
<tr>
<td>Chile</td>
<td>.15, additional levy of .40 on after-tax profits of resident corporations and limited liability companies</td>
</tr>
<tr>
<td>Colombia</td>
<td>.40, plus .10 -1.15 excess profits tax</td>
</tr>
<tr>
<td>Ecuador</td>
<td>.30</td>
</tr>
<tr>
<td>Peru</td>
<td>.20 to .55</td>
</tr>
<tr>
<td>Venezuela</td>
<td>.15 to .50 (except oil and mining)</td>
</tr>
</tbody>
</table>
The deferral advantage does not apply to profits earned by foreign branches of U.S. corporations.

Because the foreign tax credit applies to both the foreign corporation tax and the foreign withholding tax on remitted profits for ANCOM countries, the Treasury would not necessarily recover any tax revenue if deferral were eliminated and retained foreign earnings were taxed on a current basis. The U.S. tax is reduced by the additional foreign tax withheld if the foreign subsidiary distributes the foreign source earnings as dividends instead of reinvesting them abroad. Since the foreign corporate tax rate in ANCOM countries plus the additional withholding tax rate on subsidiary profits remitted to the U.S. parent is in all but one case higher than the 48 percent U.S. rate, U.S. tax recovery under a system of no deferral would be reduced dollar for dollar by remittance and payment of the additional tax withheld. The 20 and 40 percent rates (52 percent effective rate) of Peru illustrates the principle which would apply in the case of all ANCOM countries if the deferral rule were repealed. For this purpose, the computation follows the changes made by the Tax Reform Act of 1976, which means that dividends received from an LDC corporation are taxed in the same manner as dividends received from other foreign corporations.

Example 1: Assuming $100 before-tax earnings, a 52-percent effective foreign tax rate, $0 remitted to the U.S. parent.

<table>
<thead>
<tr>
<th>Gross profits of subsidiary</th>
<th>$100</th>
</tr>
</thead>
<tbody>
<tr>
<td>Foreign tax ($100 x 20%)</td>
<td>$20</td>
</tr>
<tr>
<td>U.S. gross income of parent:</td>
<td></td>
</tr>
<tr>
<td>Dividend deemed received</td>
<td>$80</td>
</tr>
<tr>
<td>Foreign tax deemed paid</td>
<td>20</td>
</tr>
<tr>
<td>U.S. tax (tentative) ($100 x 48%)</td>
<td>$48</td>
</tr>
<tr>
<td>Foreign tax credit</td>
<td>20</td>
</tr>
<tr>
<td>U.S. tax liability</td>
<td>$28</td>
</tr>
</tbody>
</table>
Example 2: Assuming $100 before-tax earnings, a 52-percent effective foreign tax rate, $48 remitted to the U.S. parent.

<table>
<thead>
<tr>
<th>Gross profits of subsidiary</th>
<th>$100</th>
</tr>
</thead>
<tbody>
<tr>
<td>Foreign tax:</td>
<td></td>
</tr>
<tr>
<td>Corporate tax ($100 x 20%)</td>
<td>$20</td>
</tr>
<tr>
<td>Withholding tax ($80 x 40%)</td>
<td>32</td>
</tr>
<tr>
<td></td>
<td>$52</td>
</tr>
<tr>
<td>U.S. gross income of parent:</td>
<td></td>
</tr>
<tr>
<td>Dividend</td>
<td>$48</td>
</tr>
<tr>
<td>Foreign tax deemed paid</td>
<td>52</td>
</tr>
<tr>
<td></td>
<td>$100</td>
</tr>
<tr>
<td>U.S. tax (tentative) ($100 x 48%)</td>
<td>$48</td>
</tr>
<tr>
<td>Foreign tax credit</td>
<td>52</td>
</tr>
<tr>
<td>Excess foreign tax credit</td>
<td>$4</td>
</tr>
<tr>
<td>U.S. tax liability</td>
<td>$0</td>
</tr>
</tbody>
</table>

The same principle would apply if only a percentage of the foreign source earnings is repatriated under a system of no deferral. For example, assuming that 50 percent of such foreign source earnings is repatriated and thus subject to the additional withholding tax, the tax recovery would be reduced by 57 percent [(28-12) / 28] as follows.

Example 3: Assuming $100 before-tax earnings, a 52-percent effective foreign tax rate, $40 remitted to the U.S. parent.

<table>
<thead>
<tr>
<th>Gross profits of subsidiary</th>
<th>$100</th>
</tr>
</thead>
<tbody>
<tr>
<td>Foreign tax:</td>
<td></td>
</tr>
<tr>
<td>Corporate tax ($100 x 20%)</td>
<td>$20</td>
</tr>
<tr>
<td>Withholding tax ($40 x 40%)</td>
<td>16</td>
</tr>
<tr>
<td></td>
<td>$36</td>
</tr>
<tr>
<td>U.S. gross income of parent:</td>
<td></td>
</tr>
<tr>
<td>Dividend received</td>
<td>$40</td>
</tr>
<tr>
<td>Dividend deemed received</td>
<td>24</td>
</tr>
<tr>
<td>Foreign tax deemed paid</td>
<td>36</td>
</tr>
<tr>
<td></td>
<td>$100</td>
</tr>
<tr>
<td>U.S. tax (tentative) ($100 x 48%)</td>
<td>$48</td>
</tr>
<tr>
<td>Foreign tax credit</td>
<td>36</td>
</tr>
<tr>
<td>U.S. tax liability</td>
<td>$12</td>
</tr>
</tbody>
</table>
Unfortunately, the most recent available data on earnings and taxes paid by controlled foreign corporations on a country-by-country basis is for 1962. Without more up-to-date information, it is impossible to determine the current foreign tax liabilities of U.S. direct investment abroad and to determine how the benefits of deferral are presently distributed. Data reported in the Statistics of Income, taken from returns filed with Form 1118 in support of the foreign tax credit for 1962, indicates that earnings derived from sources within the ANCOM countries may generate excess foreign tax credits for distributed earnings.

<table>
<thead>
<tr>
<th>Country</th>
<th>Taxable income from foreign source</th>
<th>Foreign tax paid</th>
<th>U.S. tax credit</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bolivia</td>
<td>$5,866,000</td>
<td>$5,435,000</td>
<td>$2,815,680</td>
</tr>
<tr>
<td>Chile</td>
<td>189,885,000</td>
<td>153,944,000</td>
<td>91,815,800</td>
</tr>
<tr>
<td>Colombia</td>
<td>45,844,000</td>
<td>23,313,000</td>
<td>22,005,120</td>
</tr>
<tr>
<td>Ecuador</td>
<td>4,673,000</td>
<td>1,601,000</td>
<td>2,243,040</td>
</tr>
<tr>
<td>Peru</td>
<td>107,964,000</td>
<td>58,887,000</td>
<td>51,822,720</td>
</tr>
<tr>
<td>Venezuela</td>
<td>655,327,000</td>
<td>398,035,000</td>
<td>314,556,960</td>
</tr>
</tbody>
</table>

It is reasonable to surmise, therefore, that the effect of terminating deferral of U.S. tax on unrepatriated ANCOM source earnings would be to increase the level of repatriation, with no revenue gain to the Treasury.

**ANDEAN COUNTRY TAX INCENTIVES FOR FOREIGN DIRECT INVESTMENT**

Basically, the purpose of the tax incentives offered by a host country is to increase the after-tax rate of return on domestic investment so that it conforms with the international supply price of capital. The gain to the host country equals the total tax paid by the subsidiary (T), minus the difference in the unit real resource cost (including subsidies and the cost of capital) if the product is produced locally with foreign capital (c) and the import cost (i), times the number of units produced by the subsidiary (q):

$$\text{gain} = T - (c-i)q$$
If it is no more costly to import the unit than to manufacture it locally with foreign capital, obviously the gain to the host country through an increased level of domestic investment is $T$.

There is evidence that tax and other investment incentives in the Caribbean and some Latin American countries have encouraged foreign-financed assembly and processing operations to locate in these areas. ("U.S. Trade with the Developing Economies: The Growing Importance of Manufactured Goods," June, 1975. U.S. Department of Commerce.)

Andean country tax incentive provisions and accounting rules are summarized in the two following tables.
**ANCOM Country Taxes on Net Income of U.S. Branches and Subsidiaries
of U.S. Parent Corporation: Tax Holiday Special Incentive Provisions**

<table>
<thead>
<tr>
<th>Country</th>
<th>Tax holiday provisions</th>
<th>Other special investment incentive provisions</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bolivia</td>
<td>10-year tax exemption for new building; 10-year income tax holiday for regional investments. Mining and hydrocarbon industries exempt from 20% income tax. Taxable on royalty income.</td>
<td>Income of oil and mining companies subject to special royalties and concession duties in lieu of income tax. 50% of net corporate profits required to be reinvested in Bolivia. Ceiling of 15% on net profits on foreign direct investment that can be remitted annually; 20% ceiling on annual remittance of original capital investment. 7% penalty on amount by which corporate undistributed profits exceed paid-up capital. Reduced withholding rate for nonresident aliens who perform certain technical, scientific, or cultural services. The Foreign Investors Statute grants tax concessions and customs duties exemptions for new investments which utilize 60% or more of Chilean raw materials or which establish basic industries not in existence in Chile. Annual inflation tax adjustment: (1) net worth increased by amount of increase in cost of living; the increase is not taxed and (2) net value of assets increased by percentage increase in cost of living; the increase is taxed. Reduced tax rate of 20% for mining companies. Tourist hotels: deduction from income equal to 15% of investment. Exporters other than coffee and petroleum: deduction from income equal to 10% of investment. All companies allowed a special 10% tax-free reserve for acquisition of fixed assets. Tax-free reinvestment allowances of up to 5% of net profits if invested in the production of exportable industrial goods or import substitutes. Under the Industrial Development Law, qualifying industries exempt from sales, property, and transfer taxes, and customs duties for varying periods. No exemption from the income tax. Retained corporate profits which are reinvested are taxable at reduced 15% rate. Food processing companies allowed additional deduction from taxable income equal to 10% of production costs. All corporations (domestic and foreign) can invest a percentage of before-tax profits, tax free, in Peru. The percentage varies depending on location and kind of industry. Producers of petroleum byproducts can reinvest tax free 60% to 100% of profits. Allows adjustment to the historical cost of assets, liabilities, income, and expenses recorded in financial statements to reflect changes in the purchasing power of currency. Dividends paid by oil and mining companies exempt from tax. Mining and oil companies granted a tax credit of 6% of new investment, plus 4% of cost of new exploration and a reduction of 0.25% of net income for each 1% increase in income derived from mining and oil. Other companies granted a tax credit of 15% of new investment.</td>
</tr>
<tr>
<td>Chile</td>
<td>Partial tax exemption until 1981 for companies investing in the less-developed provinces of Chile.</td>
<td></td>
</tr>
<tr>
<td>Colombia</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Ecuador</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Peru</td>
<td>Tax exemption for 10 years for production of certain foods and materials.</td>
<td></td>
</tr>
<tr>
<td>Venezuela</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Country</th>
<th>Capital gain income</th>
<th>Depreciation methods</th>
<th>Reinvestment provisions</th>
<th>Licensing arrangements</th>
<th>Section 482-type allocations (note a)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Chile</td>
<td>Taxable at 15% category one rate applicable to ordinary income.</td>
<td>Accelerated and straight-line depreciation. When fixed assets are stated at a valuation amount in excess of cost, income is taxed based on the valuation amount.</td>
<td>No depreciation allowance for mining companies.</td>
<td>Withholding tax reduced to 2% for nonresident who performs technical, scientific, or cultural services in Chile.</td>
<td>Foreign corporation doing business through Bolivian branch taxed on assumed net income: 15% of gross revenue (transportation, international communications, international insurance); 15% of gross revenue (movie distributors).</td>
</tr>
<tr>
<td>Columbia</td>
<td>Capital gains on casual sales of securities except capital gain on real property taxed as a percentage of ordinary basis.</td>
<td>Straight-line depreciation over 50% of cost basis (buildings), 20% (vehicles), 10 years (personal property). Director General of National Taxes may authorize declining balance, double declining balance method.</td>
<td>3-year period for amortization of exploration expenses. Depreciation allowance of 3% of gross value of petroleum extracted with maximum limit of 3% of total net income before depreciation deduction. When decreased by an amount equal to 25% of gross value of crude petroleum. Exploration expenses amortizable over the period of exploitation.</td>
<td>On sale of research and development expenditures: cost basis presumed equal to 3% of sales price. Cost of research and development expenditures amortizable over the greater of period of contract or 5 years. Cost may be reduced by 10% of gross value of crude petroleum.</td>
<td>No carryforward of losses. Outside U.S. income, no carryback.</td>
</tr>
<tr>
<td>Ecuador</td>
<td>Taxed as ordinary income for sales of real property. Tax is reduced by 1% for each year asset held.</td>
<td>Straight-line depreciation over 20 years (buildings) or 10 years (personal property) unless approved by the Director General of National Taxes to use accelerated depreciation or stepped-up basis to reflect revaluation.</td>
<td>No depletion allowance for mining companies.</td>
<td>Withholding tax reduced to 2% for nonresident who performs technical, scientific, or cultural services in Chile.</td>
<td>No carryforward of losses. Outside U.S. income, no carryback.</td>
</tr>
<tr>
<td>Peru</td>
<td>Taxed as ordinary income when realized.</td>
<td>Detailed depreciation rates provided for each class of assets ranging from 3% (buildings), 5% (vehicles), 10% (personal property). When fixed assets are stated at a valuation amount in excess of cost, depreciation charged to income may be based on the valuation amount.</td>
<td>Any &quot;reasonable&quot; method of depreciation is allowable. Amortized depreciation allowable to persons or taxing authorities where the business activity is in the national interest. Unit-of-production method of depreciation specified for oil and mining industry.</td>
<td>No depreciation allowance for mining companies.</td>
<td>No carryforward of losses. Outside U.S. income, no carryback.</td>
</tr>
<tr>
<td>Venezuela</td>
<td>Taxed as ordinary income when realized.</td>
<td>Detailed depreciation rates provided for each class of assets ranging from 3% (buildings), 5% (vehicles), 10% (personal property). When fixed assets are stated at a valuation amount in excess of cost, depreciation charged to income may be based on the valuation amount.</td>
<td>Any &quot;reasonable&quot; method of depreciation is allowable. Amortized depreciation allowable to persons or taxing authorities where the business activity is in the national interest. Unit-of-production method of depreciation specified for oil and mining industry.</td>
<td>No depreciation allowance for mining companies.</td>
<td>No carryforward of losses. Outside U.S. income, no carryback.</td>
</tr>
</tbody>
</table>

* Under Section 482 of the Internal Revenue Code, the Commissioner has authority to redistribute the income among related taxpayers such as parent and subsidiary corporation, Stockholders and controlled corporation if such reallocation is necessary to properly reflect the income generated by the separate activities of the related taxpayers or to prevent tax evasion. Reinvestment provisions are contained in the tax laws of most foreign countries.

**Source:** Corporate Taxation in Latin America: International bureau of fiscal documentation, November 1975.

**Appendix VIII**

**Acquisition Costs on Net Income on U.S. Branches and Subsidiaries**

<table>
<thead>
<tr>
<th>Type of Foreign Business</th>
<th>Method of Determination</th>
<th>Percentage Limitations</th>
<th>Percentage Limitations on Income from Other Activities</th>
</tr>
</thead>
<tbody>
<tr>
<td>branches</td>
<td>As U.S. branches</td>
<td>30%</td>
<td>Not applicable</td>
</tr>
<tr>
<td>subsidiaries</td>
<td>As U.S. subsidiaries</td>
<td>30%</td>
<td>Not applicable</td>
</tr>
</tbody>
</table>
December 2, 1976

Mr. J. K. Fasick  
Director  
International Division  
U.S. General Accounting Office  
Washington, D. C. 20548

Dear Mr. Fasick:

I am replying to your letter of October 15, 1976, which forwarded copies of the draft report: "A Study of US Direct Investment in the Andean Common Market."

The enclosed comments were prepared by the Deputy Assistant Secretary for Inter-American Affairs.

The several meetings between GAO staff members responsible for preparing this study and State Department officers concerned with Andean Pact affairs permitted an informal discussion on aspects of the study of concern to us. We found these meetings helpful in relating overall US developmental policy objectives in Latin America to the Andean context. We hope that our views regarding Latin American attitudes toward foreign investment enabled the GAO staff to obtain a better perspective of the Andean area.

The Department believes the GAO study serves to give additional recognition to the Andean Pact as an important developing area for US interests. The study projects a balanced view of factors influencing American direct investment in Andean countries and clearly perceives that host government investment controls, per se, do not necessarily deter such investment. At the same time recognition is given to the desire of Andean governments to insure that foreign investment assists the developmental process.

We appreciate having had the opportunity to review and comment on the draft report. If I may be of further assistance, I trust you will let me know.

Sincerely,

Daniel L. Williamson  
Deputy Assistant Secretary for Budget and Finance

Enclosure: As stated

GAO note: Changes have been made in the body of the report where appropriate and the Department's comments have not been included herein.
Mr. Henry Eschwege
Director, Community and Economic
Development Division
U. S. General Accounting Office
Washington, D. C. 20548

Dear Mr. Eschwege:

This is in response to a revised version of the draft report entitled "U. S. Direct Investment In South America's Andean Common Market."

We have reviewed the enclosed comments of the Deputy Assistant Secretary for International Economic Policy and Research and believe they are responsive to the matters discussed in the report.

Sincerely,

Guy W. Chamberlin, Jr.
Acting Assistant Secretary for Administration

Enclosure
Mr. Henry Eschwege  
Director  
Community and Economic Development  
Division  
U.S. General Accounting Office  
Washington, D.C. 20548  

Dear Mr. Eschwege:

The January 1977 GAO draft of the study entitled "U.S. Direct Investment in South America's Andean Common Market" is an informative, comprehensive, and interesting commentary on the U.S. investment position in six representative less-developed countries. The modifications and additions made by GAO as a result of agency comments on an earlier draft are especially important, particularly the evaluations of the impact of Chile's withdrawal from the Pact and the effect of LDCs' laws and policies on their respective investment climates.

We agree that it would be highly useful for the Secretary of Commerce, under authority of the International Investment Survey Act of 1976, to gather data that may enable us to determine the extent of the relationship between U.S. direct investment abroad and the availability of raw materials resources to the United States. If our studies indicate that a strong relationship does indeed exist, the Department of Commerce would be pleased to give consideration to advising the Administration and the Congress of procedures to develop cooperative efforts between the U.S. Government and U.S. firms in order to assure U.S. access to raw materials. It may be that while U.S. access to raw materials via direct investment abroad is declining, joint ventures and a variety of contractual arrangements may serve as substitute techniques to assure adequate supplies of raw materials. In short, we believe such a study and analysis would be extremely helpful in the establishment of U.S. policies vis-a-vis energy and non-energy raw materials.
Thank you for the opportunity to review and comment on your draft report. I appreciate the consideration you have given our previous comments.

Sincerely,

S. Stanley Katz
Deputy Assistant Secretary for International Economic Policy and Research

GAO note: Changes have been made in the body of the report where appropriate and the Department's earlier comments have not been included herein.