BARGAINING POWER AND STRATEGY IN THE FOREIGN INVESTMENT PROCESS: A CURRENT ANDEAN CODE ANALYSIS

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I. INTRODUCTION

Significant changes in the global economic balance of power have taken place during the last several years. Japan and the Western European nations have made substantial progress in achieving technological equality with the United States,¹ and many developing countries have taken or are now taking steps to improve their bargaining position relative to the developed countries.²

In addition, the past few decades have produced an enormous growth in the amount of direct equity investment made by companies in countries other than their home country.³ In order to maintain control over their domestic economies, developing country governments have come to rely on foreign investment laws, tariffs, quotas, and other means of regulating foreign economic influence.⁴

In 1970, the countries of the Andean Common Market (the Andean Pact or ANCOM),⁵ adopted uniform foreign investment


³. The great majority of such investment has been undertaken by the so-called "multinational," "transnational," or "international enterprises." The transnational enterprise, though difficult to define precisely, can be generally characterized as a parent corporation which maintains a substantial amount of equity interest and/or control over a "large cluster of corporations of various nationalities." See R. VERNON, SOVEREIGNTY AT BAY: THE MULTINATIONAL SPREAD OF U.S. ENTERPRISES 4-18 (1971) [hereinafter cited as VERNON, SOVEREIGNTY]. As of 1967, U.S. parent corporations were estimated to be managing about $110 billion of overseas assets through their positions of control. Id. at 18.

⁴. Foreign investment laws are now in force or under consideration in nearly every country in the world. For the investing conditions in a given country see Investing, Licensing, and Trading Conditions Abroad (updated monthly).

⁵. The Andean Common Market is made up of six nations on the western side of Latin America: Bolivia, Chile, Colombia, Ecuador, Peru, and Venezuela. The legal instrument of its establishment is the Agreement on Andean Subregional Integration, commonly known as the Treaty of Cartagena, adopted in Colombia in 1969. For text of the Treaty in English see 8 INT'L LEGAL MAT'LS 910 (1969). For a description and discussion of the Treaty provisions,
regulations. The Andean Foreign Investment Code, as Decision 24 of the Andean Commission is called, regulates both the treatment of foreign capital entering or within ANCOM, and related agreements on the transfer of technology, patents, licenses, and royalties. The member countries of ANCOM were required by Decision 24 to implement this Code as domestic legislation following its adoption by the Andean Commission.

The governments of the ANCOM members were motivated by both common and individual interests when they adopted the Andean Code. Among these were the desire to achieve a reduction in foreign economic influence, and to be able to plan more efficiently a regional industrial structure. This was to be done in a way which

including a complete bibliography of articles concerning them see Riesenfeld, Legal Systems of Regional Economic Integration, 22 Am. J. Comp. L. 415, 436-43 (1974). The Andean Common Market is often referred to as a "subregional common market," since it exists within the larger framework of the Latin American Free Trade Area (LAFTA), composed of eleven Latin American nations. LAFTA was established in 1969 by the Treaty of Montevideo. Treaty Establishing a Free Trade Area and Instituting the Latin American Free Trade Association (Montevideo Treaty), Feb. 18, 1960, 30 U.N. ECOSOC Supp. 4, at 32, U.N. Doc. E/3333, E/CN.12/AC.45/13/Rev. 1 (1960); Inter-American Institute of International Legal Studies, Instruments Relating to the Economic Integration of Latin America 207 (1968). As its name implies, the purpose of the organization is to establish a free trade zone among the member nations. For a discussion of LAFTA see Riesenfeld at 431-36.

6. The Commission is the Supreme Organ of the Treaty of Cartegena and is instructed per Chapter I, section A, of the Treaty to "empress its will" in the form of "Decisions." The Andean Foreign Investment Code is one in a series of such Decisions relating to ANCOM. For the most recent text of Decision 24 (as amended by Decision 37 of June 24, 1971, and Decision 37-A of July 17, 1971), see 11 Int'l Legal Mat'ls 126 (1972).

7. Decision 24 was promulgated by the Commission pursuant to Articles 26 and 27 of the Treaty of Cartegena. Article 27 provides, inter alia, for "a common system for treatment of foreign capital and likewise, systems for trademarks, patents, licenses, and royalties," 8 Int'l Legal Mat'ls 910, 917 (1969).

8. All Decisions of the Commission require subsequent internal ratification by the member countries. The problems surrounding internal implementation of the Code are discussed in Section III of the text.

9. This desire is reflected in the Introduction of the Code which reads:

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 the 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.

11 Int'l Legal Mat'ls 126-27 (1972).

10. Among the goals of ANCOM is to rationally allocate industrial responsibility among the member countries through the "sectorial programs of industrial development" (SPID) called for in Chapter 4 of the Treaty of Cartegena. The first such program has now been established for the metalworking industry, and a similar program for the petrochemicals industry has just been completed. See Furnish & Atkin, The Andean Group's Program for
would give no individual member country a significant economic advantage over the others.\textsuperscript{11}

Since the adoption of the Andean Foreign Investment Code, there have been important changes in the political and economic situations of the member countries (for example, the quadrupling of oil prices which has made Venezuela a new economic power in the Western Hemisphere), and there have been several important developments in the Code's local implementation. This Article is designed to apprise the practitioner concerned with Latin America of progress in the implementation of the Andean Code and related regulations in the six ANCOM countries, and to discuss implications for the investment lawyer. It examines the progress of the Andean Pact's efforts in the field of foreign investment regulation in terms of bargaining theories previously used solely by economists, political scientists, and military strategists, but which have recently begun to receive attention from international lawyers.\textsuperscript{12} It is the premise of this Article that both international lawyers and government officials should begin to see the forces which influence the foreign investment process in a general theoretical framework in order to fully understand and perhaps better control these forces.

\textbf{II. BARGAINING THEORY AND FOREIGN DIRECT INVESTMENT IN DEVELOPING COUNTRIES: A DYNAMIC PROCESS}

A. The Changing Economic Power Relationship

1. As Defined by Economists

Bargaining theory is an analytical framework developed to describe the process of continuous negotiation which characterizes the relationship between foreign direct investors and host governments in developing countries. The bargaining theory discussed by international economists such as Raymond Vernon\textsuperscript{13} and Charles Kindle-
berger emphasizes the relative economic power at the disposal of participants. As the economic power relationship between a foreign direct investor and a host country government changes, the investment conditions which the investor must accept also change. This relative economic power, reflected in bargaining strength, depends on a variety of factors, which are discussed below.

2. FACTORS WHICH DETERMINE THE BARGAINING POWER OF THE FOREIGN DIRECT INVESTOR

a. Economic Resources

The great majority of foreign direct investments in both developed and developing countries are undertaken by multinational or transnational enterprises (TNE's). There are four major economic resources which are generally attributed to TNE's. These resources are investment capital or access to capital, technology, managerial expertise, and international markets. The relative economic

Countries: their role in trade and development, U.N. Doc. TD/B/399 (1972) [hereinafter cited as Vernon, Restrictive Practices].


15. In developing countries, private investment capital is a critical resource. TNE's can finance an investment project in developing countries either by using their own financial reserves or by borrowing from financial institutions. In terms of borrowing capability, the TNE has the advantage over the local entrepreneurs in developing countries of better credit standing based on the TNE's proven performance and substantial equity holdings. Public international lending institutions, such as the Inter-American Development Bank, make loans almost exclusively for developmental projects such as water companies and other infrastructure industries, instead of to private industrial projects.

16. Technological capabilities are perhaps the most important single asset of the TNE. The Andean Pact is focusing much of its attention on acquiring technological resources. U.S. based TNE's, and to a lesser extent those of Japan and Western Europe, lead the world in technological innovation. At the high end of the technology spectrum are the advanced computer and semi-conductor industries in which the U.S. position is very strong. Technology becomes more widely held when we proceed down the spectrum to the machine tool and soft-drink industries, in which the requisite technology for establishing a plant may be obtained from a wide variety of sources.

17. When the TNE establishes a subsidiary in a foreign country, it must also provide trained managers to oversee operations and to coordinate the activities of the subsidiary with the other international operations of the firm. The TNE has typically established a highly coordinated and effective system of internal management as the result of previous experience in other countries. As time passes, the subsidiary trains local personnel to take over the management function so that the firm can blend into the local environment. Thus the subsidiary provides the host country with a new pool of local managerial talent. See Vernon, SOVEREIGNTY, supra note 3, at 171, 184.

18. Access to international markets is extremely important both in the extractive and manufacturing industries. The giant extractive industry TNE's provide a vital link between
bargaining power which a foreign investor is able to marshal from these resources depends upon the degree of control which it is able to maintain over these resources and upon their importance to the host country. If the capital, technology, management, and market access required for an investment project are available from a wide variety of sources, then the host country can award an investment project to the investor who offers the most generous terms. On the other hand, if the required technology is scarce, or if the investment project requires a high initial infusion of capital—as in the extractive industries—then the foreign investor can demand more generous terms because the number of suppliers is limited.

b. Motivation

If there is a compelling reason behind the TNE’s decision to invest in a particular country or region, then it will be more willing to accept the investment terms which are offered by the host country government. If the investor’s motivation is weak, that is, if the investor is more or less indifferent as to whether the investment should be undertaken at all, then he can demand better terms for investing.

The motivations behind the decision to invest in an extractive industry project may be comparatively simple. The TNE may want to assure a supply of a natural resource, for example petroleum, copper, or cobalt. The TNE may want both to obtain the supply at the cheapest price—that is, from the original source—and to deny to competitors any access to the source of supply. In addition, the resource may be available in only a limited number of geographical locations so that the investor does not have a variety of options from which to choose.

In the manufacturing industries, the situation is far more complex, and numerous theories have been developed to explain the motivations of foreign investors. Among the factors which are thought to give rise to a manufacturing investor’s decision to go abroad are: (1) as the technology embodied in a product becomes widely held it is necessary to move production into a foreign market the extractive phase in the developing country and the processing and marketing phases in the developed countries. The expenses of acquiring the shipping capabilities to transport raw materials between countries and of building refineries and mills are enormous. In addition, a direct link between extraction and end user provides an assured market for the resource. Finally, in the manufacture of consumer and intermediate goods, the TNE provides an international system of distribution and marketing. This system is essential to the exporting producer.
to reduce costs and effectively compete in the foreign market; 19 (2) TNE's fear losing a foreign market to a competitor and follow their competition into a region in order to protect themselves; 20 (3) earnings are higher in foreign markets than in domestic ones, for example, in the United States; 21 (4) TNE's try to distribute the risk of loss either through business 22 or currency 23 fluctuations by investing in several regions; and (5) it is the nature of the capitalist economic system to impose itself on other systems or to risk eventual collapse. 24

This suggests the number of motivation scenarios which have been developed. Foreign direct investors approach developing countries for a variety of reasons and the factors which motivate the TNE must be taken into account when analyzing relative bargaining power. For example, if a TNE is seeking to establish a plant because its competitors have already done so and it fears losing the foreign

19. The product life cycle model, developed by Raymond Vernon of the Harvard Business School is probably the most widely accepted explanation for the behavior of TNE's in expanding abroad. Briefly, this model suggests that: (1) technological innovation occurs in the developed countries wherein the firm which develops the technology maintains a temporary monopoly over production and distribution of the product which embodies it; (2) at this initial point, the company faces little or no competition and can afford to produce the product where it is developed, and export it to foreign markets; (3) as time passes, the technology disperses (it is copied) and many producers enter the market—price competition ensues; (4) because labor inputs are cheaper abroad and because transportation and tariff costs raise prices in the foreign market, the producer goes abroad to lower the production cost and selling price of the product both for local consumption and export; (5) finally, local competitors enter the market with competitive advantages and the foreign investor introduces a new product. See Vernon, Sovereignty, supra note 3, at 65-106.

20. The oligopolistic reaction model of foreign direct investment motivation stresses the defensive character of foreign investment and attempts to explain why TNE's follow each other into foreign markets in closely ordered groups. Essentially, firms are taking out a form of "risk insurance" against losing a market to their TNE competitors. For an elaborate empirical study which supports the oligopolistic reaction model see F. Knickerbocker, Oligopolistic Reaction and Multinational Enterprise (1973).

21. TNE's have historically reported higher earnings from their overseas subsidiaries than from their domestic operations. In 1974, return on equity of 163 companies surveyed showed that on the average, U.S. firms obtained a domestic profitability of 11.9 percent (down from 12.4 percent in 1973), while foreign profitability stood at 17.2 percent (down from 17.8 percent in 1973). See What Happened in 1974 to International Firms' Profitability, Business International, Aug. 8, 1975, at 249-50.

24. From Lenin onward, there have been those who suggest that TNE's are but the capitalists' way of implanting their economic system abroad and, more or less, condemning the poor of developing countries to lives of poverty. See V. Lenin, Imperialism, The Highest Stage of Capitalism: A Popular Outline (1969); H. Magdoff, The Age of Imperialism: The Economics of U.S. Foreign Policy (1969); J. Barne & R. Muller, Global Reach (1974).
market to its competitors, then its bargaining strength relative to the host country government will be weaker because it is not indifferent to whether or not an agreement is reached.

c. Recourse to Law or Diplomatic Intervention

The transnational enterprise is a private party bargaining with a sovereign, the host country government. The host country government, in its sovereign capacity, has the power to manipulate its domestic law and thus to change its legal relationship with the foreign investor. If the host government decides to change the terms of an investment agreement or to expropriate the property of a foreign investor, the foreign investor has four basic alternatives: (1) to challenge the action in local courts; (2) to rely on international law and to seek enforcement in arbitration, foreign or international courts; (3) to request diplomatic intervention by its home country government; or (4) to threaten to withdraw its investment.

While the foreign investor may be able to obtain some help from any or all of these sources, he is nevertheless at a decided disadvantage relative to the host country government.

3. FACTORS WHICH DETERMINE THE BARGAINING POWER OF DEVELOPING HOST COUNTRIES

a. Economic Resources

The economic bargaining power of a developing host country depends on a variety of factors. Among these are: the value of a natural resource(s) which the TNE is seeking to exploit; the geographical location of, and access to, the country and its resource(s); the availability of the resource(s) from other countries (and under what conditions); the stage of the country's economic development, that is, the structure of its capital market and the

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25. This of course does not hold true for state-owned enterprises.
26. Obviously, the sine qua non for bargaining with an extractive industry producer is the possession of a mineral resource. The more scarce and necessary the resource is in world markets, and the higher its selling price, the better is the bargaining position of the country. Thus, cartels attempt to create conditions of artificial scarcity.
27. If a TNE faces high initial costs in developing a transportation infrastructure to reach remote areas, it is going to demand a return which justifies its initial costs. Likewise, countries which lack direct sea access present potentially high transportation costs.
28. A host country can make demands only to the extent that potential investors cannot obtain the resources on better terms in other countries. Another function of the cartel is to stop competition among suppliers by establishing uniform terms of supply.
29. A country with a well developed capital market can demand equity participation for
income level of its inhabitants;\textsuperscript{30} the size of its consumer market;\textsuperscript{31} the condition of the country’s labor market;\textsuperscript{32} the investment terms being offered by other countries (with similar resources);\textsuperscript{33} and whether or not foreign investors have already established operations in its territory.\textsuperscript{34}

As a general rule, the more valuable the resources of a host country and the greater the degree of monopoly control which the country maintains over them, the stronger the country’s economic bargaining position relative to foreign direct investors.

\textit{b. The Development Needs of the Developing Countries and the Value of Foreign Direct Investment: Motivation}

If the development planners of a country consider that foreign direct investment plays a positive role in the development process, then they will seek to attract investors by offering reasonable or generous investment terms. They will also be more likely to “play fairly” with investors in order to maintain an attractive image.\textsuperscript{35} On the other hand, if development planners take a negative view of foreign direct investment or are indifferent as to whether foreign investors come or go, then there is no need to maintain an attractive investment climate or to be cautious or reasonable in negotiations. In this respect, the bargaining position of the host country government is strengthened if it takes a negative or indifferent view towards foreign direct investment.

There is nothing close to unanimity of opinion concerning the local investors or purchase turnkey factories, relying on foreign investors only for the supply of technology and planning expertise.

\textsuperscript{30} The attractiveness of a consumer market depends on a number of factors such as population, income, electricity, and cement production, cars in use, etc. For a typical analysis of consumer market strength see \textit{Business Latin America}, Dec. 25, 1974, at 411.

\textsuperscript{31} Id.

\textsuperscript{32} The wage rates which must be paid to employees and the availability of skilled manpower which reduces training time and cost are important considerations for investors. It has been the author’s experience that among the reasons which TNE’s cite for not being more active in the developing African countries is the lack of skilled or semi-skilled labor.

\textsuperscript{33} Again, in most cases countries can make demands up to the point where it becomes more economical for investors to move elsewhere.

\textsuperscript{34} If a TNE’s competitors have already established themselves in a market, the host government can use their presence as leverage vis-à-vis newcomers. See F. Knickerbocker, \textit{supra} note 20, at 197-98.

\textsuperscript{35} A current example of a country which believes that foreign direct investment is important to its development aspirations is Egypt, which is trying to promote an investment “free zone” and to achieve some sort of stability vis-à-vis neighboring Israel. See 13 Int’l. Legal Mat’ls 1500 (1974).
value of foreign direct investment in the development process and the literature on the subject is extensive. The positive view of foreign direct investment and its impact on the development process is that it develops the industrial or extractive capabilities of a country and provides export earnings and import substitution at the least relative economic cost to the host country. The arguments against foreign direct investment are both economic and socio-political, and reflect the concern that nation-states and their citizens might lose control over their own economies and destinies.

c. Sovereign Authority

The power of sovereign governments to enact or change legislation within their domestic territories gives the developing host country government a powerful bargaining advantage over private foreign direct investors. While international law may provide an investor with legal remedies in the event of an investment dispute, these

38. Some of the negative economic arguments are that TNE's: (1) tend to export more capital than they bring into a host country as new investment; (2) by acting as the supplier of technology tend to reduce domestic incentive towards pursuing indigenous research and development; (3) use foreign managers to run local firms, thereby discouraging the development of local entrepreneurial talent; (4) pay higher wages than domestic enterprises and foster socio-economic stratification; and (5) have easier access to local credit and therefore deprive local investors of access to domestic savings. See Díaz-Alejandro, Direct Foreign Investment in Latin America, in THE INTERNATIONAL CORPORATION, supra note 23, at 319.
39. The negative view of foreign direct investment is not confined to any particular geographical area, range of the political spectrum, level of economic development, or class of society. One has only to look to the U.S. Congress for examples of xenophobic legislation to curtail such foreign investment. The Dent-Gaydos Bill, H.R. 8951, 93d Cong., 1st Sess. (1973) introduced on June 25, 1973, "to amend the Securities and [sic] Exchange Act of 1934 to restrict persons who are not citizens of the United States from acquiring . . . more than 5 percentum of the voting securities of any issue whose securities are registered under such act . . .." See Note, The Rising Tide of Reserve Flow, 72 MICH. L. REV. 551, 553 (1974). Regarding the fear of foreign economic domination outside the United States, for Latin America, see Díaz-Alejandro, supra note 38, at 329-32; for Europe, see J. SERVAN-SCHRIEBER, THE AMERICAN CHALLENGE (1968); for Canada, see Rotstein, Shedding Innocence and Dogma, 1973 INTERNATIONAL PERSPECTIVES 12; see generally H. STEPHENSON, THE COMING CLASH: THE IMPACT OF MULTINATIONAL CORPORATIONS ON NATIONAL STATES (1973).
principles are neither so universally recognized nor so capable of application and enforcement as to provide investors with effective means of challenging the decisions of host country governments.41 The Report of the Group of Eminent Persons to Study the Impact of Multinational Corporations on the Development Process and on International Relations42 states, in fact, that "developing countries have, of course, the power through legislation, to modify the terms of agreements."43

B. The Role of Strategy in the Bargaining Process

1. The Relationship between Bargaining Power and Strategy

Although the economic power relationship between a host country and a foreign investor may determine the terms of an investment agreement, and a change in this power relationship may result in the demand for a change in the terms of this agreement, there is often no one single set of terms which may be acceptable to both parties. Bargaining strategy, which is more widely discussed by political44 and military45 scientists than by economists, is employed to achieve the most advantageous outcome within the range of mutually acceptable outcomes.

2. The Use of Strategy by Host Government and Foreign Investor

Both a developing host country government and a foreign direct investor may recognize that they are better off to reach some investment agreement than to reach none at all.46 The strategy objective

41. This is not to imply that foreign governments do not recognize the principle of compensation in the event of expropriation. While compensation is not always "prompt, adequate, and effective," it is generally paid in one form or another. However, in situations which fall short of expropriation, such as the requiring of local equity participation, the imposition of new taxes, changes in royalty arrangements, etc., foreign investors, because of the commitments which are already sunk into an investment, usually find themselves in a take it or leave it situation.

42. See Impact Report, supra note 36, at 38.

43. Id. The Report also suggests that provisions for review of various clauses of investment agreements "after suitable intervals" could be useful under the same circumstances. For the reaction of the U.S. Government to the Report see State Department, The Views of the United States Government Concerning the Report of the Group of Eminent Persons on "The Impact of Multinational Corporations on Development and International Relations" (1975).


46. To illustrate, when the developing country government believes that economic reali-
for the foreign direct investor is to obtain the most attractive investment terms from the host government without demanding so much as to cause the investment to be disapproved or confiscated. The strategy objective for the host government is to obtain the largest possible share of the benefits of the investment without losing the investment and its benefits altogether.

An example of a bargaining tactic is to establish commitment to a "principle." By publicly announcing adherence to such a principle, a government or investor places its credibility and reputation on the line in a bargaining situation. A government can announce that, from a given date forward, it will no longer permit investors to maintain more than 49 percent ownership of an investment. With its credibility riding on the "principle of local majority ownership," the government enters negotiations in a position from which it cannot back down without damaging its credibility. The government has publicly given up its option to make a concession and the investor is forced to adjust his bargaining strategy to the established set of rules.

C. Conclusion

Relationships between foreign direct investors and developing
host country governments are not static. On the contrary, as the bargaining power of the host country government increases, the terms on which foreign direct investments are treated are also subject to change.

This is not necessarily a passive process. Countries can, individually or collectively, take action to increase their bargaining power relative to foreign direct investors; theoretically, foreign direct investors can do the same. Next, we will examine the steps which the countries of the Andean Common Market have taken to increase their bargaining power relative to foreign direct investors, and will attempt to identify the effects and the problems which this action has created for both the ANCOM countries and foreign direct investors.

III. THE ANDEAN FOREIGN INVESTMENT CODE: ITS STRUCTURE AND EFFECT ON FOREIGN DIRECT INVESTORS

The system of regional economic integration created by ANCOM both increases the attractiveness of the member countries to foreign direct investors and increases the bargaining power of the member countries relative to these investors. The enactment of the Andean Foreign Investment Code and its subsequent imple-
mentation in the six member countries represents a new trend in the developing countries towards the treatment of transnational enterprises\(^{52}\) and, if successful, may become a model for future economic development worldwide.\(^{53}\) Cooperation, as the Organization of Petroleum Exporting Countries has demonstrated, can bring about radical economic changes.\(^{54}\)

While the Andean Code provides minimum standards for the treatment of foreign direct investors in each of the ANCOM members,\(^{55}\) the process of domestic implementation\(^{56}\) and enforcement\(^{57}\) has been uneven. This reflects the fact that the attitude towards foreign direct investment embodied in the Code is more consistent with the internal policies and economic needs of some of the member countries—such as Venezuela and Peru—than it is with the policies and needs of others—such as Bolivia and Chile. Herein lies one of the major difficulties of both the ANCOM compact and other cooperative international arrangements:\(^{58}\) nations tend to identify

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52. See text accompanying note 6 supra.

53. The Andean Code is cited with praise in the United Nations report Impact of Multinational Corporations on Development and on International Relations, and several of its major provisions are suggested as means of changing the role of foreign investors in developing countries. See Impact Report, supra note 36, at 59-62.

54. See Section III.D. of the text.

55. Article 33 of the Andean Code provides that:
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.

56. In Bolivia the text of the Andean Code was established as a part of national law through Decree Law 9788, issued June 30, 1971. In Chile, the Andean Code was ratified by Decree Law 482 issued by S. Allende. Decree Law 746, reaffirming Chile's adherence to the Code following a major confrontation over it with other ANCOM members, was issued in November 1974. Although the Code was initially ratified in Colombia by Presidential Decree 1299 and Regulation D2153 issued on July 3, 1971, this Decree was declared unconstitutional by the Colombian Supreme Court. After the Colombian Congress gave the President authority to ratify the Code, it was implemented by Decree Law 1900 on September 15, 1973. Ecuador ratified the Code by Supreme Decree 974 on June 30, 1971. In Peru, the Andean Code was ratified by Decree Laws 18900 of June 30, 1971, and 18999 of October 18, 1971. Venezuela, which ratified its entry into ANCOM and its acceptance of the Andean Code in September of 1973, was accepted for ANCOM membership and had the Code effectively ratified on January 1, 1974. Implementation of the Andean Foreign Investment Code, State Department memorandum, ARA, June 11, 1975.

57. See Section III.B. of the text.

58. The controversies in the European Economic Community regarding the flow of farm products is a good example of this. England, for example, has been reluctant to permit its agricultural sector to face competition from other EEC members and has often accused other members of "dumping" their surplus produce on English markets.
with and to pursue their individual interests more forcefully than they do their interests in international cooperation.59

The provisions of the Andean Code can be roughly divided into three major categories: (1) those concerning equity ownership and control; (2) those regulating the business operations of firms; and (3) those relating to the transfer of technology.

A. Provisions Relating to Equity Ownership and Control

1. THE DIVESTMENT REQUIREMENT

Foreign-owned and controlled enterprises, other than those which fall into either of two exempted categories, are required gradually to divest themselves of majority ownership and control over a 15 or 20 year period following entry into ANCOM.60 Foreign-owned enterprises which were present in ANCOM countries before the enactment and implementation of the Code are required to declare their intention to divest within three years following the date of the Code’s implementation,62 if they want their products to enjoy duty-

59. This is for the most part due to the fact that governments are more accountable to their constituents than they are to the international communities.

60. Foreign enterprises are required to transform into so-called “mixed-enterprises.” Mixed enterprises are made up of between 51 and 80 percent local ownership and control over firm decision-making must be in the hands of local (or “national”) investors. National authorities must approve the control arrangements. Decision 47 of the Andean Commission provides that a “mixed enterprise” may also be one in which at least 30 percent ownership and effective control is in the hands of the State. See Decision 47, 10 DERECHO DE LA INTEGRACIÓN 197 (1972).

61. A transformation timetable is provided in Article 30. Article 31 contains certain provisions which must be stipulated in a transformation agreement. The typical transformation timetable requires that 15 percent of stock, assets, or rights must be placed on sale for national investors at the time of entry into ANCOM (except in Bolivia and Ecuador, where the Code provides that for an initial three-year period foreign investors may maintain 100 percent ownership). Within one-third of the transformation period—15 years in Chile, Colombia, Peru, and Venezuela—30 percent of ownership must be in local hands. Within two-thirds of the period, 45 percent must be so situated, and before the date of completion at least 51 percent ownership and effective control must be maintained by national investors (for Bolivia and Ecuador the transformation timetables are somewhat different). Decision 24, 11 INT’L LEGAL MAT’LS 126, 136-37 (1972). While the transformation agreement registered with the host government must contain a system which insures the sale of ownership rights to local investors, there are some difficulties inherent in this requirement. See text accompanying notes 117-22 infra.

62. The Code, as we have seen, was implemented at different times in the various member countries. Therefore, the three-year limit on declaring an intention to divest is different for the various countries. In addition, both Bolivia and Ecuador have declared that, because of their least developed status, their timetables will not be started earlier than the last of the other members. From a reading of Venezuela’s implementing Decrees, it appears that this date would be January 1, 1977.
free status within the common market. Subsequent to the enactment of the Code, the Andean Commission has ruled that companies existing in ANCOM prior to the Code may declare their intention to divest after the three-year deadline; but when this intention is declared, the company must meet the transformation percentages in force at that time.\(^{63}\)

Foreign-owned companies are required to register the value of their investment with the office of the competent authority in the host country.\(^{64}\) According to the Code, the value of an investment may include financial capital, plant, machinery, or equipment,\(^{65}\) but it may not include intangible or technological contributions such as patents, licenses, or trademarks.\(^{66}\) The valuation which is agreed upon with the competent authority is of great importance to the investor, not only in determining the amount for which the enterprise can be sold to local investors,\(^{67}\) but in calculating, as well, the amount of profits which can be annually remitted abroad or reinvested.\(^{68}\) Because the authorities of the individual member countries are responsible for concluding the valuation agreement with the individual investor, the negotiations for an agreed valuation provide a degree of flexibility which the parties can use to reconcile their interests.

2. EXEMPTIONS FROM THE DIVESTMENT REQUIREMENT

There are two major categories of enterprises which are exempt from the divestment requirement described above. The first concerns foreign enterprises in the extractive industries, or the so-called "basic products" sector.\(^{69}\) The individual member countries are permitted to regulate firms in the basic products sector in any way they

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63. See Ancom Balks at Sectorial Plans but Rules on Fadeout, Patents, BUSINESS LATIN AMERICA, June 12, 1974, at 186.
64. Decision 24, art. 5, 11 INT'L LEGAL MAT'LS 126, 130 (1972).
65. Decision 24, art. 1, id. at 128.
66. Decision 24, art. 21, id. at 134. Intangible technological contributions, although not defined in the body of the Code, are referred to in Annex 1. In addition, implementing legislation such as that of Venezuela makes it clear that patents, trademarks, technical services contracts, and the like cannot be included in the valuation. See Decree 63, art. 59, 13 INT'L LEGAL MAT'LS 1220, 1231 (1974).
67. See text accompanying notes 117-22 infra.
68. See Section III.B. of the text.
69. The basic products sector is defined to include "primary activities of exploration and exploitation of minerals of any kind, including liquid and gaseous hydrocarbons, gas pipelines, oil pipelines, and exploitation of forests." Decision 24, art. 40, 11 INT'L LEGAL MAT'LS 126, 135 (1972).
see fit.\textsuperscript{70} While this exemption reflects the fact that uniform regulation of the extractive industries might present difficult problems for ANCOM because of the uneven distribution of mineral resources and unequal development of the extractive industries sectors,\textsuperscript{71} exemption from ANCOM regulation cannot be interpreted as a boon for investors.\textsuperscript{72} Recent events in Venezuela provide witness to this fact.\textsuperscript{73}

There are other groups of activities for which the Andean Code provides special treatment, but the individual member governments may provide exemption from this treatment, and control TNE’s by national regulations that they consider appropriate.\textsuperscript{74} The Code provides that no new foreign direct investments may be made in the “public services” sector,\textsuperscript{75} in insurance, commercial banking, and other financial institutions,\textsuperscript{76} or in domestic transportation, advertising, radio, newspapers, magazines, or other enterprises related to domestic marketing.\textsuperscript{77} In the public services sector, existing firms may continue to operate and may make new investments which are necessary for efficient operation. Foreign banks\textsuperscript{78} may continue to operate, but they must cease receiving local deposits within three years of the Code’s entry into force unless they agree to convert into “national” enterprises. The enterprises in the domestic marketing activities mentioned must convert into national enterprises within three years.

\textsuperscript{70} Decision 24, art. 44, id. at 140. The exemption for the basic products sector includes an exemption from the profit remittance ceiling.

\textsuperscript{71} For example, in regards to the unequal distribution of resources, Chile, as one of the world’s leading exporters of copper, would be extremely reluctant to have this sector of its economy governed by ANCOM regulations. In regard to unequal development, while Venezuela, Ecuador, and Peru all have substantial petroleum deposits, their petroleum industries are at very different stages of development. Therefore, different standards of treatment must be accorded to investors in order to allow the lesser developed to encourage investment, while the more developed, for example, Venezuela, can nationalize.

\textsuperscript{72} Peru, for example, has announced its intention to eventually nationalize its extractive industries. \textit{See generally Plan Inca}, \textit{PERUVIAN TIMES}, July 1974. For a Spanish text of Plan Inca see Expreso (Lima), July 29, 1974 (Special Supplement).

\textsuperscript{73} The Venezuelan Congress passed the petroleum nationalization bill in August 1975. \textit{See N.Y. TIMES}, Aug. 19, 1975, at 45, col. 2.

\textsuperscript{74} Decision 24, art. 44, 11 INT’L LEGAL MAT’LS 125, 140 (1972).

\textsuperscript{75} Public services are defined as “drinking water, sewage, electric power, illumination, garbage collection, and sanitary, telephone, mail and telecommunications services.” Decision 24, art. 41, id. at 139.

\textsuperscript{76} Decision 24, art. 42, id. at 139.

\textsuperscript{77} Decision 24, art. 43, id. at 139.

\textsuperscript{78} No mention is made in the Code as to what regulations the insurance industry or “other financial institutions” are subject to, other than that no new investments may be made in them. Decision 24, art. 42, id. at 139.
The member countries may, however, choose to apply different standards of regulation for any or all of the above mentioned activities, and several have done so. Some of the member countries have added additional sectors to those which are reserved for “national” enterprises.

Finally, enterprises which export at least 80 percent of their production to non-ANCOM markets are exempted from all divestment requirement. Those products which remain in ANCOM will not, however, enjoy duty-free status.

B. Questions Regarding the Divestment Requirement

There are several significant questions regarding the divestment requirement of the Andean Code which present themselves to the foreign investor. The first is the question of whether the Code provisions requiring divestment of majority equity ownership and control are being strictly enforced by the ANCOM countries, or whether the Code has merely established a set of “rules of the game” which may be broken when the circumstances call for it.

1. STRICT ENFORCEMENT OR “RULES OF THE GAME?”

Although empirical data on the performance of individual firms

79. In Bolivia, Supreme Decree 11450, June 1974, exempts banking and financial institutions from the Code’s provisions. See State Department memorandum, supra note 56, at 1. In Chile, Decree Law 748, Nov. 7, 1974, exempts development banks, and Decree Law 818, December 27, 1974, exempts commercial banks from the Code. Id. at 2. In Colombia, Decree No. 2719 of December 28, 1973, exempts banks, commercial financial institutions, and companies engaged in domestic marketing from the Code. Decree 235 of February 24, 1975, provides that foreign banks and credit institutions must transform into mixed companies under the supervision of a new Commission. Decree 169 of January 31, 1975, regulates companies involved in domestic marketing activities. See Airgram No. A-66 from the U.S. Embassy in Bogota, Colombia, to the Department of State, Apr. 2, 1974. In Ecuador, Supreme Decree 1029 of July 31, 1971, exempted all specially treated sectors from the Code. Resolutions 01 to 105 issued in January 1975 substituted internal regulations for most of these sectors and added others. See note 80 infra. Peru has not invoked the escape clause. Venezuela has chosen not to invoke the escape clause in most instances but has indicated that special regulations will be issued for banks and other financial institutions. Decree 62, art. 4, 13 INT’L LEGAL MAT’LS 1220, 1221 (1974). Venezuela has, like Peru, added additional sectors to the “national” category. See note 80 infra.

80. Pursuant to Decision 24, art. 38, Ecuador has ruled that construction firms must transform into national enterprises. 11 INT’L LEGAL MAT’LS 126, 138 (1972). Venezuela has added “professional services” to the national enterprise category. The professional services sectors, vaguely defined, is regulated by domestic law and reserved to national enterprises. Decree 62, art. 1, 13 INT’L LEGAL MAT’LS 1220 (1974).

81. Decision 24, art. 34, 11 INT’L LEGAL MAT’LS 126, 137 (1972).
in ANCOM is scarce, it seems clear that both the member country governments and foreign direct investors are taking the divestment requirement seriously. Several qualifications regarding this conclusion must be made. First, the initial date for the divestment decision of existing companies has not yet been reached in most of the member countries. Therefore, whether or not firms would have been forced to divest at this date in order to enjoy ANCOM duty-free status can only be verified by the example of Peru and the pronouncements of the other host country governments. However, the ANCOM countries have tempered their original all-or-nothing position by providing that firms may bypass the initial date if it is not essential that their products enjoy duty-free status, and that they may decide at a future date on divestment.

The data from Peru indicate that the Peruvian government has strictly enforced the initial divestment deadline, going even beyond the rules as now provided by the Andean Code. Peru required that manufacturing firms meet the initial divestment deadline in order to enjoy ANCOM tariff concessions, and enacted a General

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82. The most thorough and reliable source on individual firm behavior which is publicly available is a weekly publication Business Latin America published by Business International Corp. This reference is used not only by businessmen, but by government officials in the United States and Latin America. While the author worked in the General Counsel's Office of the Overseas Private Investment Corporation and had access to material relating to the application of the Code vis-à-vis U.S. firms, this information is not available for publication. Nothing in this Article in any way reflects the opinions of the U.S. Government or OPIC.

83. Colombia did not implement the Code until September 15, 1973, and Venezuela not until January 1, 1974. Therefore, for Colombia the initial divestment decision need not be made until September 15, 1976, and for Peru, January 1, 1977. See note 58 supra. In Peru, the initial date was reached and the divestment requirement was enforced. See note 85 infra. Chile has had a great deal of internal debate over when and how the Code was implemented, and though technically, the initial date for enforcement has passed, there is no evidence of firms divesting (although most were expropriated during the Allende administration).

84. Originally, Article 28 of the Code provided that existing firms had to decide within three years of the date of the Code's entry into force as to whether they intended to divest and take advantage of the duty-free market. See note 61 supra.

85. This change was made by a ruling of the Andean Commission, in June 1974, not by an amendment to the Code. The ruling provides that companies which have not provided divestment plans by the three-year deadline will lose ANCOM tariff concessions, but may subsequently choose to divest and gain them. However the final deadline for divestment remains the same. See Ancom Balks at Sectorial Plans But Rules on Fadeout, Patents, Business Latin America, June 12, 1974, at 186.

86. See Peruvian Firms Use Comunidad to Meet Fade-Out Requirements, Business Latin America, June 5, 1974, at 183. This article resulted from a survey which Business Latin America conducted among companies located in Peru. The results are that the great majority of companies met the initial deadline requirement by selling 15 percent ownership to a worker comunidad. See note 87 infra.
Industries Law which requires that firms gradually sell 50 percent of their equity to a worker “comunidad.” Foreign firms were given little choice whether or not to accept the initial deadline, since failure to meet it would result both in permanent loss of ANCOM duty-free privileges and a divestment of ownership. Peru, however, must be regarded as a special case within ANCOM because of its radical economic policies. Existing manufacturing enterprises in other ANCOM countries have yet to be forced into divestment.

The second observation which can be made from the available empirical data is that, almost without exception, new companies entering ANCOM are entering as joint ventures from the outset, not only meeting with the Code’s initial local participation requirement but in most cases surpassing it. These companies are finding partners either in the private sector or with local governments.

A third observation—a judgment made from readings of official ANCOM government pronouncements, business world reaction,

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87. Peru’s General Industries Law of 1970, Decree Law 18350, 9 INT’L LEGAL MAT’LS 1225 (1970), provides that manufacturing companies must sell at least 50 percent of their equity ownership to a workers group called the comunidad. This is accomplished by providing the comunidad with 15 percent of the firm’s pre-tax profits each year until the comunidad has purchased 50 percent of equity.

88. For a statement of Peruvian economic ideology see Plan Inca, supra, note 72.

89. The empirical data in this case come from a three-year survey the author made of articles in Business Latin America. Of 18 major new foreign direct investments reported for the ANCOM countries between 1972 and mid-1975, 13 were begun as joint ventures with local participation above 30 percent. All five of the new investments beginning with 100 percent of capital were headed for Bolivia and Ecuador where firms need not have any local participation until five years after production begins (and then only five percent). The limitation on this data is, of course, that if companies are actually making secret deals with ANCOM governments, these deals are not likely to be reported in any publication.

90. In Venezuela, President Perez’s nationalist economic policies and the text of Decrees 62 and 63 themselves make it clear that Venezuela intends to apply the divestment requirements rigorously. See Decision 24 in Venezuela: Harsher than Anticipated, BUSINESS LAT AMERICA, May 29, 1974, at 175-76.

In Peru, the statements of President Velasco and the requirement of compliance with the General Industries Law make divestment a certainty. Velasco’s credibility rides on his treatment of TNE’s. For Colombia, the government may be slightly less enthusiastic about the divestment requirement than Peru or Venezuela, but it nevertheless has indicated that it fully intends to meet its international commitments. See An In-Depth Look At What Really Is Happening in Colombia, BUSINESS LAT AMERICA, June 25, 1975, at 201-02. Ecuador surprised many foreign businessmen with its tough internal implementation of the Code. See Ecuador Puts New Slant on ANCOM Rules, BUSINESS LAT AMERICA, Apr. 23, 1975, at 136. With its new oil income, Ecuador can afford to be tough with investors. Chile and Bolivia are the two ANCOM countries which have vacillated most with respect to the Code: Chile attempting to change several Code rules with the passage of Decree 600 and declaring the Code unimplemented then later backing down on all of these points. See Andean Countries Challenge Chile’s Investment Law, BUSINESS LAT AMERICA, Sept. 25, 1974, at 312; Ancom Solution to
and unclassified U.S. Government reports— is that the ANCOM
governments, most forcefully Peru and Venezuela, intend to apply
the divestment requirement vigorously. As of yet, there is little rea-
son to doubt the good faith of these pronouncements. However, as
the modification of the initial timetable deadline and the hedging
by Bolivia and Chile have shown, the ANCOM Commission and
some of the member countries are attempting to adapt to specific
economic circumstances when necessary.

2. CAPITAL MARKETS

A second important question regarding the divestment require-
ment is whether sufficient local capital will be available to purchase
majority equity ownership at fair prices.

While the domestic capital markets of the ANCOM countries
are not particularly well developed, it does not appear that capital
for divestment will be lacking. In the first place, foreign companies
will have between 15 and 20 years to complete the divestment pro-
cess, so that local capital may be generated slowly. Divestment
would not require large lump-sum payments. Second, petroleum
export revenues from Venezuela and Ecuador have substantially
improved the capital base of these countries, and Venezuela is chan-
neling significant amounts of capital to regional lending institu-
tions at commercial rates. Third, Peru has created a unique profit shar-
ing plan which firms expect to provide the capital for divestment.
Finally, international and regional lending institutions (for exam-

Investment Code Controversy Shows Strong Solidarity of Bloc, BUSINESS LATIN AMERICA, Nov.
27, 1974, at 384. Bolivia claims that firms which intend only to supply its market need not
divest. See State Department memorandum, supra note 56, and BOLIVIA, LEY DE INVERSIONES
68-76 (1972).

91. In both Business Latin America and the Latin American Economic Report, businessmen reflect a resignation to the fact that the divestment requirement will, in fact, be enforced.

92. U.S. Government Embassy unclassified reports consistently advise U.S. businessmen that they should expect to comply with the Code and the divestment requirement. See, e.g., Airgram No. A-221 from the U.S. Embassy in Bogota, Colombia, to the Department of State, Dec. 31, 1974, at 10, which states “Colombia will, of course, continue to apply the Andean Foreign Investment Code.” See also Airgram A-36 from the U.S. Embassy in Quito, Ecuador, to the Secretary of State, Apr. 24, 1975, at 7; Airgram A-69 from the U.S. Embassy in Caracas, Venezuela, to the Department of State, Apr. 22, 1975, at 2.

93. See note 90 supra.

94. Venezuela has made $500 million available to other Latin American countries through the IDB which can be used for commercial purposes. See Inter-American Development Bank—Venezuelan Fondo de Inversiones: Trust Fund to Contribute to the Financing of Economic Projects, 14 INT’L LEGAL MAT’LS 315 (1975).

95. See note 87 supra.
ple, the Andean Development Corporation, created mainly to aid divestment) have taken an active interest in aiding the ANCOM countries in the divestment process. 66

3. HOW THE DIVESTMENT REQUIREMENT SHOULD AFFECT INVESTOR DECISION-MAKING

The major disadvantage of loss of equity ownership and eventual loss of managerial control over a foreign subsidiary operation is that the parent company and the new local owners may disagree over how the subsidiary should be operated. The relinquishment of control over corporate decision-making can present problems, such as whether profits should be distributed or retained and invested; to what markets products should be exported; and whether patents, trademarks, and the like should be sold to other firms. For the great majority of manufacturing firms these problems are probably not tremendously significant, since it can be generally assumed that local investors and foreign investors share the same desire to maximize the return on investment. The firms for which these problems may be more acute are those in high-technology industries where control over technological resources may be at a premium. The firms most resistant to the divestment program are those which are least interested in giving up control over new production processes and products. 67

As a matter of policy, new foreign direct investments should probably be made as joint ventures with substantial local equity participation from the outset. By forming local partnerships with either private investors or governments, the foreign investor can avoid many of the bureaucratic entanglements involved in the gradual divestment process. Thus, the investor would have less concern over whether local capital will be available when the time for divestment comes, whether disagreements with local bureaucracies over share valuations will arise, whether confiscatory taxes will be levied, and related problems arising in dealings with any complex but not yet fully developed bureaucratic structure. By establishing a sub-

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66. The divestment bank scheme, originally proposed by A. Hirschman, came to life in the form of the Andean Development Corporation which provides investment capital to Andean investors. See A. Hirschman, How to Divest in Latin America and Why (1968); Fresard Rios, El Tratado que crea la Corporación Andena de Fomento, 3 Derecho de la Integración 28 (1968); Andean Loan Body Gets New Financial Muscle, Business Latin America, Feb. 19, 1975, at 60.

67. Vernon discusses the problems of the highly innovative firm regarding divestment programs in Vernon, Sovereignty, supra note 3, at 265-70.
stantial local partnership, the foreign investor is likely to obtain more favored treatment from local government officials because the investment will be perceived as providing greater local benefits, and because major local investors are more likely to be on friendly terms with local government officials.

Because divestment of managerial control can only take place at the end of a 15 or 20 year period, an optimal arrangement for the foreign investor is local equity participation, combined with maintenance of managerial control until the last available date. In this manner, the foreign investor trades his technological resources and managerial expertise for the maximum period of decision-making authority.

For investors with projects already operating within ANCOM, the decision of whether to divest and take advantage of the tariff elimination program, or to retain ownership and control and to supply primarily local markets, depends again on a careful cost-benefit analysis. Firms which are under-utilizing productive capabilities and whose products could easily be transported to other markets within ANCOM may gain from trading equity for an expanded market area. On the other hand, firms which are oriented primarily to local markets and whose productive capacities are geared only to meet these markets (which may prefer exporting to third country markets) would discover little incentive for transformation.

As a general rule, the only firms which may be reluctant to accept the divestment requirement are those which place a premium on their technology, production processes, and trade names. However, for firms whose competitive advantages lie more in the areas of capital investment capabilities, managerial expertise, and marketing capabilities, the divestment program does not create a substantial disincentive to investment in ANCOM.

C. Provisions of the Andean Code Affecting Operations

The Andean Code prescribes a comprehensive set of provisions which regulate the operations of foreign-owned firms within ANCOM. These provisions include: (1) a ceiling on the amount of net profits which can be remitted abroad; (2) a limitation on the amount of net profits which can be reinvested in the enterprise; (3) regulations of the transfer of capital gains abroad; (4) regulation of the amount of interest which can be paid to amortize loans; (5) restrictions on access to local credit; (6) a system to oversee transfer pricing practices; (7) the assertion of domestic jurisdiction for the
settlement of investment disputes; (8) a series of regulations on agreements for the transfer of technology, patents, trademarks, licenses, and royalties.

The Andean Code provides that foreign investors are limited to remitting net profits of up to 14 percent of the value of the registered investment annually.98 The value of the investment is registered with the competent local authority when the firm enters the host country or, in the case of existing firms, as of a date set by local officials. The Andean Code provides general rules regarding valuation. The value of the investment may include foreign capital, machinery, and equipment,99 but it may not include intangibles such as patents or trademarks.100 However, beyond these general rules and a listing of certain specifics which must be contained in registration forms101 the method to be used in determining valuation has been left to local authorities.102 The valuation procedure is important both in terms of profit and reinvestment because the amount of net profits which may be remitted abroad is limited to a percentage of the registered value of the investment in terms of capital gains restrictions.103

The effective control of profit remittances depends upon maintaining an effective system of foreign exchange controls. While a few of the ANCOM countries did not maintain a foreign exchange regulating system before the Code was adopted, this is being remedied.104 While foreign companies may, with the help of the host govern-

98. Article 37 of the Code reads:
Upon authorization by the competent national authority, foreign investors shall have the right to transfer abroad, in fully convertible currency, the verified net profits resulting from the foreign direct investment, but not in excess of 14 percent 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.

Decision 24, art. 37, 11 INT’L LEGAL MAT’LS 126, 138 (1972).

99. Decision 24, art. 1, id. at 128.

100. Decision 24, art. 21, id. at 134.

101. Decision 24, annex 1, id. at 144.

102. Decision 24, arts. 5 & 6, id. at 130.

103. See text accompanying notes 114-19 infra.

104. Venezuela, for example, maintained no foreign exchange controls at all before it implemented the Code. See INVESTING, LICENSING, AND TRADING CONDITIONS ABROAD, Aug. 1974, at 12. Chapter VII of Decree 63, however, authorizes the Supertendency of Foreign Investments to regulate remittance of profits abroad. In addition, Venezuela’s Decree 63 prescribes penalties for firms which remit profits above their authorized level. For the first offense the amount of profits which were illegally remitted must be reimbursed to the Central Bank of Venezuela. For a second infraction, the firm’s negotiation is cancelled and the foreign investor must offer his share of the investment for acquisition by national investors.
ment, petition the Andean Commission for special profit treatment (and there is indication that requests for special treatment are generally granted\textsuperscript{105}) the 14 percent profit ceiling has nevertheless been the subject of debate within the ANCOM system, and it is possible that this ceiling will be adjusted in the not-too-distant future.\textsuperscript{106} Some of the arguments which could be cited against the 14 percent profit ceiling are: (1) interest rates for commercial borrowing and inflation rates both in the developed and developing countries are too high to make a 14 percent rate of remittance on investment either attractive or reasonable; (2) once the ANCOM countries have fully integrated their system of foreign exchange controls, alternative means of remitting profits other than as declared earnings will be prohibited—and, therefore, levels of declared net profits will increase;\textsuperscript{107} and (3) since TNE's are prohibited from capitalizing intangibles and paying royalties from subsidiaries to parents some additional compensation should be added as an adjustment.\textsuperscript{108}

In addition to limiting the amount of net profits which a foreign investor may remit abroad, the Andean Code also limits the amount of net profits which can be reinvested in an enterprise without prior authorization from the competent national authority. In the absence of authorization, foreign investors are limited to a five percent net profit reinvestment annually, calculated as a percentage of the registered investment. Up to the five percent limit, reinvestments must still be registered with the national authorities.\textsuperscript{109}

The question arises as to what may be done with profits above the 19 percent level—that is, the 14 percent remittance plus the five percent reinvestment limit—in the absence of additional reinvestment authorization. Foreign firms may make new investments in the host country, but these new investments must be applied for and authorized just as new investments coming from abroad.\textsuperscript{110} Foreign investors may invest in other national or mixed firms, provided that such investment can be made without purchasing shares al-

\textsuperscript{105} Interview with Louis Goodman, Staff Associate of Social Science Research Council, in New York City, Apr. 14, 1974.

\textsuperscript{106} The profit ceiling question has been on the Commission's agenda and there seems little strong objection to having it changed. See Andean Code Changes Proposed, BUSINESS LATIN AMERICA, Sept. 25, 1974, at 312.

\textsuperscript{107} Reported rates of return on investment from manufacturing companies in Latin America have fallen in the 10 to 20 percent range. See La Investment and ROI Prospects Turn Favorable for US Firms, BUSINESS LATIN AMERICA, Nov. 20, 1974, at 370-71.

\textsuperscript{108} See note 38 supra and accompanying text.

\textsuperscript{109} Decision 24, art. 13, 11 INT'L LEGAL MAT'LS 126, 132 (1972).

\textsuperscript{110} There is no bar in the Code against using excess profits to establish a new enterprise.
ready held by national investors,\textsuperscript{111} and that the investment does not change the mixed or national character of the enterprise.\textsuperscript{112} Finally, Decision 70 of the Andean Commission lists certain types of local bond issues which can be purchased with "excess profits" without the requirement of authorization.\textsuperscript{113}

The provisions in the Andean Code regarding the re-exportation of a foreign investor's capital abroad are perhaps the most ambiguous provisions in the Code,\textsuperscript{114} and therefore leave a good measure of discretion in the hands of the individual member government. It appears that foreign investors are limited in their re-exportation of capital to the amount of the investment authorized and registered with local authorities.\textsuperscript{115} In addition, the foreign direct investor must agree with the local authorities, at the time the investment is registered, on the method which is to be used to value his shares at the time of sale for divestment purposes.\textsuperscript{116} The valuation procedure which is used by the local authorities becomes, as it does with the profit remittance regulations,\textsuperscript{117} of primary importance to the foreign investor. By inflating or deflating the value of the initially registered investment, the local authorities can either

\textsuperscript{111} Decision 24, art. 3, 11 INT'L LEGAL MAT'LS 126, 129 (1972).
\textsuperscript{112} Decision 24, art. 4, id. at 130.
\textsuperscript{113} By Resolution 6074, September 1974, Venezuela defines these securities to include, \textit{inter alia}, public debt instruments, mortgage bonds issued by Venezuelan mortgage banks, commercial bonds which grant no right of participation in the management of the company, and obligations issued by the Andean Development Corp. State Department memorandum, supra note 56, at 5.

In addition, some foreign investors have reported that they are allowed to use their excess profits for local expenses not directly related to their businesses, for example intra-company airfare costs.

\textsuperscript{114} The provisions of the Code which deal directly with the question of capital re-exportation are Articles 7-10 inclusive. Decision 24, 11 INT'L LEGAL MAT'LS 126, 131 (1972).
\textsuperscript{115} This interpretation follows from Article 8, which provides that:

\textit{[R]e-}exportable capital is understood to be the capital formed by the total of the original foreign direct 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 net losses, if any.

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

Decision 24, art. 8, 11 INT'L LEGAL MAT'LS 126, 131 (1972).

This amount would include additional new foreign investments made in the enterprise which are authorized and registered.

\textsuperscript{116} Decision 24, art. 31. \textit{Id.} at 137. The need for this valuation procedure reflects the fact that there are no operational "stock markets" in any of the ANCOM countries and that, when the time for divestment approaches, local private capital may be scarce. Therefore, share values will have to be administratively determined.

\textsuperscript{117} See note 102 supra and accompanying text.
increase or decrease the permissible level of profit remittances and the maximum amount which the investor can receive at the time of the sale of his share in the enterprise. Thus the valuation procedure provides both government and investor with a bargaining flexibility which is lacking in other areas of the Code.

Whether the foreign direct investor is limited in capital re-exportation to the amount of the registered investment is not absolutely clear. Neither the Andean Commission nor local implementing legislation has done much to settle the ambiguity surrounding these provisions. The Code could just as easily be interpreted to indicate that investors may re-export whatever amount of capital is received at the time his shares are sold.118

In either case, the investor does not face a capital loss at the time of sale, since for tax purposes he will have depreciated the value of his assets on his own records. The foreign investor is, however, required to pay whatever taxes the host country may impose on the sale of his assets to local investors before re-exportation.119 A great deal depends upon the discretion of the local authorities and upon the foreign investor’s ability to bargain with them effectively.

The Andean Code regulations govern credit transactions. All contracts for external credit must be authorized and registered by competent local authorities.120 Payments made to amortize loans from abroad must be authorized by local officials in accordance with registered contracts.121 In addition, the Code limits the amount of interest which may be paid on an intra-company loan between a foreign parent or affiliate and an ANCOM subsidiary to not more than three percent above the going rate of interest on first class loans in the country from which the loan is made.122 Finally, foreign enterprises are denied access to other than short-term local credit

118. This interpretation of the Code proceeds from both the Code and the national implementing legislation. Article 10 reads: “Foreign investors shall have the right to transfer abroad the amounts obtained from the sale of their shares, participation, or rights, after payment of the pertinent taxes.” Decision 24, art. 10, 11 INT’L LEGAL MAT’LS 126, 131 (1972). Venezuela’s implementing legislation is typified by Decree 63, Article 33, which reads: “Foreign investors shall be entitled to remit abroad the amount resulting from the sale of their shares, participations, rights to national investors or from the liquidation of the company,” 13 INT’L LEGAL MAT’LS 1221, 1226 (1974).

119. Decision 24, art. 10, 11 INT’L LEGAL MAT’LS 126, 131 (1972). This provision on the application of domestic taxes to re-exported capital may lead to the conclusion that the investor is better off in obtaining substantial local equity participation at the outset of the investment.

120. Decision 24, art. 14, id. at 132.

121. Decision 24, art. 16, id.

122. Decision 24, art. 16, id.
in accordance with rules to be established by the Andean Commission. 123

In order to effectively control the flow of foreign exchange out of the ANCOM countries, the Andean Code authorizes the member countries to establish an "information and price control system of intermediate products that may be furnished by suppliers of foreign capital and technology." 124 The system grew out of a study which showed that profits were regularly taken out of Colombia by TNE's as inflated payments made by subsidiaries to parents for intermediate products and not as declared earnings. 125

The establishment of effective transfer-pricing controls requires the creation of a highly efficient bureaucracy. Data on the arm's-length prices of an enormous amount of intermediate goods must be accumulated and stored for retrieval, while prices undergo continuous change. The practicality of such a system was questioned by Senator Javits in the Report of the Group of Eminent Persons. 126 Reports from the ANCOM countries have yet to indicate that substantial progress is being made in the development of such a system.

The Andean Code prohibits the inclusion, in agreements concerning foreign investments or the transfer of technology, of clauses which remove jurisdiction over investment disputes from the host country. The Code also prohibits the subrogation of foreign states to the rights of its national investors in the event of investment disputes. 127 The provision on subrogation is principally directed towards government operated investment insurance companies—such as the U.S. Overseas Private Investment Corporation 128—which succeed to the rights of their national investors after the payment of a claim (for example, for expropriation compensation) in order to permit the use of diplomatic intervention to obtain compensation from host country governments. 129 The provision by the ANCOM govern-

123. Decision 24, art. 17, id.
124. Decision 24, art. 6(c), id. at 131.
125. See generally Vaitos, Transfer of Resources and Preservation of Monopoly Rents, in HARVARD UNIVERSITY CENTER FOR INTERNATIONAL AFFAIRS, ECONOMIC DEVELOPMENT REPORT No. 168 (1970). See also, on the role of transfer pricing in the remittance of profits, Impact Report, supra note 36, at 74-75.
127. Decision 24, art. 51, 1 INT'L LEGAL MAT'LS 126, 141 (1972).
128. Several developed country governments now operate programs of foreign investment guarantees for their national investors.
129. OPIC's legislative purpose is to stimulate the flow of U.S. private capital into less developed countries by guaranteeing these investments against political risks and providing developmental loans. See, e.g., Public L. No. 93-390 (Aug. 27, 1974). Since OPIC operates
ments that investment disputes may only be decided in the host country does not mean that a foreign investor could not appeal a denial of justice to an international tribunal and seek whatever remedies are available under international law.

D. Provisions Regulating the Transfer of Technology

The ANCOM countries attach great value to the role of modern technology in the industrial development process. The goal of ANCOM technology policy is to acquire necessary technology from abroad at the least possible cost and with the fewest strings attached, and simultaneously to improve local research and development capabilities.

The ANCOM countries have developed a new attitude towards the transfer of technology from abroad, whose impact is only beginning to be felt by foreign direct investors. In essence, the attitude derives from the belief that technology should not be commercialized, but that developed country industries should make it freely or cheaply available to developing countries. Research on a self-sustaining basis, however, it must require compensation from host country governments or rapidly deplete its insurance reserves. OPIC seeks compensation only as required by general principles of international law and not through U.S. Government diplomatic intimidation.

130. The introductory portion of Decision 84 of the Andean Commission reads in part: "Our contemporary world is characterized by the controlling influence that is inherent in the possession of know-how and the capacity to utilize it in economic and social orientation." See INT'L LEGAL MAT'LS 1478 (1974).

131. The ANCOM countries relate their previous relation to technology transfer as follows:

Member Nations have had recourse to external services in a proponderant form to satisfy the needs of technical development, with such undesirable results as the following solutions inadequate to the characteristics of economic development of the Member Nations and to the availability of productive factors; extremely elevated costs; limited possibility to exercise a choice among various alternative solutions; the displacement of local operations and elements, and the underutilization of local scientific and technological resources; a conditioning of political and economic decisions to technological solution imposed from abroad; and a miscellany of unsatisfied needs due to the inadequacy of technological solutions . . . .

Decision 84, id. at 1478.

132. Decision 84, para. 5, id. at 1481.

133. This impact comes as the ANCOM countries gradually require investors to conform their technology agreements to the Andean Code's regulations. Venezuela has, for example, given foreign investors until December 31, 1975, to have their contracts approved by the Superintendency of Foreign Investments; after which, contracts which do not conform will cease to have legal effect. Decree 63, arts. 61 & 63, INT'L LEGAL MAT'LS 1221, 1232 (1974).

and development costs involved in the generation of new commercial technology are fixed costs of the enterprise involved. This fixed cost is recovered by the enterprise when its product is marketed—that is, the product incorporates the technology, and the technology costs are reflected in the selling price of the product. For a parent company to sell this technology to its own subsidiary is to profit twice from the technology: once from the sale of the product itself, and once from the sale of the technology.\textsuperscript{135}

The ANCOM countries have created legal mechanisms for implementing their policy relating to technology transfer in the Andean Code and in the recently enacted Decisions 84 and 85 of the Andean Commission.\textsuperscript{136} The Andean Code provides broad rules on several aspects of the technology transfer (or "commercialization") process, and Decisions 84 and 85 supplement the Code with detailed provisions relating both to the creation of a regional technological infrastructure and to the legal treatment of patents, licenses, and trademarks within ANCOM.

The Andean Code provides that technological agreements may not be capitalized as foreign direct investments.\textsuperscript{137} In addition, parent companies or their affiliates are prohibited from receiving royalty payments from their subsidiaries incorporated in ANCOM countries for the use of patents, trademarks, licenses, and in some cases, even technical assistance in the form of personnel.\textsuperscript{138} All

\textsuperscript{135} Id.

\textsuperscript{136} Decision 84 of the Andean Commission, Decision on The Bases for a Subregional Technological Policy, and Decision 85, Decision on Industrial Property, were adopted in June 1974. For the text of these two decisions see 13 INT'L LEGAL MAT'LS 1478-99 (1974). The ANCOM governments were given a period of six months following the approval of the Decisions to incorporate them into domestic law. Implementing legislation is not yet available, and it is not yet reported that the Decisions have been implemented. It is possible, of course, that these new Decisions may be modified somewhat in their implementation in the individual member countries. Nevertheless, for the purposes of this discussion we will treat these Decisions as if adopted in total.

\textsuperscript{137} Decision 24, arts. 1 & 21, 11 INT'L LEGAL MAT'LS 126, 128, 134 (1972). This, of course, means that technology capital cannot be used to increase the right to profit remittances, or be included in valuation calculation for the purposes of re-export of capital. See Section III.D. of the text.

\textsuperscript{138} Decision 24, art. 21, id. at 134. While the Code prohibits royalty payments for "intangible technological contribution," this term is not expressly defined in the main body of the Code. Intangible technological contributions are referred to in Annex 1 of the Code as: "Marks, Industrial Models, Managerial Capacity, Technical Knowhow Whether or Not Patented, and Alternate Possible Technologies." In Venezuela's implementing Decree 63, technological contributions are expressly defined for Article 21 purposes to include technical assistance in the form of qualified personnel. Decree 63, art. 6, 13 INT'L LEGAL MAT'LS 1221, 1222 (1974).
technological agreements, whether between parent and subsidiary, or between an ANCOM incorporated firm and unrelated foreign firm, must be approved by the competent authority of the receiving member country.\footnote{139}

Patent and trademark licensing agreements are prohibited from incorporating a variety of restrictive clauses which might tend to limit the flexibility of the receiving ANCOM company in the use of the license (for example, export restricting clauses, tie-in clauses, and the like).\footnote{140} The recent Decisions 84 and 85 of the Andean Commission, however, establish in detail the guidelines for the registration and authorization of patents, trademarks, and licenses within ANCOM, and the uniform legal treatment which such registration will confer.\footnote{141}

Decision 85 provides regulations for the registration of patents in the receiving ANCOM country and delineates the legal rights which ownership of a patent may confer. Patents may not be granted for certain types of products.\footnote{142} The application for a patent must include a technical description of the invention complete enough to allow duplication.\footnote{143} Patents may be granted for a maximum period of ten years, with renewal and proof of exploitation required after five years.\footnote{144} Subject to the limitations expressed in other areas of Decision 85, a patent confers on the owner the exclusive right to exploit it in the recipient country, to grant licenses for its exploitation, and to receive royalties or compensation for its exploitation. Patents do not confer an exclusive right to import the patented product or one manufactured under the patented process.\footnote{145} Filing a patent application in one ANCOM country gives the applicant a (one-year) priority right to file for patent in the other member countries.\footnote{146}

The more interesting regulations of Decision 85 have to do with the licensing of patents. Patents may only be exploited in ANCOM

\footnote{139} Decision 24, art. 18, 11 \textit{Int'l Legal Mat'ls} 126, 132 (1972).
\footnote{140} Article 20 for clauses which may not be contained in contract on the transfer of techniques or patents and Article 25 for clauses which may not be contained in trademark licensing agreements. Decision 24, arts. 20 & 25, \textit{id.} at 133, 135.
\footnote{141} Decision 84 deals primarily with the establishment of a regional technology policy. Legal details are contained in Decision 85. See note 136 supra.
\footnote{142} This includes, \textit{inter alia}, pharmaceutical products and beverages. Decision 85, art. 5, 13 \textit{Int'l Legal Mat'ls} 1489, 1490 (1974).
\footnote{143} Decision 85, art. 12(e), \textit{id.} at 1491.
\footnote{144} Decision 85, art. 29, \textit{id.} at 1492.
\footnote{145} Decision 85, art. 28, \textit{id.}
\footnote{146} Decision 85, art. 10, \textit{id.} at 1491.
pursuant to authorization by competent national authorities.\textsuperscript{147} Licensed patents must be exploited within the country of registration according to conditions established in Decision 85.\textsuperscript{148} After a period of three years from the date that the patent is granted, any person may apply to the competent authority for the granting of a “compulsory license” if the patent has not been exploited adequately within the member country. After a period of five years the competent authority may grant a compulsory license regardless of whether or not conditions of exploitation have been satisfied.\textsuperscript{149} The holder of a compulsory license must pay an “adequate compensation” to a patent holder.\textsuperscript{150} The government of the country in which the patent is registered may at any time grant a compulsory license in view of national development needs or interest in the public health.\textsuperscript{151} Licenses which do not comply with the regulations established in Decision 85 will be considered void.\textsuperscript{152}

Trademarks must be approved and registered by the competent national authority as well,\textsuperscript{153} and registration of a trademark grants the right of exclusive use for continuously renewable periods of five years.\textsuperscript{154} Likewise, trademark licensing agreements must be approved and registered.\textsuperscript{155} Trademark licensing agreements may not include a variety of export-restrictive clauses, which were earlier prohibited by Article 25 of the Andean Code.\textsuperscript{156} Trademarks are not subject to “compulsory licensing” as are patents.

The new ANCOM regulations governing patents, licensing, and trademarks represent an attempt by the member countries to make modern technology more freely accessible to commercial enterprises in the region. The regulations provided by Decision 85 represent a radical departure from the traditional concept that patent ownership rights should be afforded the highest degree of protection. In effect, the patent licensing rules provided by Decision 85 mean that

\textsuperscript{147} Decision 85, arts. 32, 42, & 43, id. at 1493, 1494.
\textsuperscript{148} The exploitation of a patent may not be suspended for more than one year; production of the patented product must meet the demands of the national market re quality, quantity, and price; and the patent owner must grant licenses under reasonable conditions to satisfy the market. Decision 85, art. 34, id. at 1493.
\textsuperscript{149} Decision 85, art. 34, id.
\textsuperscript{150} Decision 85, art. 34, id.
\textsuperscript{151} Decision 85, art. 39, id. at 1494.
\textsuperscript{152} Decision 85, art. 40, id.
\textsuperscript{153} Decision 85, art. 60, id. at 1497.
\textsuperscript{154} Decision 85, art. 69, id.
\textsuperscript{155} Decision 85, art. 81, id. at 1498.
\textsuperscript{156} Decision 85, art. 81, id.
ANCOM country governments are free to give away a registered patent to any enterprise which desires it, so long as this procedure is considered in the interests of the member countries' development plans, and so long as some unspecified form of compensation is provided to the patent owner. The rules do not specify that "compulsory licenses" may be issued solely to ANCOM national investors, and it appears that a foreign investor's registered patents may even be licensed to other foreign enterprises in ANCOM.

Decision 85 was designed to be implemented in the domestic law of the ANCOM members within six months following its approval by the Commission.\footnote{157. Decision 85, art. 86, id. at 1499.} No information has yet been made available on the process of implementation and, as was the case with the Andean Code, the time limit on implementation may be exceeded by the member countries. However, when the Decision is implemented its rules will apply to patents, licenses, and trademarks already registered in the region.\footnote{158. Decision 85, art. 85, id.} In addition, the rule established in Article 21 of the Andean Code which provides that subsidiaries may not pay royalties to their parent companies is already being enforced in at least some of the member countries;\footnote{159. Venezuela, for example, has indicated to foreign direct investors that as of December 31, 1975, their technology agreements must conform to Decree 63 regulations, one of which, Article 21, prohibits the payment of subsidiary to parent royalties. Foreign firms have been informed that after December 31, 1975, they will no longer be permitted royalties to their parents.} and while technology supply costs may to some extent be added to the selling price of products and thereby returned as profit, these profits are limited to 14 percent per annum on the registered value of the investment (which cannot include technology).

The impact of the new technology transfer regulations on foreign direct investor behavior can only be speculated upon, as they have no precedent in modern investment regulation. It might be expected that for foreign firms whose research and development costs are high (for whom innovative technology represents a primary competitive advantage over their international rivals), the ANCOM technology regulations will represent a major disincentive to new investment. Or, at least, these firms may wait a period of several years after the development of a new technology before bringing it into the Andean region. For firms whose products embody technology which is widely dispersed and whose investment advantages lay more in the access to capital, marketing, or managerial skills, the
technology regulations should have little impact at all.

The ANCOM countries are betting that foreign investors will be willing to trade their technology for access to the expanded ANCOM market. The outcome of this gamble remains to be seen. If successful, the ANCOM policy may improve their technological infrastructure and increase their industrial self-sufficiency. If unsuccessful, the result may be another period of years in which ANCOM industries fall farther behind those of the developed countries in technological development. It remains to be seen how far the ANCOM countries can proceed in extracting concessions from foreign direct investors before disincentives overshadow opportunities.

IV. THE INTEGRATION OF MARKETS AS APPLIED TO THE ANDEAN FOREIGN INVESTMENT CODE

A. Changing the Economic Balance of Power

In the second section of this Article the relationship between host developing countries and foreign direct investors was analyzed in terms of bargaining theory. It was noted that as the economic power relationship between the two major bargaining participants changes, the terms by which foreign direct investors are permitted to operate are also subject to change. The member countries of the Andean Common Market have taken affirmative action to increase their economic bargaining power vis-à-vis foreign direct investors. The movement towards creating a free trade zone among the members and establishing a common customs barrier have, in effect, created one large economic unit where before there existed an unrelated collection of smaller units. The creation of this integrated market and the concentration of sovereign authorities in the Andean Commission have enhanced the economic bargaining power of the ANCOM countries and have resulted in a change in the terms under which foreign direct investors are permitted to operate.

As of 1973 the combined population of the ANCOM countries was 71.6 million persons. By 1980 this figure is expected to reach more than 90 million.160 Thus, measured in terms of population, the ANCOM market is now larger than that of either Argentina or Mexico, and is second only to Brazil among the Latin American countries.161 In addition to a large consumer market, the ANCOM coun-

161. Id.
tries collectively offer to foreign direct investors a wide range of natural resources vital to manufacturing activities, for example, Venezuelan iron and petroleum, Bolivian tin, and Chilean copper, and a large manpower pool, not as yet fully tapped.

Of course, for a common market to be an attractive market there must be some indication that the reduction of tariff barriers will result in an increase in intra-regional trade. Recently released IMF Direction of Trade statistics\(^\text{162}\) provide empirical evidence that tariff reductions in the ANCOM region are producing an increase in intra-regional trading activity.

| Intra-ANCOM Exports (f.o.b.) and Imports (c.i.f.) (Millions of $U.S.) |
|------------------------|------------------------|------------------------|------------------------|------------------------|
|                        | 1968                   | 1973                   | % increase 1968-1973   | Ancom % of total exports |
|                        | Exports                | Imports                | Exports                | Imports                | 1968       | 1973       |
| Bolivia                | 3.7                    | 4.6                    | 24.2                   | 8.0                    | 554        | 74         | 2.2        | 10.7       |
| Chile                  | 15.0                   | 49.3                   | 23.4                   | 69.4                   | 56         | 20         | 1.6        | 1.9        |
| Colombia               | 24.0                   | 22.0                   | 79.1                   | 41.7                   | 230        | 90         | 4.3        | 7.3        |
| Ecuador                | 12.3                   | 17.3                   | 75.4                   | 32.4                   | 513        | 87         | 6.3        | 13.8       |
| Peru                   | 23.1                   | 28.2                   | 45.2                   | 90.7                   | 96         | 222        | 2.7        | 4.3        |
| Venezuela              | 64.6                   | 19.7                   | 51.4                   | 23.1                   | -20        | 17         | <0.5       | <0.5       |
| Total                  | 142.7                  | 141.1                  | 298.7                  | 255.3                  | 108        | 81         | 2.5        | 4.1        |

If Venezuela is excluded from the figures above, because the tremendous rise in petroleum prices actually decreased its share of intra-ANCOM exports, the figures for the remaining five ANCOM countries show an increase in intra-regional trading of 217 percent between 1968 (the year before ANCOM was formed), and 1973. While the base from which these countries began is not great,\(^\text{163}\) the increase may well be indicative of a trend towards the satisfaction of ANCOM demands with locally produced products.

As a general proposition the ANCOM countries, like all of the Latin American countries, are at an intermediate stage of industrial development.\(^\text{164}\) At this stage, in order to maintain a competitive import-substituting and export-producing manufacturing sector,

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162. IMF, Direction of Trade, Statistics Bureau, reprinted in Andean Trade Expansion is Spurred on by Integration Efforts, BUSINESS LATIN AMERICA, May 21, 1975, at 163.

163. That is, intra-ANCOM trade as a percentage of exports rose from a 1968 base of 2.5 percent, to a 6.0 percent total in 1973.

the ANCOM countries must to some extent depend on foreign capital and technological expertise. At present, Bolivia, Ecuador, and Chile are more dependent on foreign assistance than are Colombia, Peru, and Venezuela. The collective attitude of the ANCOM countries towards the contribution of foreign direct investment in the development process can be more readily identified—although certainly the range of positions between Chile and Peru may be considerably different. This attitude is that foreign direct investment has both positive and negative attributes, and while the positive contributing factors may be encouraged, the negative attributes—such as a tendency towards political intervention—cannot be allowed to predominate. Individual investment projects must be examined carefully to determine the contribution which may be afforded to the development process and must be accepted only on the basis of positive contribution.

The ANCOM countries retain the bargaining advantage of sovereign authority, and with this authority at least partially concentrated by the Andean Commission, their power has been enhanced. That is, foreign governments and investors are no longer confronted by a single and relatively small Latin American country when they attempt to influence or object to a decision which an ANCOM government has made. Parties attempting to bargain with the ANCOM countries are now confronted with a sovereign unit whose territorial mass extends the entire western length of Latin America. While this enhancement of sovereign power cannot be measured in statistical terms, the U.S. Government, for example, would more likely sooner take an action which might alienate a single state like Bolivia than one which might alienate the entire Andean group.

The economic bargaining power of foreign direct investors is limited by the lack of concentrated authority. While the ANCOM governments may present a united front to foreign investors, these investors remain in competition with each other in the international arena and, in the case of U.S. investors at least, may be prohibited by antitrust laws from agreeing with unanimity to a set of minimum investment terms from the ANCOM countries. And even if U.S. investors could agree to form a united bargaining position vis-a-vis the ANCOM countries, their competitors from Japan and Western Europe would remain independently able to fill an investment vacuum. A policy of confrontation might be successful if cooperation could be established among the direct investment suppliers of all the developed countries. This policy, however, would be both im-
practical and counterproductive.\footnote{That is, a united demand by the Western developed investment suppliers for a change in the terms of the Andean Code would probably cause political problems which would more than outweigh the benefits of improved investment terms.}

In addition, the greater the incentives for investment offered by a particular region, the more likely that foreign direct investors would be willing to accept less attractive investment terms. Thus, whichever factors explain the motivation behind a foreign investor's decision to enter a particular region,\footnote{See Section II.A.2 of the text.} the increase in ANCOM market size and the trend towards increased intra-regional trade are bound to represent positive investment incentives. The increased economies of scale which foreign direct investors are permitted and the protection which a common tariff barrier may afford will increase the competitive advantage of the local producer. Transnational competitors are not likely to risk losing a market as large as ANCOM to their rivals.

\section*{B. The ANCOM Bargaining Strategy}

Within the limits of the economic balance of power, host countries and foreign direct investors may employ bargaining strategy to obtain for themselves the most attractive set of investment conditions that are mutually acceptable. The bargaining strategy of the ANCOM countries has taken the form of the Andean Foreign Investment Code. The Andean Code establishes for all of the member countries a set of minimum non-negotiable bargaining principles which the members are prohibited from relaxing. The commitments of the member countries are enforced by public opinion, domestic law, and the sanctioning powers of their ANCOM neighbors.\footnote{The most powerful evidence that this sanctioning power is effective is that Chile was forced to back down from a different set of principles which it established in contravention of the Code. See note 90 \textit{supra}.}

The major commitments of the ANCOM countries include the gradual divestment of majority ownership and control in non-exempted sectors, the adherence to strict requirements for agreements on the transfer of technology, and, to a great degree, the limitation of the remittance of profits abroad.\footnote{Exemption from this requirement requires petitioning the Andean Commission. See text accompanying note 105 \textit{supra}.} Because these major principles are non-negotiable, they place the foreign direct investor in a position of either investing and accepting the terms offered, or rejecting these terms and refraining from entering ANCOM.
On the other hand, the Andean Code by no means eliminates all bargaining between individual ANCOM governments and potential foreign direct investors. The valuation of the foreign direct investment (on which much of the potential for an investment's profitability depends) has been left to the discretion of the individual member governments. In addition, the levels of income taxation and capital re-export taxation, as well as the ability to petition the Commission for a change in profit remittance levels, have been left in the hands of individual member governments. Therefore, for foreign direct investors who are willing to accept the major requirements of the Andean Code, there remains a flexibility within which a relatively attractive investment agreement can be negotiated.

The increase in ANCOM's economic power vis-à-vis foreign direct investors and the strategy of commitment to several major investment regulating principles are designed to produce a major change in the role which foreign direct investors play in the political, social, and economic life of the ANCOM countries. For the desired changes to be achieved, the ANCOM countries must maintain a firm commitment to these principles, because once negotiation over the major principles of the Andean Code is permitted, the ability of the member countries to maintain them will be severely diminished.

C. The Outcome of the ANCOM Strategy

We cannot judge the impact of the Code on the basis of whether the flow of foreign direct investment into ANCOM has increased, diminished, or remained the same because the ANCOM countries clearly had goals in mind other than maintaining a steady flow of foreign direct investment when adopting the Code. How can we measure the political, economic, and social value of increased participation of local investors in the industrial development plans and future of a region?

The U.S. Department of Commerce statistics on the book value of U.S. direct manufacturing investments in ANCOM and other Latin American countries supply little in the way of revealing analysis.¹⁶⁹

¹⁶⁹. These statistics are compiled from the Department of Commerce publication *Survey of Current Business*, for the years 1968-1974.

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In the five year period between 1968 (two years before the Andean Code was adopted) and 1973, the increase in the book value of U.S. manufacturing investments in the ANCOM countries as a whole (excluding Bolivia and Ecuador) was considerably greater than that for Argentina, slightly less than the increase for Mexico, and considerably less than the increase for Brazil. Chile, where the value of U.S. manufacturing investment actually decreased during this five year period, experienced severe political disruptions during this period, so that the decline in foreign direct investment activity can hardly be attributed solely to the Andean Code. Peru, where the value of U.S. manufacturing investment remained nearly constant, pursued a policy towards foreign direct investors which went beyond the requirements of the Andean Code.

The Department of Commerce estimates on property, plant, and equipment expenditures by U.S. manufacturers, which are more current, tell much the same story. Again we find that ANCOM as a whole was the site of expenditure increases slightly higher than in Argentina, slightly lower than in Mexico, and with other Latin American countries lagging far behind Brazil. Again, the lack of dynamism in Chile and Peru must be attributed to domestic political activities as much as to the Andean Code.

What conclusions can we draw from these statistics? First, it appears that Brazil is far more attractive to foreign direct investors.

Estimates of Property, Plant and Equipment
Expenditures by Majority-Owned Foreign Affiliates
of U.S. Companies—Manufacturing Totals (Millions of $U.S.)

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than other Latin American countries. Brazil offers the largest consumer market in Latin America in terms of population, an unusual history of political stability, and a governmental attitude which is hospitable to foreign direct investment.\textsuperscript{171} Beyond this, the ANCOM countries as a unit have attracted slightly more foreign direct investment than Argentina and slightly less than Mexico in the period since the Andean Code was adopted. Argentina and Mexico have adopted foreign investment regulations somewhat similar to those of the ANCOM countries.\textsuperscript{172}

But as has already been indicated, the measure of success or failure of the ANCOM policy towards foreign direct investment will depend on the future of economic development in ANCOM, the increase in political, economic, and social autonomy, and the creation of a technological infrastructure which is capable of meeting the challenges of the developed world. It may well be 20 years before the results are clear.

D. Implications and Conclusion

A great tension presently surrounds the relationship between developing countries and foreign direct investors throughout the world. Governments feel themselves threatened by what they perceive as the overwhelming power of transnational enterprises to influence their economies and destinies. Transnational enterprises consider themselves threatened by what they consider a disregard on the part of sovereign governments for their legal rights.

\textsuperscript{171} For a thorough discussion of investment conditions in Brazil, see generally P. GARLAND, DOING BUSINESS IN AND WITH BRAZIL (1972).

\textsuperscript{172} For Argentina, see 12 Int'l Legal Mat'ls 1489 (1973). For Mexico, see id. at 643.
The member countries of the Andean Common Market have taken innovative steps towards achieving a balance between their own interests and the interests of foreign direct investors. They have integrated their economies, and to some extent their sovereign authorities, in order to increase their economic power vis-à-vis foreign direct investors, and they have adopted and implemented the Andean Foreign Investment Code to take advantage of the new economic balance.

The continuous bargaining process which characterizes the relationship between host countries and foreign direct investors indicates that investment agreements are subject to renegotiation and change. The Andean Foreign Investment Code provides a legal mechanism to accomplish this change over time by requiring foreign investors gradually to relinquish their control over manufacturing enterprises. The Code thus provides a mechanism for reducing the political tensions surrounding the presence of transnational subsidiaries by eliminating the necessity for abrupt demands or expropriations by the ANCOM countries. It also embodies a degree of flexibility which permits both governments and investors to seek and make concessions on the terms of investment agreements.

The ANCOM model of integration and investment regulation may well be the wave of the future. Unless the international community as a whole can prescribe guidelines for the operations of transnational enterprises, it remains for individual countries and regions to deal with the issues surrounding them on their own. In this Article an attempt has been made to characterize the relationship between host countries and foreign direct investors and to show how the actions of governments can affect this relationship. Legal systems cannot be divorced from the realities which they govern, and if systems are to be developed which can reduce the tensions surrounding foreign direct investment, the factors which govern investment conditions must first be understood.