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## Structuring Direct Investment in Latin America: Keeping Pace with New Financial Regimes, Innovative Investment Vehicles, and Changing Labor Laws

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Multi-media uses digital binary language that unifies all technologies in order to transmit and transcribe information. With this new invention, this new technique, we can use audio or video individually or together. You have unification of different activities that were separate in the past: the entertainment industry, the computer industry, the telecommunication industry, the publishing industry — all jumbled into one industry of the future. This is an important point. You can see the figures for the past year and provisions for the coming year. The market will grow by more than 10%. The CD-ROM drives are the peripherals that are needed to use multi-media in personal computers. The installed base of CD-ROM drives will more than double in the next year.

What are the legal problems of the multi-media industry? The principal problem is that if you are producing a multi-media work, you are tempted to use items that may be the property of a third party. Music is an example. Even if the composition is public domain, the performance may not be. Secondary performances are not always protected.

Another problem is establishing the price. In the cinema or music, you have established, customary prices. These do not exist on the multi-media side, and the costs of production can be difficult to calculate because of different rights that different parties may own. Thus, the first step is not just to settle with one owner, but rather to investigate and settle with all possible copyright owners. A work that is in the public domain in one country may not be public domain in another. Rights even can vary from state to state. Furthermore, countries with a civil law approach have different views towards copyrights.

The commentators advise a worldwide unification of definitions of rights so that the owners can collect their money and give the multi-media makers a chance to produce. The first advice we give clients is to avoid anonymous use. If you cannot determine the owner, do not use the material. What if you cannot find the owners or the terms of the right? This is a problem because old contracts may not specify new media techniques. Even if the contract includes a “all future media” clause, not all countries may recognize it. It is a good idea to get a specific multi-media agreement.

### III. STRUCTURING DIRECT INVESTMENT IN LATIN AMERICA: KEEPING PACE WITH NEW FINANCIAL REGIMES, INNOVATIVE INVESTMENT VEHICLES, AND CHANGING LABOR LAWS

#### L. JANÁ SIGARS

The moderator for the next section will be Salvador J. Juncadella. Mr. Juncadella has been with this conference since it commenced. He is one of the conference’s bright stars and one of the persons to whom we look to give us guidance and answer any questions we might have. He is a great resource

and a great lawyer. He was formerly general council for Exxon Interamerican Inc., a regional office for Exxon Petroleum interests in more than twenty countries in the Caribbean and Central and South American area. Mr. Juncadella helped compile the International Transactions Manual, which is an important publication for the ABA. He also is on the Board of Directors and Vice President of the Argentine/Florida Chamber of Commerce. I would like to present to you with great honor Salvador Juncadella.  
SALVADOR J. JUNCADELLA<sup>17</sup>

Thank you so much. I would like to say a few words about the Inter-American Bar Association and then I am going to present the interesting panel in a simplified manner.

The Inter-American Bar Association was founded more than fifty years ago in Washington, D.C. The purpose of the Association was to promote the development of law in the Americas, but more important than that, an exchange of views, an exchange of ideas and opinions between lawyers in the Americas. The Inter-American Bar has the interesting peculiarity of being composed of over 100 bar associations in this hemisphere, ranging from Canada to Argentina. If we combine the number of lawyers in those associations we have over one million lawyers. The American Bar Association alone has 450,000 members and the Bar Association of Brazil has 350,000 members. More important than mere quantity, is the individual members of the Association which range about 3000 members. These lawyers actually exchange both opinions and ideas.

They are divided into twenty committees of different fields of law, and once a year there is an annual meeting. For one week seminars are carried out on different subjects. The possibilities are great, not only from an educational point of view, but from the point of view of getting acquainted with lawyers from differing countries. Not only from Canada, the United States, and the big South American countries, but even from the small countries in the Caribbean, such as Haiti. It is a tremendous opportunity for everybody. The Inter-American Bar Association is devoted exclusively to matters related to this hemisphere. This is extremely important. I urge you, if you are not a member of the Inter-American Bar Association, to become a member. I think it would be of substantial benefit to you to become a member of the Inter-American Bar Association, not only because of the academic background of the Association, but because of the possibilities of extending your scope and relationship.

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17. Salvador Juncadella is an international consultant for the law firm of Morgan, Lewis, & Bockius in Miami, FL. He is a member of the ABA Section of International Law and Practice and serves as the Vice-Chair for Central America on the Inter-American Law Committee. Mr. Juncadella received his doctor of law from the University of Havana in Cuba.

Now to the final topic of this section. The steering committee selected the subject for this panel, which is an interesting and completely new area of law in Latin America. It concerns the challenge of making new laws in the banking, insurance, and financial services area. In order to make a proper selection we decided that there are four countries which are relevant on this subject. Those countries are Peru, Ecuador, Argentina, and Venezuela. In order to cover the issues related to these matters, we selected four prominent lawyers from those countries.

First, we have Jorge Bustamante from Peru. Next, we have Raul Izurieta from Ecuador. Thirdly, we have Patricia Lopez Aufranc from Buenos Aires, Argentina, who will talk about issues related to Argentina. Finally, Francisco Castillo Garcia will discuss matters related to Venezuela. The first speaker will be Dr. Jorge Bustamante from Lima, Peru.

*A. Country Updates: Peru, Ecuador, Argentina, and Venezuela,  
Addressing the Laws Affecting Banking, Insurance, and Financial  
Institutions*

JORGE BUSTAMANTE<sup>18</sup>

The investment climate in Peru is involved in a dramatic transition from an economy which has been plagued by runaway inflation to a market system which is already yielding encouraging results. Peruvian legislation has been substantially modified by the current Administration as part of an economic modernization program. Due to a fiscal and monetary alternative program, inflation dropped from 7650% in 1990 to less than 40% in 1993. The Peruvian legislation has paved the way for the development of a free market economy, where foreign investment is not discriminated against. The basic principles supporting the modification of Peru's legislation are embraced by laws that grant rights and benefits in favor of foreign investors.

First, the state promotes and guarantees foreign investment in the country in all economic sectors. Reserves in favor of the state have been revoked. The government has an aggressive privatization program: more than 233 state corporations are in the process of being privatized. The law provides that prices will be fixed for the most important state corporations and could be canceled with a minimum payment of 10% cash, the rest going to reduce Peru's public debt. Second, the foreign investor has the same rights and obligations as the national investor, and any discrimination between them is absolutely forbidden. Third, foreign investments made in the country are automatically authorized. Once made, they are registered with the competent national authorities. Fourth, the investor is entitled to transfer abroad the full

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18. Jorge Bustamante is a senior partner with the law firm of Estudio Romero in Lima, Peru.

capital obtained from its investment in the country, with no prior authorization whatsoever. This includes the sale of shares or rights in the full amount of the net dividend or profits obtained from its investment. Fifth, license agreements for the use of technologies, patents, trademarks, and other foreign intangible assets as well as for technical assistance, basic engineering, and management of franchise agreements will automatically be registered upon authorization with the competent authority. Sixth, the investor has the right to use the best exchange rates at the time of carrying out the respective concessions. Seventh, the investor has the right to enter into a contract with the competent authority to guarantee stability as to the tax regime, the free availability of foreign currency, and as to the hiring of workers. Eighth, stability agreements entered into will be enforced until the expiration date and cannot be unilaterally modified by means of law. Ninth, the length of stability agreements will be ten years counted at the deciding date. Any disputes originating therefrom shall be settled by arbitration. State corporations and local governments are authorized to submit all disputes to national or international arbitration. Tenth, the investor shall be entitled to take out insurance, both in the country as well as abroad, to cover non-commercial risks in respect of its investments.

Peru has committed itself before the international community to honor foreign investment. To further this purpose, Peru has entered into the following agreements. First, an agreement with the multi-lateral Investment Guarantee Agency to encourage the flow of investment between member countries. Issue guarantees include car insurance and rate insurance against non-commercial risks with respect to investments and carrying out appropriate activities to promote investments among developing member countries. Second, investment incentive and financial agreements (OPAC) between the United States and Peru relate to any investment insurance and guarantee furnished thereunder. According to this agreement, any dispute between both governments regarding the interpretation or application of the agreement shall be submitted to arbitration. Third, the International Settlement of Investment Disputes (ICSID) provides for the investor an arbitration system for the solution of any dispute without it first being necessary to exhaust the administrative or judicial means. Peru also has entered into several bilateral agreements which contain clauses regarding fair and equitable treatment and non-discrimination. Peru has signed these agreements with Thailand, Switzerland, Korea, the United Kingdom, Northern Ireland, and France, to name just a few.

Also, there are general principles covering banking, financial, and insurance agencies. In addition to the above general principles, loss related to various economic activities embraces the following principle: foreign investment is subject to the same treatment as national capital and public law entities compete under equal conditions with private laws, enterprises, and

entities. The companies of the country's financial system may freely fix the interest rates applicable to the loan and the participants. This is subject in some cases to exceptions, but only in extreme situations. Insurance companies will freely fix their rates and individuals residing in the country may take out insurance and rate insurance abroad. Formal rules are shared by the financial and insurance companies. New companies might be authorized by the superintendency of banks and insurers before they are incorporated and begin operations. This is only for the purpose of incorporation, if some entity decides to share or to buy shares of an existing bank there is no obligation to ask for any authorization. In order to establish a new company, its corporate capital as per its shareholder contributions in cash shall conform to the minimum amount established by law. That amount adds constant value which has to be updated on a quarterly basis according to the national wholesale price index published on a monthly basis by the National Statistics Bureau.

Authorizations to establish banks and financial companies from abroad are required. Banks and financial companies domiciled abroad and planning to establish branches in the country will be open to the public, but must obtain the superintendency's authorization. Once it has been proved that the relevant requirements have been complied with, the superintendent will issue the corresponding resolution authorizing the operation of the company in question. The capital assigned to the branches of the foreign companies must be brought to and registered in the country.

Furthermore, authorizations are needed by the representatives of foreign companies not established in the country. The representatives designated by a bank, a financial company, or a rate insurance company not established in the country must be authorized by the superintendent. This representative shall only maintain commercial relations with: (a) similar companies operating in other countries in order to possibly take foreign trade and provide for its finances; (b) companies interested in buying or selling goods and services in foreign countries; or, (c) potential seekers of foreign trade or capital reserves, banking, financial, and consumer credit. Trade companies shall keep in reserve an amount not smaller than the equivalent of 35% of the capital. The above reserve shall be formed by setting aside on an annual basis not less than 10% of the profits after taxes.

Companies and entities of the country's financial system and their directors and personnel and the superintendent are forbidden under bank secrecy laws from furnishing any information in relation to the deposits kept by their clients. Bank secrecy does not apply in the event that the information is required by the courts or the public prosecutor to fight drug trafficking. Security deposit funds are funds kept with the Central Reserve Bank and aimed at protecting depositors and investors in the companies and entities of the financial system. The superintendent keeps a registration

system called a database that provides information on debtors of the companies and entities of the financial system. This information is available to companies and entities of the financial system and to the Central Reserve Bank. Companies and entities in the financial system are subject to a single minimum reserve of 9% which may consist of money in cash on deposit with the Central Reserve Bank.

To generate profits, commercial banks are involved with foreign exchange concessions (the most important revenue generator for most banks) as well as with other financial services such as leasing, stock brokerage, and share activities. Due to high interest rates for deposits in U.S. dollars, large inflows of foreign currencies have been observed throughout the past year. Legislation is being sought to stimulate and increase competition from foreign financial institutions. Multi-national banks are organized as foreign capital with the aim of promoting and participating in newer types of banking, such as financial investment and business development operations and services and related activities both in the country and abroad.

Corporations are subject to a 30% tax on net profits. However, dividends and any profits to shareholders are tax free. Therefore, there is no remittance tax. Additionally, individuals and corporations obtaining dividends and profits from other corporations are not obliged to compute this in determining their taxable rate.

Peru through its new Constitution and recent laws has relaxed labor regulations. Job stability laws have been practically eliminated. The State only guarantees fair labor practices. Also, employers are now allowed to modify, suspend, and substitute working conditions if necessary to improve production and productivity as needed for the assistance of the company.

FRANCISCO CASTILLO GARCIA<sup>19</sup>

Thank you very much. When I was invited for this conference back in November, I gladly accepted the opportunity to speak about the new banking law in Venezuela. The steering committee of the Florida Bar and this conference had a crystal ball, and they knew this was going to be a hot issue in Venezuela in the following months. I was only going to speak of the new banking law. However, Mr. Jay Malina in his presentation made three comments on the Banco Latino issue, thus there is no way I can avoid that topic. Therefore, I will have a presentation of the new law in light of the Banco Latino issue — how it occurred and probably would not have occurred if the law had been in place earlier.

As you already know, the government intervened with Banco Latino in January of 1994. Banco Latino was the second largest bank in terms of

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19. Francisco Castillo Garcia is a senior partner in the Venezuelan law firm of Bentata, Hoet, & Asociados in Caracas, Venezuela.

deposits in Venezuela. The intervention affects, 5% of the Venezuelan population directly, and probably up to 20% indirectly, so you can imagine the impact of this situation on Venezuelan business and, of course, on the banking industry.

Since the intervention on behalf of Banco Latino, nine other banks are receiving financial support from the FOGALI (the Spanish initials for the fund to guarantee deposits), which is a government fund funded jointly by the government and the banking system. These nine other banks or financial institutions are under very strict supervision programs and are subject to a number of restrictions which are stronger than those governing the rest of the banks. In order to receive the financial support these banks had to offer to FOGALI, further guarantees on assets were needed, thus the shareholders had to pledge more than 51% of their shares.

In fact, the situation of Banco Latino has not come as a surprise to many observers. The banking system had been ill for some time, and many banks were engaging in risky business. Fiscal deficit, inflation, and high interest rates rapidly changed the scope of the banking business in Venezuela. Borrowers were increasingly reluctant and afraid to apply for financing when interest rates were over 70% and inflation was around 35% to 40%, hence this was an obstacle if you had any business and tried to finance it through banking loans. So banks instead of lending money started to change the scope of their business and started, through related companies, to invest directly in projects of different types — real estate, industry, tourism, or whatever seemed an attractive opportunity. Banks, at the same time as they were engaged in these investment related companies, received institutional guarantees, so if the banks started to engage in long term investments, you can imagine the problems they would have if they were receiving short term deposits. Sooner or later they would have a cash flow problem, a liquidity problem, and in the cases of the institutional guarantees they would certainly have losses.

Strong rumors about the Banco Latino started around September of 1993 and within a few months around sixty billion Bolivares were withdrawn from Banco Latino. No bank can withstand a continuous withdrawal of deposits, and Banco Latino was of course no exception to this rule. On January 14, 1994, the bank closed its doors to the public, and of course the intervention was unavoidable. Some consider that the intervention should have been done a lot earlier, but if you analyze the Venezuelan political situation you can see why this did not occur. We had a provisional government since President Perez was removed from office in July of 1993, and the temporary President was not about to take such a strong measure as to intervene with Banco Latino before handing the government over to the new President, Rafael Caldera. However, waiting was no longer possible, and on January 17, 1994 he had to declare the intervention.



There are numerous pathetic stories surrounding Banco Latino. For example, a retired person had his funds in Bonesto, a Bank in Spain that was also intervened by that government, so he withdrew all his funds from Bank Bonesto in December, and, attracted by the interest rates in Banco Latino, deposited everything in Banco Latino and now has no way to take his funds out. Others were offered 100% interest rates not to withdraw their funds in December, and attracted by this offer, they left their money there. In short, because of the ironies of life and the lack of information on the part of the general public, some persons deposited their funds in Banco Latino Caracas and were left with paper from Banco Latino Curaçao which is an offshore entity, which under the previous law was not subject to control by the banking agency in Venezuela.

A lot of legal issues are now being discussed. One of them is the development of a secondary market, which leads to the question: can you sell or assign your paper, your deposits in Banco Latino, to a debtor of the bank so that he can offset that debt and in this way recover part of your funds? The problem is quite complex, and it is not yet regulated or ruled. We hope that the war of the intervention will soon lead to a procedure on how this could be done. In the case of the Banco Latino Curaçao, which is subject to other legislation, this is not possible after the date of intervention in Curaçao, which was January 19, 1994. Actually the bank in Curaçao, which was an offshore entity, had to change its legal status from an offshore entity to a commercial bank and this was done on the same day by the court and then the court immediately declared a moratorium. Today the Banco Latino in Curaçao is also subject to intervention also by the Central Bank of the Netherlands (Antilles), and they have ratified that it is not possible to offset any kind of deposits against debts of the bank if the operations by which you acquired the deposit were executed after January 19, 1994.

We believe that many of the problems we are facing right now would not have occurred if the banking law was in effect sooner. It is sometimes a good experience to grow, and we believe that in the end this situation will have a very positive effect on the banking industry in Venezuela. And probably the new law will also be improved by new regulations. The new law has only been in force less than two months, but you can see already some of the things that will have to be improved, seen in the light of the crisis of Banco Latino.

The law contains many elements. The new law provides transactional freedom, under the previous law banks had a long list of permitted transactions. Now the law allows any activity or business which is compatible with the banking business. At the same time, it establishes prohibitions or limitations. One type of limitations are the general limitations which apply to any kind of bank. Some of them were restrictions or limitations in place before the new law. Now they have been ratified and

codified by the new law. Examples of these restrictions are that a bank may not lend more than 10% of its capital to a single person, to the members of the board of directors, or to shareholders who own more than 10% of the bank.

There also are prohibitions that apply only to certain types of banks. Commercial banks, for example, may not lend funds for a term over three years. Mortgage banks may not receive funds that may be moved with checking accounts or by checks. These limitations apply only to certain types of banks, but in general the new law would establish a complete freedom of any activity that may be compatible with banking activities. This of course puts a stronger burden on the supervisory agency, the agency which will have to ensure that the bank would not engage in risky business and that it will have sufficient capital to respond to its obligations. Under the supervision of the banks, one concept has been introduced by the law which is essential: the concept of financial groups. This concept was not included before and will allow the agency to supervise not only the bank itself, but also companies that are related to the bank by equity participation or board membership or that have any type of control over the bank by agreements over decision making by the bank. This will permit the agency to require a consolidated financial statement of the group and will avoid lending between related companies which was one of the problems that we faced with Banco Latino.

Another issue that will probably now be regulated by the agency, which was not included in the previous law, is what we call in Venezuela the "money desk" or the *mesa dinero*. This money desk is a financial transaction. If you have excess funds you go to the bank and say, "I have these funds I would like to deposit in the bank," instead of receiving the deposit, the bank would say, "Hold on a second, I will find someone else who needs these funds," and will act as an agent to put together the person who needs the funds and the person who has the excess funds. This borrower will issue a draft in favor of the lender. So the bank would not register this in the books as a liability or an asset. This, in the case of Banco Latino, happened in a transaction that covered almost a billion dollars and was practically the same size as the bank, off the records, through the money desk. Some of these funds went to Banco Latino Curaçao. All of this will be regulated by the new law.

One of the aspects that I mentioned before was that the financial support of FOGALI required that shareholders pledge shares to FOGALI for its financial support. This will certainly open new opportunities. One of the main elements of the new law, that delayed the approval of the law for many years, is that it opens the banking system to new foreign investment completely and immediately. Foreign investors now receive equal treatment. A foreign investor has exactly the same opportunities to invest in the banking

industry in Venezuela as a national investor, and will have to comply with exactly the same regulations.

What are the major issues that would be at stake when you ask for an authorization? One would be the capability or the experience of the principal officers and the promoters of the bank in the banking industry. Another factor would be the sufficiency and the origin of the capital contributions. The law puts a strong emphasis in trying to clarify where the funds come from so that we avoid investment in the banking industry of drug money.

Foreign investors may participate in different ways. They can purchase shares of an existing bank or promote a new bank or simply establish a branch. If they decide to promote a new bank and it is a subsidiary of an existing bank abroad, then it will not have to comply with the minimum requirement of ten promoters. However, all banks will be required to have at least seven board members with banking experience, half of which will have to be residents of Venezuela. The banking law provides a lot of informational requirements. A lot of information is required from anyone who invests and purchases shares of a bank, either through the stock market or directly. If the purchase is more than 10% of the bank, then it will have to have approval from the agency. As I said before, growing is not easy, sometimes it hurts, but I believe that this situation with Banco Latino in the end will open new opportunities for the banking industry.

Of the nine banks now in trouble, some of them are known to have been lending to related companies and shareholders for long periods of time — this will have to change. If the measures of financial support for these nine are not successful, the agency will eventually receive all the shares which have been pledged and will have to put the bank up for sale in less than one year.

President Caldera, who has been the President of Venezuela since February 2, 1994, had a very populist message during his campaign. Personally I did not vote for him, and we were all very concerned about what he was going to do because his campaign was mainly directed at what we call the “anti-package.” The “package” was the economic measures that were put into effect by President Perez. During Caldera’s campaign he did not even say what he was going to do, he only said that he would change everything, but he did not say what. In fact, all of major businesses were concerned about the possibility of Caldera winning the election, and yet even though he won the election, the big surprise is that no big changes have been introduced.

He is aware of what the problems are. He has clearly declared that the main problem in Venezuela is the fiscal deficit and he has advocated a strong plan for the reduction of government expenditures. At the same time during his campaign he opposed very strongly the value added tax and told the population that he would eliminate the tax in order to reduce the fiscal

deficit. How could he do that? Once he was in office he clarified more or less what he is going to do. They are going to eliminate the value added tax by changing its name and keeping it on the wholesale level, but not trying to impose it on the retail level. This approach has created a lot of problems with the population because of the lack of knowledge about this tax and how it operates.

At the same time the corporate asset tax also will be kept, another amendment to the income tax law which also created a strong reaction from the business community. They have clarified that this is not to increase the tax rates, but to eliminate the personal deductions which individuals, who were not engaged in business, had a right to. For example, I as an individual, not as a business, have a right to deduct from my taxes my personal telephone bills, the bills for repairs to my car, and a number of deductions that in no other country you will find. So this is a needed reform. This was an extremely popular decision from the Congress two or three years ago to win the sympathy of the population by eliminating taxes which were not at that moment the best of measures.

Also, the Caldera Administration has agreed that they will keep pace on the privatization program. This privatization program includes the oil industry through the so-called strategic associations, which during the campaign they opposed, but now have said that they will open up to even more strategic associations. Finally, he has brought in a team of people that is well respected and known to be honest. An example of this is Gustavo Rosen, who was Minister of Education during the Perez Administration and then was appointed as President of Petroleum of Venezuela (the oil industry holding company). Rosen has now been appointed by Caldera to be the chair of the intervention board of Banco Latino and Rosen has appointed a very active manager to try to solve the crisis of Banco Latino, which, as I said, affects indirectly almost 20% of the Venezuelan population.

As I said before, growing is not easy, sometimes it is difficult, but I have a real positive feeling that in the end the restructuring of the financial sector in Venezuela will have extremely positive effects. Thank you for your attention.

RAUL IZURIETA<sup>20</sup>

Buenos Dias, my speech professor at the University used to tell us that a speaker should take care of little details. He should step forward so people can see him, he should speak loud so people can hear him, and he should speak short so people can tolerate him, and I am going to attempt to do all three.

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20. Raul Izurieta is a lawyer with the Ecuadorian firm of Estudio, Izurieta, Mora, & Bowen and is also the Secretary of the Inter-American Bar Association in Quito, Ecuador.

Ecuador is a country located in the northwest part of South America. It is approximately the same size as the state of Colorado, here in the United States, with a population of eleven million. Fifty-five percent live in the rural areas and 45% in the urban areas. We live under a full democracy; we elect a President every four years as well as a Congress. It is a government that respects human rights, private enterprise, and private ownership. The banking, insurance, and financial institution systems are related. The Ecuadorian banking system is comprised of forty-two consumer, commercial, and foreign banks. All of them are subject to government supervision through the Superintendent of Banks. The Ecuadorian government itself directs five banks and financial institutions in the country. Among them are the Central Bank, which handles the monetary system; the National Bank of Development, which contributes to the agricultural area, to the agri-industry which is the basis of our economy; the Helping Bank which provides funds to poor people, in order that they can build their own houses; and the National Finance Corporation, which is a financing institution that handles most of the international trade for private enterprises, such as the Inter-American Development Bank, the World Bank, and the Bank of the Andean Pact, which are the most influential ways of getting money from abroad.

Most of what has been said from Peru and Venezuela applies to Ecuadorian common law, so I will not repeat some of the things that were already said. I just want to mention that most of the banks are commercial and private. Most of the banks can handle any banking operation, including credits, mortgages, and loans in general. From the external point of view we have banks from the United States such as Citibank, we also have Lloyds Bank, and Holland Union Bank, which demonstrates that any bank can come and establish its services in Ecuador.

The existing financial resources for commercial development are provided largely by government sponsored banks, as well as the commercial banks. The rate of loans is just about the same as the rate of inflation, which as of today is around 29%. It is our purpose to reduce it to 20% by the end of 1994. The resources are often taken in the form of credit guarantees, as well as direct short and medium loans with reasonable terms. These terms can go up to seven years, and in some cases they can be extended farther. The public financial institutions do not grant direct credits, but fund the private institutions who supervise the dispersal of the monies. The National Finance Corporation, which is a governmental corporation, offers long term financing by means of private banks for the promotion and development of investment, industry, and exports. The National Finance Corporation also coordinates the credit guarantees on loans provided by other public and private institutions.

As of today, foreign investment is fully open to banking, insurance, and financing institutions. The investors, like Ecuadorian citizens, have to pay

a 25% fixed rate tax on profits made during the fiscal year, which starts January 1 and ends on December 31. There is, as in all countries, a scale of exemptions for paying the tax.

The merger of a portion of a private bank with a finance company is supported by the following measures. First, tax exemption for three years, following the formation of a new institution by merger. Second, tax exemption for incorporation expenses and legal costs that are a result of the merger. At this time, as is happening in most Latin American countries, we are aware of the need for foreign investment. This also applies for banking and financial institutions. Ecuador considers foreign investment essential to its growth and development. Therefore, all laws in the country have been changed recently to encourage foreign investment.

It is proper to say that foreign investment is treated as national, with all the guarantees and necessary legal backing. In relation to the United States, three months ago the government signed a treaty whereby all foreign investment from the United States is guaranteed against nationalization, acts of terrorism, or any threat to the investment itself. Of course, it does not guarantee the profits, but it guarantees the security of the investment. Limitations on foreign investment are only for reasons of national security. There are limitations on foreign investments in the media, such as radio, newspapers, and television. There is no limitation on expatriation of capital or profits. The treaty with the United States, which I just mentioned, establishes that any type of dispute between the investor and the country must be solved by arbitration. This is a guarantee that many investors requested. We also are trying to establish what is called the "Maquila System" which has to do with financing. This allows the investor from abroad, the U.S. investor, for instance, to bring raw materials into the country, make them into a finished product in Ecuador and then re-export them back to the United States for sale. We also have the concept of free zones for the benefit of investors from abroad.

On December 31, 1993, Ecuador enacted the law on modernization of the State. This law allows the government to delegate its obligations in connection with public services to the private sector. Privatization can be made through a total or partial capitalization of a corporation, leasing, concessions of use, public service, public works, license, franchise, or any other judicial figure existing under the Ecuadorian laws including sale, transforming, uniting, or liquidating State owned corporations, or by using any other mode which can be established by the Ecuadorian President. All of these forms also can be used for contracting studies, designs, constructions, maintenance, or exportation of public works. Investors are being invited to participate in these different forms of privatization of public companies in Ecuador. Telecommunications, airlines, ships, hotels, sugar refineries, plants, lands, buildings, ports, toll services, custom services, and

electricity are among the companies slated for privatization. The law allows for investment in all types of privatization in the country.

In the same spirit, Ecuador has opened the seventh round of negotiations for exploring and exporting oil and gas (as Ecuador used to be one of the OPEC countries) in the Amazonian Zone as well as in the shore and offshore areas of our coast. There is a new procedure for contracts and concessions whereby the operator, who is the investor, owns the exploration and exportation of the zone won in these negotiations. The documents for participating in this round are available now and can be presented until May 31, 1994.

Thus, Ecuador is open for foreign investment in banking, insurance, and financial institutions. It is also open for foreign investment in every other field, with the exception of national security and the media. So I am inviting you all to think of Ecuador as a possible country for investment for your clients.

SALVADOR JUNCADELLA

Thank you, Raul, for your first class presentation, and now we finish the presentation of this panel with Argentina and for that purpose we have selected a prominent lawyer from Argentina. The prominent lawyer is Patricia Lopez Aufranc.

PATRICIA LOPEZ AUFRANC<sup>21</sup>

Thank you very much. It is really tough to be the fourth speaker to review the changes in an area where the changes have been in most cases along the same lines. How can I distinguish Argentina from the Bustamante and Castillo presentations? Well to start with I will tell you that I endorse 100% of what they say. Argentina has done the same. How can I distinguish it? We have been doing it for four years. They are starting privatization, we have almost completed it. We have privatized the telephone company, the gas supply company, the water works, and the oil industries. In addition, you will realize the scope of the reform when you realize that we have given these industries to our arch enemies of the past. We have given the power plants that serve Buenos Aires to the Chileans and YPF, the oil company to the world through an international 3.2 billion offering which was the deal of the year in all financial publications. So we are ahead of them only in how far we have gone with the reforms. But apart from that let me review the reforms very briefly, comparing them with what my colleagues have said.

In regard to financial institutions, there are two main areas which are worth noting. One is the redefined role of the Central Bank and the other is

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the strengthening of the entire system. In Argentina, for many years, the Central Bank was the arm that implemented the monetary policy of the government. That meant printing money whenever the government needed it, whether there was any backup for that money or not. The present Administration enacted one of the cornerstones of their economic program, which is the so-called convertibility law. This law is revolutionary in the sense that it ties up the Central Bank. The law says that in order to print money, the Central Bank has to have, at the rate of one to one, one dollar for every peso it prints. This means that if the government needs money, it will have to get the reserves somehow to print it. By this very clever mechanism the responsibility for the monetary control, to some extent, has been shifted from the Executive to Congress. When the governors, for example, of the different states knock on the door of the Ministry of the Economy asking for money because their states are having difficulties, the Minister can say, "Go to your Congressmen, I cannot do it, my hands are tied. I cannot issue print money unless I have this backup." This really has been the cornerstone of stability through the reinforced powers given to the Central Bank.

With respect to the supervision and strengthening of the market, as in the case of our neighboring countries, the reserve requirements and credit limits have been reinforced so that the mechanism shows the real strength of the bank. In the past, minimum capital used to be a fixed amount which would be indexed pursuant to inflation, but it did not have a direct relationship to how good or how strong a bank was. Nowadays, they have applied rules similar to other Latin American countries. When they differ from those rules it is because they are either tougher or stricter or because through a complex formula they take into account the interest rates that the banks charge on their assets. That means that if the bank charges high interest rates, they have to have more capital, because their portfolio is considered riskier. There also were new rules regarding the concentration of risk and rules which would put a lower ceiling on the maximum financial facilities a bank can grant to a single client. The new rules consider a group of companies as a single client and, therefore, try to have banks spread the risk more.

How has banking changed before and after this reform? The change is very significant. The banking business in the highly inflationary context that Argentina had has nothing to do with banking in a more stable economy. Argentina did not have long term financing, banks received deposits and granted loans for very short terms. When I say short terms I mean that it was difficult for companies to get loans for over thirty days. So they had to roll over the loans indefinitely. You can imagine, if any of you are lawyers really connected to business, how difficult it is to finance a project with terms that are stated every thirty days, and in addition to that, how difficult it is to run a financial system which is restated every seven days.

Let me give you some figures. As of June 1989, during the birth of



hyper-inflation, deposits with fixed terms of less than fourteen days accounted for 89.3% of total deposits, while deposits of more than thirty days accounted for 4.43%. This means that the key word was volatility. They were there, they were not there, depending on how the government counts; they had a code, they did not have a code. Then the deposits flew from the system. In that scenario, certain large companies could resort to international financing provided they were willing to run exchange risks. I tell you that in the past you really had to be a gambler to run that risk. Since 1982, when the debt crisis came, even that source dried up completely.

Also, in the past foreign trade was highly regulated and it meant that you needed approval for everything. Not only were imports regulated, but the types of financing that you could obtain were highly regulated. It was compulsory for exporters to repatriate the proceeds of their exports through the bank and sell them to the Central Bank. The foreign currency used to “belong” to the Central Bank and the exporters could not dispose of it. In many cases the rate that was paid for this foreign currency resulting from their exports was much lower than the black market or free rate, implying a loss. To complicate the system, at some stages of our history up to ten different exchange rates co-existed depending on whether you were exporting wheat, or importing capital assets, or whiskey, or whatever. It was a very complicated system.

Since the reforms the banking industry has changed completely. These reforms were aimed at de-regulation, increasing competition, lowering costs, lowering interests, and increasing access to credit. What *are* the most distinctive aspects of this reform over the last year? One of them is the creation of certificates of deposit, checking accounts, and saving accounts, all denominated in U.S. dollars. The banks can now offer these to their clients whether they are Argentineans or foreigners. In addition to that, reserve requirements have been reduced or equalized so that a very important dollar market coupling the peso market has developed.

Let me review these changes in a little more detail. As I mentioned earlier, in the past foreign trade was highly regulated. You had to sell the dollars to the Central Bank and you were limited in the type of financing you could obtain. All this generated an enormous amount of red tape and was one of the sources of what street jargon used to call “Argentine costs.” All those unnecessary costs were making Argentine products less competitive. Nowadays, imports and exports are almost free with a very few exceptions, like quotas for one or two products. Exporters are totally free to do whatever they want with the proceeds of their exports; there is no need to repatriate the funds, they can dispose of them freely.

Since 1989 there have been no exchange controls, meaning anybody can walk into a bank and wire funds anywhere without even the need to identify himself. Banks have “know your customer” policies and that kind of thing

for money laundering issues, but from the standpoint of the Central Bank, there is no need. You can bring your money in and you will be able to take your money out. In addition, in 1989, Congress passed a law prohibiting the government from interfering in this system and specifying that the terms agreed to in the dollar market between the banks and their clients will not be altered by the government. We all know that there is really no limitation on what a government can do as far as legislation is concerned. Nevertheless, I think that, from a political standpoint, the fact that Congress has passed this law without any noise demonstrates that it has committed itself to non-interference.

That law was passed in 1989. In 1991 the convertibility law, that I referred to earlier, was passed. This law established full convertibility, so that the Central Bank is by law obligated to sell dollars on demand to whoever requests them. This has made the Argentinean dollar market (the local market of dollars within the Argentine banking system) grow enormously.

The relative importance of U.S. dollar deposits as compared to peso deposits has increased enormously. As of January 1994, the average daily balance of U.S. dollar deposits in the daily financial system was 18.5 billion dollars and the average daily balance of peso deposits was twenty-two billion dollars. They are almost the same. This represents 16% of the TBI and it is expected that it may double in two years. This also generates sources of funds that did not previously exist.

In the peso system a number of reforms also have been introduced to liberalize the system. For example, reforms have been introduced to abrogate a certain number of taxes which were very unclear, like taxes on banks' debits and checks. In addition, the minimum term of term deposits (which, as I mentioned, used to be seven days), has been raised to thirty days. There are no deposits below thirty days. The market has reacted without problems. People have not withdrawn their deposits, which reflects an increase — a significant increase — in confidence.

Another market that has developed enormously is the mortgage and consumer loan business. In the past, there was no consumer financing in Argentina, and there was no mortgage financing. Whenever I tell my American friends that in order to buy my apartment I had to literally come with two hundred thousand dollars, one bill on top of the other, count the bills and hand them over to the owner, they just cannot believe me. "Are you rich?" "No, I had to work hard." So, the mortgage loan business is something that did not exist. Now it exists.

The source of the funds for the loan business are: (1) the Argen dollar market which I just mentioned; (2) lines from abroad; and, (3) beginning a short time ago, negotiable obligations. Negotiable obligations are corporate bonds, which have tax incentives. These bonds have no reserve re-

quirements, so they have been a good source of funds for those banks that can get into the international market when the local market is still limited. Argentina also has signed a major agreement and a lot of promotion agreements similar to those that Peru has signed. About fifteen of the investment promotion agreements in total.

In the area of securities, there also have been enormous changes in banking because the securities market has been booming. There is an increasing amount of activity and opportunities for banks. Argentina does not have the distinction between investment banks and commercial banks. Thus, banks have been able to take a lot of opportunities in this area, in both the sections of debt and equities, resulting from the recently privatized companies.

The reforms concerning insurance have been of similar scope and similar depth. The reforms redefined the role of the State and strengthened the market. The redefined role of the State is, basically, that the State has walked away from the industry. We demolished the State monopoly on reinsurance. Now reinsurance is totally free. A person seeking insurance can take his business wherever he chooses. Also, there are no restrictions on the setting up of companies. As far as reenforcing the market is concerned, we have taken measures to increase transparency and increase the flow of information so that companies can act as debtors. Now companies have a more solid capital base to respond to their obligations.

In conclusion, I would say that all this stabilization has brought an enormous challenge to the business community. The challenge is to learn to live without inflation, with open competition, and with the State withdrawing from the scene. The government has, up until now, been very successful economically. These reforms have been carried out by a democratic government that enjoys broad support. Most of all, during the past four years, the government has not hesitated or backtracked. This really shows clear goals and determination.

*B. Planning Strategic Alliances in Latin America: Joint Ventures  
(Private and Governmental) Wholly-Owned Entities  
and Other Alternative Structures*

LUIS ZUÑIGA<sup>22</sup>

My talk today has to do with strategic alliances and joint ventures in Latin America. I will focus on the opportunities and on the types of models that I generally utilize to develop businesses, not just in Latin America, but throughout the world. I am not going to speak a lot about the mechanics of

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how to put together joint ventures, because I believe that is a topic in which you are all very well versed. So I will try to emphasize the opportunities and why Latin America is an exciting market. I hope I am not the first speaker in this conference that will tell you that it is indeed the greatest market in the world today in which to develop a new business.

I will try to follow an outline. First, I will give you an idea of the market profile from our viewpoint. I also will give you some idea of the quantitative data on the information technology market, just to give you some basis from which we say that it is an important market for investment. Then I will discuss models and the different types of criteria that we utilize to decide which type of model best suits a particular country in a given time. Then I will conclude.

Strategic alliances in Latin America are certainly attractive and I am sure you have heard a lot about privatization, about modernization, and about adoption of free market policies. Those are the main reasons why the Latin America market has flip-flopped from the 1980s into the 1990s. In the 1980s investing in Latin America was a problem. Foreign investors really got a black eye in terms of investments and many foreign companies really got burned when they invested in Latin America. In the 1990s, however, the whole tendency has been towards a free market economy, towards open markets, and towards modernization and democracy. This has really made a big difference. Also, the U.S. and European markets have turned soft over the past five years, making Latin America an even more exciting place to take some risks and grow.

Latin America is, I believe, now firmly on the side of open and free markets. Some of you might say, "Brazil is not really an open and free market," and I will not argue with you. In many ways it is not. It is open to the extent that it allows, at least from my vantage point, the importation of all kinds of products of high technology. On the other hand, it is not quite free because it still keeps very high tariff levels and a very protectionist attitude toward local Brazilian companies. However, that in itself is an opportunity. It is a good country in which to establish a joint venture precisely for that reason. It does pay to have a partner that is local, and it does pay to have an association that is viewed by the Brazilian government as being local. Therefore an investor in a joint venture can take advantage of lower tariffs and make his products or services more competitive in the market.

In the rest of Latin America, the barriers are coming down. They are coming down fast and that really represents a great opportunity for consumers: lower prices and the search for high quality. Latin American consumers are rapidly becoming just as selective in terms of low price and high quality as are American consumers. This is a boom for many companies that are in the consumer market. It is also a great opportunity for

investors. There is a lot of purchasing power in Latin America, despite what you have heard Mr. Ross Perot say about Mexico. There is a tremendous amount of purchasing power in Mexico. There is a tremendous amount of purchasing power elsewhere in Central and South America. Companies have really got to realize that and move fast to get there.

In terms of which markets are open, from my own perspective (I am sure that some of you might argue with why I picked these countries) the high technology markets are: Argentina, Chile, Colombia, Mexico, Peru, and Venezuela. These markets represent good investment opportunities right now. Patricia Lopez Aufranc spoke about what is going on in Argentina. I think Chile, of course, was a pace setter. Both Argentina and Chile had been the leaders of free market economy and policies ten years ago. However in the last two years Argentina has done remarkably well. Mexico is also a very attractive market. Peru recently has become a very attractive market as well. You have to look past what you read in the press in the United States. You really have to look a little deeper. There are a lot of opportunities there.

As to where you might find these opportunities, well, local companies are now very keen on restructuring to be competitive. They know that protectionism is dead. They have to be good. They have to be efficient. They have to become part of a free market economy. Oftentimes, in order to really catch up with the new market trend, the local companies have to import some of the "know-how" from the outside. So there are opportunities for U.S. and multi-national corporations to really engage with local corporations that need the "know-how" to become competitive quickly.

There are a number of modernization programs and many governments have given those programs a very high priority. In many cases, the governments want to privatize some publicly-held companies. A good case in point was the banking system in Mexico a couple of years ago, and there are many other examples. So there are very good opportunities there. Multi-national corporations are eager to try to grow their business and eager to look for markets that have potential growth and are fairly stable. These corporations now look at Latin America today with a different perspective than they did five or six years ago.

I will now give you some examples of where these privatization programs are going in many of the countries I already mentioned and in some others as well. Additionally, infrastructure in many of these countries is being overhauled completely. First, oil and gas companies are being modernized in all of the countries. Ecuador was here earlier talking about some of the work they are doing in the oil and gas industries. There is also Venezuela, Colombia, Brazil, and even Mexico. In Mexico, they talk about oil as a *patrimonia nationale*. The fact of the matter, however, is that the Mexican government and PEMEX are actively engaged, with multi-national

corporations, in trying to figure out the best way to increase production, gain better methods of going to market with their raw materials, and adding to the petrochemical industry. The same is true in Venezuela. I am sure the same is true in Colombia and other countries. So there are lots of opportunities in the oil and gas arena.

Second, telecommunications from Argentina to Mexico, is undergoing a tremendous upheaval. In every country you visit, the infrastructure around telecommunications is being modernized. There are many joint ventures going on today. General Telephone and Electronics is in Venezuela and Argentina. Mexico is now talking about instituting a second long distance company and is openly talking about competition between two long distance companies in the country. That is creating a lot of opportunity for the MCI's, the AT&T's, and all of the Bell companies to get in and take part in the market.

Third, as to the airlines, Iberia Airlines has invested in Argentina and Venezuela. Some of those investments perhaps have not been as productive as they would have liked, but the fact of the matter is that there is tremendous opportunity there. The utilities are the same way.

In the banking sector, I mentioned briefly the privatization that went on in Mexico a couple of years ago. This is an area where the high technology companies took full advantage. Mexico needed to privatize the banking system, because the banking system was quite antiquated. The bankers realized that for them to compete with the Citicorps and the Chase Manhattan of the world, that were eager to establish beachheads in Mexico City, they would have to come up to speed quickly. There was a tremendous undertaking in investments as the Mexican banks privatized. As you know by now, many of these banks were sold to Mexican investors. As a result, the banking system in Mexico is quite productive. It is well put together and they continue to make investments to become even more competitive. This happened in only two and a half years. So there are many joint ventures in place, there are many joint ventures in process, and I am sure there are many more to come. It is an exciting area of the world in which to do business.

Let us turn now to what I am most familiar with, the information technology market. According to statistics from International Data Corporation, in fiscal year 1993 the local market for information technology in Latin America was approximately seven billion dollars. Approximately 46% of that business is in Brazil. That is why Brazil is so important, in spite of all the problems that we may mention. Argentina, Mexico, Venezuela, Colombia, and Brazil, together take about 85% of the total information technology market in Latin America. International Data Corporation is predicting between 14% to 16% growth per year for the next five years. That is exciting. If you talk about 14% growth year over year, which is the chart that I have here, by 1998 that market will be approximately 13 1/2

billion dollars. That is an exciting market.

You can see that some of the players are now becoming more important. Brazil, in terms of overall marketshare, will drop down by five percentage points, but that is still 41% of 13 1/2 billion dollars, a sizeable investment. Mexico is really a tremendous opportunity. Venezuela is staying at 7% market share, but as in the previous example, it is 7% of 13 1/2 billion instead of 7% of seven billion. That is real growth. Argentina is going from 7% to 8%. These are exciting numbers. If you look at Brazil's domestic market, you are looking at a 3.2 billion dollar market. In the case of Mexico, exports are significant. Overall the Mexican market is 2.4 billion. They consume 1.6 billion, which means that they are exporting 800 million dollars a year.

Prior to the North American Free Trade Agreement (NAFTA) many companies had set up manufacturing operations in Mexico simply because of the degree of local content that was required to do business in that country. With the opening of the markets local content is no longer an issue. In fact, you do not really have to manufacture in Mexico, but there are some very sound reasons for investing in that market under the free trade agreement. Digital Equipment Corporation is investing heavily in increasing its manufacturing capability in Mexico, for two reasons. First, because it is sound business. Second, it is a good first step to export products into Venezuela and other countries as free trade agreements throughout South and Central American countries become more prevalent. This is a good market, followed by Argentina, Venezuela, Colombia, and Chile. As I said, those countries account for about 85% of the market.

Having quantified a bit, at least a segment of the market that I am familiar with, I would like to talk about the models that are utilized to go to market. Certainly this applies to Latin America, but it also applies to Asia and other parts of the world. Many companies take independent distributors as a first step to go into a market. Many companies use it as the only way of going to market. Later I will talk a little bit about the criteria that we use to decide which type of model fits any given country at any given time. Independent distributors are certainly one of the most popular ways of going to market in Latin America. Another model is the joint venture with a local partner or partners. Also, there is the wholly owned subsidiary which is the third model. There are many other models but these are the three most popular, at least in my industry.

In terms of the selection criteria that one utilizes to decide how to go to market, one should look at the products and or services to be marketed. That an important criteria. The degree of sophistication of a product or service will very often determine what type of model you select. Independent distributors are good for certain types of products and services but they are not the most efficient if your product or service is highly sophisticated and

requires high levels of training or high levels of capital investments. One should also consider the degree of risk that a company is willing to assume as it enters the market and the commitment to the market. Many companies today are reading the *WALL STREET JOURNAL*, *BUSINESS WEEK*, and so forth, and they are all reading how Latin America is a hot market. They would like to be there. However, they frankly do not understand the market, they have no idea how to go to market, I am not sure that they really want to commit any heavy capital investments to that market.

In that sense, an independent distributor could be the best way for them to try to get a taste of that market. Another criteria is how much a company is willing to invest or is capable of investing. The payback expectation can vary. Some companies talk in terms of three or six months, other companies talk in terms of three or five years. The payback expectation to a certain extent determines the selection criteria and what model to utilize. Another criteria is the market maturity relative to the products or services that one is trying to develop or promote in the market.

Let us now analyze the independent distributors. There is an upside and there is a downside. The upside of going to market with an independent distributor is that it gives a foreign company immediate access to a local market. The distributor, I am assuming that one chooses a reputable one, knows the market well. It has the credibility and the commitment of that market and can really provide a fast return on sales to a company at a fairly low risk. There is limited capital investment. Again, depending a lot on the type of products or services that one is trying to develop in a country the independent distributor model requires only a low investment. In many cases, for a product which is not highly sophisticated, the investment of the manufacturer is limited to marketing brochures, a fairly superficially trained sales force for the distributor, some marketing support, and perhaps some technical support at the beginning. Many companies are attracted to this model. On the one side it seems like you are looking at a big market and there may be a way of getting access to that market with a fairly limited capital investment.

The downside of independent distributors is that you have to settle for less. In a market that is growing, a distributor is not necessarily going to give you full access to the market. For many reasons not necessarily having to do with the quality of the distributor, the distributor, being an independent company, is generally not committed 100% to one product or to one manufacturer. They are looking at many, so they have a tendency to split their attention and split their resources. They look at a market in a time slice basis and, therefore, you may suffer. On the other hand, remember, there is a low risk from your capital investments so there are tradeoffs.

There is, of course, limited access to markets because of what I have just described. You are not really selling directly to the consumer or to the end



user, thus have a limited influence on what the end user may choose to do with your product or service. I have found, and this is from personal experience, that in terms of highly sophisticated products or services a distributor is many times not the optimum way of going to market. This is simply because it requires commitment, capital investment, a lot of training, a lot of technical know-how, and oftentimes a distributor truly looks at return on sales in a matter of months. Few distributors are talking about investing for years ahead. They like to see their return on sales in a matter of 60, 90, or 120 days. On the other hand, a good example of products that have been highly successfully processed through distributors is automotive parts. Everywhere in the world you will see automotive parts being sold through distributors and dealers; those kinds of products have a natural affinity to independent distributor networks.

Let us talk a little bit about joint ventures. Joint ventures in my view are an exciting way of doing business. It really promotes the ability of a company to gain a marketshare quickly and also promotes, the quality of many corporations. Latin America has been successful with joint ventures with local companies and joint ventures are certainly a way for companies to continue to do business in this part of the world. A reputable local partner will add value immediately. You will have a channel distribution network, the local partner has a local company image that can help you immediately, and the local partner is willing to share in the capital investment.

In some countries, like Brazil, having a local partner is more than just having a partner. It is a key ingredient because of local content laws. In Brazil if you have a local joint venture, and we have one in the personal computer business which is highly successful, it really pays to have a local partner. The joint venture is seen as a Brazilian national company. There is a board of directors which manages the operations of the company. The resulting revenues are not consolidated on our side, but are treated as local revenues. The company quite effectively promotes our products as a joint venture product.

In Mexico joint ventures used to be a good way to enter into the market because of local content laws. Today with the NAFTA agreement, and even before NAFTA, Mexico has opened up considerably and there is not that much need for joint ventures. But even where local content is not a requirement, a joint venture with a reputable local partner is an excellent way of going to market in South America.

How does a foreigner add value to the joint venture? Well, often the foreign partner is supplying the technology, the products, or the services. He is also providing the training, the technical support, and, to a certain degree, the marketing strategy. Now marketing is a big word and it means different things to different professions. In the high technology industry, having a marketing strategy that differentiates a company from another is essential,

because, just to use a simple example, personal computers today are all basically the same. So what you are looking for is ways of differentiating your products from others. Oftentimes, although I am not suggesting that we do this by trick, marketing provides a differentiator. It gives a customer or consumer an idea of what the added value of a product is vis-à-vis the competition. Thus, marketing is a key ingredient in going to market and developing a business. A multi-national hopefully will add its image and its expertise to the joint venture, so both the local partner and hopefully the foreign partner will win.

Here is an example of a joint venture that I am personally familiar with. In the 1980s I was doing a lot of work in Asia. I was there with Gould Electronics and we had tremendous technology, but we had a very difficult time entering the Japanese market. As Bill Clinton is finding out, it is not easy to enter the Japanese market, even though you can have all kinds of logical reasons for doing so.

What we ended up doing at Gould was to associate ourselves with a company that was well known in Japan, the Nikon Mining Corporation. Nikon Mining was the leading producer of non-porous metals in Japan. It had nothing to do with high technology. Gould Electronics was a leading supplier of products such as the electronic foil that is used in the development of printed circuit boards. Nikon Mining actually gave us the entry into the Japanese market. It gave us immediate credibility in the marketplace. Japanese companies in Japan make a big difference. In contrast, U.S. companies in the United States sometimes make a difference but we do not really look at the label from companies to decide to buy the product. In contrast, the Japanese do.

The consumer in Japan is certainly a second priority to the manufacturer, so that worked out very well. It took two years to do a joint venture in Japan, something that I thought would take only three months to accomplish. However, once we were able to agree, the joint venture became an overnight success, mainly because the credibility in the market was immediately gained by the relationship with Nikon Mining.

Finally, a little on the wholly-owned subsidiary. This is oftentimes the result of an evolution from an independent distributor or a joint venture. This is an area where the legal profession helps tremendously. The legal contract, no matter what kind of an agreement you set out to do, must contain clauses that enable the foreign partner to go alone in the market when he chooses to do so. Many disputes can be avoided if the legal contract is clear on how the company can buy options from the local partner and move on to a higher percentage of ownership.

In connection with disputes, another point to consider is items like jurisdiction, which sometimes becomes a real problem when you are trying to settle with a local partner. There are several reasons for choosing a

wholly owned subsidiary. If the market gross prospects and the sophistication of your product are high and the country is politically and economically stable, a wholly owned subsidiary makes a tremendous amount of sense. It also makes sense because some companies like to protect their technology. They are frankly not comfortable with turning over their technology to a local partner.

There is also the case of company culture. I will give you an example of this. IBM traditionally followed the wholly owned subsidiary model. I guess you can say that IBM never found a country it did not like to put a subsidiary in. They were everywhere with wholly owned subsidiaries.

UNISYS, Hewlett-Packard, and Digital kind of followed the combination of the three models that I spoke about. In some countries they have distributors, in some countries they have joint ventures. In major countries they have wholly owned subsidiaries. Newcomers to the market in Latin America, like COMPAQ, are also following a similar type of tradition. They have subsidiaries in some countries and they are graduating to distributors elsewhere.

In conclusion, no matter what model you choose, Latin America is fertile ground for strategic alliances in the 1990s. South Florida and the legal profession are really in an excellent place at this time to take full benefit of this opportunity. We have the location and we have the cultural affinity. We also have the expertise. The legal profession can really take full advantage of the opportunities and assist corporations that are trying to develop businesses in Latin America. The North American Free Trade Agreement, I believe, will be a catalyst for growth and true economic integration. I believe, in conclusion, that the Americas is a most exciting region of the world for profitable growth and we should take full advantage of it.

#### QUESTION AND ANSWER

QUESTION: I would like to know to what extent the tax laws in a country influence the decision about what form of business to choose?

ANSWER: They are very important and to a great extent they do have an impact on decisions. I believe that, for instance, in Brazil, being a Brazilian national company has a very positive implication on tax laws and that is one of the reasons why there are so many joint ventures in Brazil. I should add also that we have a wholly owned subsidiary in Brazil so we operate under two types of entities there. However, taxes are definitely an important criteria.

QUESTION: Do you think customers would react differently to different types of foreign investment?

ANSWER: The joint venture provides more of a commitment to the country and to the market than an independent distributor. Many times it

depends, of course, on the type of products or services you are providing. Oftentimes a customer will be more comfortable doing business with a company that is in the country via a joint venture because it knows the company has a long-term commitment to the country. The customer knows the company has made an effective investment, that it has local technical support provided by the joint venture.

In contrast, an independent distributor is at an arm's length relationship. The customer, or the user, knows that they have to go to that distributor to get support, and the distributor is an independent enterprise and is not part of the company that is supplying the product or service. Thus, that is one critical item in differentiating one over the other.

QUESTION: In joint ventures is it important to work with companies that operate in the same area?

ANSWER: Yes. It is best if the company you are associating yourself with has an affinity for the market and the products that you are trying to promote. It is not to say that it will not work otherwise. Such an example is the Japanese model where Nikon Mining and Gould got together and Nikon had no idea about high technology, nevertheless it worked out well. However, generally speaking I think it is faster and more efficient if the company you are associating yourself with has already made a commitment to the marketplace. That way they are willing to invest further into that market.

### C. *Labor Market Issues: Dealing with the Hurdles and Possible Complications*

MARK ZELEK<sup>23</sup>

I am going to focus on Mexican labor law because, since NAFTA's passage, this is where the action is, at least in my office. Mexico is a good place to start, because Mexico is the first country in the world to constitutionally recognize labor rights, so many other Latin American countries base their labor laws on the Mexican labor laws. If you have an understanding of Mexican labor law, it will probably give you a good idea of what the laws are in other countries.

I do not know how many of you saw in the paper a little while ago, but two complaints have been filed with the National Administrative Office (NAO). The NAO is the body which was set up to handle complaints filed under the NAFTA side agreement. These complaints were filed by two major unions, the Teamsters and the Electrical Workers, against Honeywell and General Electric. The unions claim that Honeywell and General Electric fired certain workers because they were involved in union organizing

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activities.

Honeywell and General Electric have vigorously denied those charges, but the significance of it, from our perspective, is that anything done in Mexico is going to be under a microscope. The U.S. unions are looking for ways to get back at President Clinton for his support of NAFTA. The unions are also trying to show that everything they said about the abuse of labor rights is correct. Therefore, it is going to be especially critical over the next few years that parties considering doing business or already doing business in Mexico have a good knowledge of Mexican labor laws.

There are really just two points that I would like you to remember about Mexican labor law. The first is the principle of job stability and the second is the principle of no unilateral changes. If you understand those two basic principles, then the rest of Mexican labor law makes a lot of sense. Because of these two principles, Mexican labor law is very different from U.S. labor law.

Let us first talk about job stability. As you all know, in the United States the general rule is employment at will. This means that a worker can be terminated or an employee can quit at any time for any reason, or for no reason at all. In Mexico, on the other hand, under the principle of job stability, it is presumed that a worker has his or her job for as long as he or she wants. Because of this rule you cannot fire a worker in Mexico unless you can show just cause.

It is very difficult for an employer to establish just cause, the reasons for just cause being set out in the Mexican labor law. There are high level misdeeds by the employee, like stealing from the employer or abusing the employer at his home. If you terminate a worker and they want to contest their termination, which is almost inevitable, they will take you to the labor and conciliation board in Mexico where the case will be decided.

I have been to these labor and conciliation boards and they are very different from the court system we have here in the United States. Basically, what happens is the representative of the employee and the representative of the employer stand in front of a little window. On the other side of that window is a woman with a manual typewriter in front of her who takes down what both parties say. Your case is going to depend on what that person takes down, you never see a judge and no one ever assesses the credibility of the evidence. The typist takes the report back to a room where there is a man or a woman who reviews it and then makes a determination whether the termination was for just cause. There are subsequent levels of appeal, but an employer never has an opportunity to present evidence in the way that it is done in the United States. The whole system is extremely pro-employee.

Unless you have a situation where the employee shot at his supervisor or something along those lines, you are probably not going to establish just cause. If you do not establish just cause, you have to pay the employee back

pay, which you also generally have to provide under U.S. labor laws. However, there is no set-off for interim earnings by the employee. In addition to the back pay, you must to pay three months' wages to the employee, twenty days' salary for each year that person worked, and another twelve days' salary for each year the person worked, limited only by the minimum wage. Thus, as you can see, it can be very expensive to terminate an employee in Mexico.

One thing that I would like to point out is, as a U.S. labor practitioner, most of our work today is with employment discrimination laws. In Mexico there are some employment discrimination laws on the books but they are incredibly unimportant because everybody has just cause protection. Therefore, there is no need for someone who fits within some kind of protected class to file on the basis of a discrimination law. They would simply do what everybody else does, they would go down to the conciliation and arbitration board and litigate their just cause case.

The second point which I mentioned earlier is the principle of no unilateral changes. As you know, in the United States it is very rare for someone to have an employment contract. In Mexico, on the other hand, an employment contract is statutorily required for all workers. Further, no changes can be made in that contract, indefinitely, without the approval of the worker. Thus, it is very important when you are preparing contracts to be used in Mexico that you take into account all types of eventualities.

Just as an example, if you have commission workers, you might want to take into account that sales might boom and you might want to reduce the commission rate. You need to account for that in the initial contract, because if you do not, there is no way to change it without the worker's agreement.

Also, if you are a U.S. company taking over a Mexican business, there is a principle of substitution of employer which means that you are stuck with the contracts that your predecessor entered into. If you are considering taking over an operation in Mexico you would want to look carefully at the contractual provisions that the predecessor company had in place.

Another thing is that in the United States fringe benefits are generally up to the employer. For instance, there is no obligation in Florida that you give anyone vacation time or holidays. In Mexico, on the other hand, most fringe benefits are statutorily required and they include things such as year-end bonuses. Employers have to pay workers, prior to December 20 of each year, at least fifteen days' salary for a year-end bonus.

Employers also are required to give employees vacation time starting at six days a year during the first year of employment, with regular increases on a fixed scale. While people are on vacation, employers are required not only to pay them, but are also required to pay them a 25% bonus to give them extra spending money. Another big problem is that employers are required under the law to have profit sharing, which means that they are

required to pay 10% of pre-tax profits to all of the workers other than the chief executive officers. There are exceptions to that rule, such as companies in their first year of business. Nevertheless, it is a principle that businesses need to take into account.

The bottom line on doing business in Mexico, which I think more and more companies are going to do over the next three years, is that it is a difficult place to do business. In all his discussions on NAFTA, Ross Perot talked about the great sucking sound because wage rates in Mexico were on the average 1/7 of those in the United States. However, businesses considering operating in Mexico also need to take into account the very strict and demanding Mexican labor laws before you just run down there and do business.

MICHAEL A. BROMBERG<sup>24</sup>

Several years ago the State of Florida had an advertising slogan which said: "The rules are different here." That is a nice advertising slogan for Florida but it is an absolute iron-clad requirement when you consider labor issues in Latin America. The rules are different from what we are used to in the United States and woe be unto you who does not adapt to those changes. There are very rigid rules and requirements affecting how one treats employees in Latin America. The employer does not have the flexibility that one ordinarily finds in the United States. The rules are fairly clear, but are fairly strict and they favor the worker. In planning one's operations it is very important to learn the rules in advance, to know them thoroughly, and conduct business accordingly. It is expensive but you can keep yourself out of trouble.

I was asked to come up this morning as an executive working in-house for a corporation which has handled both the legal issues and the personnel issues. I was asked to come up and give some stories to bring this topic to light. I am not quite sure why anybody would choose me to do that because *my* employer does not have labor problems — we never get into trouble. Fortunately, I have a friend who has told me of some instances where there might have been some minor problems, and so I am going to tell you my friend's stories. If it should turn out that some of these stories might have happened with my company, they were before I got there. Really I cannot be blamed for any of these types of problems. I will apologize in advance to those of you whose interest is purely in exporting or operating through distributors because this whole topic does not really apply to you but you can sit back smugly and laugh at those of us who suffer through the problems which are similar to those encountered by my friend.

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It is key to note that it is very difficult to get rid of a worker for just cause. As a result, what you are mostly faced with are rules that clearly specify what you want to do if you want to terminate a worker without just cause in each country, and there are clear formulas and rules which apply to the payment of indemnities. By and large you can sit down and run your calculator and figure out how much it is going to cost you to get rid of a worker. It is usually beneficial to do a cost analysis if you want to reduce the size of your operation or if there is a particular worker that you want to get rid of. This alleviates the problems that you face in trying to confront the procedures for reduction with just cause, such as reinstatement and backpay. You can avoid all that by saying, "Here is your indemnity check, go away." However, even knowing that there are these formulas and how to apply them, it is never quite that simple. An example is Venezuela.

In Venezuela what you have to know is that if you have ever worked for a company in Venezuela and you have a career with another company which is related — a subsidiary, an affiliate, or a parent company — outside of Venezuela, the Venezuelan courts are going to say that you have continued your labor relationship with that Venezuelan company and you will be able to claim Venezuelan rights upon your departure. Venezuelan rights are some of the most beneficial for the employee in all of Latin America. The basic rule in Venezuela is that if you quit you get one month's salary for each year's service, and if you get laid off you get two months' salary for each year of service based on your last month's salary. It is very lucrative to lose your job in Venezuela.

To give one example, my friend had an executive who started his career in Venezuela, was transferred subsequently to the United States and a number of other locations, and then started a long international career. Eventually he decided that the United States was his career path. He obtained a green card and became a permanent resident, became a permanent employee on the U.S. payroll with pension rights, health insurance, and so forth in the United States. At one point in time, he was transferred back to Venezuela as a U.S. employee, not as a local Venezuelan hire. In this company you maintain your status in your home country when you are on a temporary assignment. Problems arise when the employee decides to quit while in Venezuela and wants all of his thirty-five years of service calculated in Venezuela for indemnities. Since he is in Venezuela on an assignment package he is getting all sorts of extra benefits, foreign service premiums and the like, for serving in Venezuela. Under Venezuelan law anything that he receives has a value and that value is used to calculate termination indemnities. Therefore, he wants to receive all of his overseas benefits from the United States, including the value of his car, and the benefits he is receiving in Venezuela calculated at one to two months per year of service. And you know what? He gets it. So you have got to be very careful on these things.



Another example is Argentina, Argentinean sales people. U.S. corporations have a global compensation structure for how they compensate sales people for sales. Many companies use commission. This company does not use commission. They have a similar system that provides some form of variable compensation based on results, but it is not a strict flat commission. Argentine law for some peculiar reason has a provision that says sales people must be paid commissions. If you do not pay a commission, they have a claim against the company. Obviously U.S. corporations say that they have a global policy not to pay commissions in Argentina and elsewhere. They wish to have a corporate system. However, they cannot impose that, so they have to sit down and negotiate with each and every employee and say, "Will you accept this?" They also have to show them why it is worth their while to accept not getting a commission in order to get them to sign a contract that provides a different compensation system. Still, they are exposed to claims under this rule.

When you have an employee who says, "Guess what? I do not accept it," then what do you do? Maybe you say they have to accept it. At that point, they say, "Aah! You violated my labor contract. Guess what? It is indemnities time. It is the big Bonanza, I am going home rich." I cannot begin to tell you just how true this is.

The management of the Argentine company decided to fight this gentlemen and said, "O.K., we are going to fight and we are not paying you your indemnities. You can go to court and fight us." This was in the period when inflation in Argentina was running at 200% a month. It turned out that in calculation of indemnities in this type of case you go back a month, so you are already always a month behind. The value of his claim tripled immediately, and it went on from there with interest rates, inflation, indexation, adjustments, and the exchange rate increases. The value of that fellow's claim ultimately increased by at least ten times.

It turns out he also claimed his departure came just one month after he had made his largest sale ever. Now, for calculating his compensation they had to look to his last month's pay, where he had a gigantic commission check. The value of his claim by the time he was finished was, in his estimation, somewhere in the neighborhood of five million dollars. Think about that. A salesman who had a salary of maybe twenty thousand dollars making a claim for termination indemnities of five million dollars. He is doing quite well with it I may add.

The problem is that because of inflation and adjustments, even if the company were to absolutely prevail, the salesman would obtain \$500,000. That is simply the way the rules are applied, so you better know your rules before you start and you better not try to play any games or fool around. Get good advice, do it straight, take your lumps and go on or do not go into business in Latin America or hire employees.

You have to recall that, unlike the United States, you cannot impose changes in Latin America. Similarly, you have to be aware that in many countries you cannot reduce pay or benefits, once granted, unless you can somehow negotiate with an employee to do it, and good luck with that. Where does this situation run into problems? We have seen a very good example in Mexico. Benefits, once granted, cannot be taken away. So when times are good, in order to hang on to employees, people add benefits. We have done the same thing here in the United States: when times are plush bonuses get bigger or they throw in company cars or something like that. When times get bad in the United States, however, you say, "Guys, we have to share the pain. We need 15% across the board cuts." In Mexico, try and take those cars away. Once they have been granted, you cannot do it. If you want to get rid of a Mexican worker's car there is a check involved. You have to calculate termination indemnities for at least the value of that benefit. It is payday again. All of this shows that you have to be very careful in terms of how you operate in Latin America. That message is now coming through.

#### QUESTION AND ANSWER

**QUESTION:** Would a Latin American country consider independent contractors as employees?

**ANSWER:** I spoke at the ABA Convention out in Denver, Colorado last month and there were three questions from lawyers who apparently had been advising their clients on these things. They were surprised when I said that their independent contractors would probably be found to be employees. So you have to be careful.

**QUESTION:** Are there any exemptions for executive employees to the basic rule that terminated employees are to be paid for all their wages and benefits?

**ANSWER:** No, they would be entitled to payment as well. The only exemption, or rather the major exemption, for executive employees is profit sharing, at least in Mexico.

**QUESTION:** Would you recommend that companies just pay these termination benefits without litigating them?

**ANSWER:** In the example of the five million dollar case, if, instead of fighting, they had calculated the rate of that day, they probably could have reached an agreement at a much more reasonable level and avoided the mark up. You have to remember, although the economic climate in most Latin American countries is much more stable today, things still accelerate far faster than they do in the United States and there are still some countries that are out of control. You are just better off taking your lumps quickly and getting on with life.

ANSWER: What I think you need to do when drafting the contract is keep in mind the five million dollar enchilada and think of all the potentialities that can take place and preserve your rights to change things. One problem you have in Latin American countries is that there is a dearth of high level executives. Unfortunately, you have to pay these executives a lot of money to get them in the door because they are extremely marketable. It is not unusual for a top notch executive in Mexico to change jobs every year. I have reviewed some of their contracts, and they are phenomenal. I have heard of a contract where an individual could make millions of dollars in bonuses, because if the company made 1% of their target, the executive would make 1% of his bonus. Even if he did not perform well, there was still a big bonus written into the contract for him. That is just what companies need to do to attract top notch executives.

ANSWER: Let me just say one other thing, just to re-emphasize that point. In a place like Mexico, the cost of top executives is so high that what many companies are finding is that the cost of general managers puts the general manager at a pay level among the five highest paid people in the company.

ANSWER: Also, you want to be careful that your executives are excluded from your U.S. pension plan. Otherwise, they can collect indemnities in Mexico, then file a claim as an employee under your pension plan and collect retirement benefits twice. You want to anticipate every eventuality and look at all the documents.

QUESTION: Is it possible for an employee to cash out in one of these Latin American countries and then return and cash out again?

ANSWER: Yes, but I will give you the same story I told you about the Venezuelan executive, who did indeed cash out when he left Venezuela. Then he came back. Credit is given for what you have paid previously in terms of indemnities, but given inflation and everything else, what had been a one or two hundred thousand dollar payout on his first departure, in historical currency, was worth fifteen thousand dollars set off against his final check. He in fact collected that amount twice. So you could say you are correct. You want to cash them out when they leave, and be careful not to send them back to the same place.

ANSWER: One other thing that a lot of companies do is to set aside money on an accrued basis while people are working, and to take into account all these indemnities at the end. This makes it so that they are not hit with the big number when they have no money set aside.

QUESTION: Is there any way a company can transfer an employee to Venezuela, but still be protected from having to pay these huge benefits if the employee quits or is terminated?

ANSWER: If someone is going to Venezuela, they are going to end up in one way, shape, or form on the payroll of Venezuela, if for no other reason

than for tax purposes. So you have got somebody in Venezuela and the government wants their social security taxes and everything else. Thus, they end up at least nominally on your payroll. What you want to do is to build a fence around them so that there is an agreement that before they leave they are coming out of the country and returning to their home base. In other words, an agreement that they cut off the relationship with the foreign assignment before they can quit.

QUESTION: Can an employee waive these statutory employment rights?

ANSWER: No, you cannot waive your rights. That is the general rule.

QUESTION: Would the Venezuelan courts only count an employee's work in Venezuela and exclude time worked abroad?

ANSWER: The answer is no, because the Venezuelan courts will indeed recognize full career service no matter where the employee has been. That was our problem with the guy after thirty-five years. Comparatively little of his service was in Venezuela, but he got credit for all that service as if he had been in Venezuela the full time.

QUESTION: In the example of the thirty-five year long employee, can you give us a little background on his job, where he was first hired, and so forth?

ANSWER: He was hired as an office boy. He had a thirty-five year career. He was hired in Venezuela.

QUESTION: Would a U.S. citizen, hired in the United States, but transferred to Venezuela have a choice of using Venezuela's employment laws?

ANSWER: To my knowledge, the Venezuelan courts have not ruled on what would happen if somebody was truly a U.S. citizen who was temporarily there and then tried to take advantage of Venezuela's laws. Apparently that case has not been reported on. My best guess is that the U.S. employee would have a good chance of prevailing.

QUESTION: This five million dollar Venezuela example does not seem to be typical of all of Latin America, since employment laws differ drastically between countries. What are your comments on this observation?

ANSWER: That is clearly the most exaggerated example I have ever seen. But you are absolutely correct that the rules are different in each country. There is no general rule that we are giving here, other than a general sense to be cautious about it. The best advice is that you need to know the rules in each country in which you are operating, because the rules are different in each country.

I would like to agree with you on something else as well. When a U.S. company looks at these termination indemnities, it is difficult to fathom why they should pay a large lump sum of money, even if it is not an exaggerated amount like we have been talking about. It is worth noting that in the United States we are accustomed to having pension rights. Pension rights are not well established throughout Latin America, although we are beginning to see

that change. Chile has good pension rights, Peru is committed to introducing new legislation, and Argentina is beginning to provide for private pensions. In Colombia, you are also beginning to see pension rights. In the United States, on the other hand, most people who leave their job at the end of their career have some safety net from their employer. Quite frequently, that is not the case in Latin America.

QUESTION: I believe that with time and greater economic integration, employment laws in the Americas will become more and more similar. Are you in agreement with this?

ANSWER: I agree with you. I think as free trade grows in this hemisphere you are going to see a leveling of the laws. That was the experience in the European Community and I think that both the United States and Latin American will change to be a bit more protective of employees over time from the business point of view.

#### IV. SIMULTANEOUS BREAK-OUT SESSION

##### A. *Financing Latin American Business Ventures: U.S. and International Agencies*

FERNANDO PELAEZ<sup>25</sup>

I am going to refer to the pragmatic and practical experiences of financing in Latin America, focusing on my experience in Venezuela. I will start by making some comments on the different sources of financing and basically giving you some history. In the 1970s, different sorts of financing available to develop industrial infrastructure in Latin America were extremely common. All of us were fully aware that capital was flowing to the main countries in Latin America to finance industrial development and the purchase of capital goods. This policy of financing without much analysis, coupled with the excess capital in the world in the 1970s due to oil prices, forced many Latin American countries to reschedule their debt. They did so mostly with banks and official institutions in America, Europe, and Asia, particularly Japan. Thus, in the 1980s, all of us in one way or another were heavily involved in the rescheduling of the public and private debt.

Nowadays, in Latin American countries, we are seeing that financing is once again flowing. However, this time there is a different approach. This new approach is great because it means that banks and official institutions are taking the experiences of the 1970s into consideration. Once again in Venezuela we are seeing financial institutions and government agencies take a very active role on project financing. This is a result of the continuous growth of our industries in some sectors — but note that financing comes

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