Peru Faces U.S. Action

Seizures Could Invoke Financial Sanctions

12/1/68

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LIMA, Nov. 30—A dispute between the United States and Peru is ticking toward an explosion that could confront the incoming Nixon Administration with its first big crisis in Latin America.

Underlying the controversy is Peru's recent action in expropriating the principal assets of the American-owned International Petroleum Co. (IPC).

This has triggered a complex chain of events that involves far more than the status of a single oil company. If allowed to go unchecked, it could lead this Andean country of 12 million people into the throes of a major economic and political upheaval.

As the situation stands, Washington sooner or later will find itself obliged by U.S. law to apply certain financial sanctions against Peru.

Among these penalties would be suspension of Peru's share of the U.S. sugar quota. This would mean the almost certain destruction of the local sugar industry—an important component of the Peruvian economy—and deal a staggering new blow to a country whose finances already are in precarious shape.

Nor is the matter likely to end there. The strongly nationalistic government of President Juan Velasco Alvardo is known to contain powerful elements who advocate retaliating against a cutoff of the sugar quota by imposing new pressures on the substantial U.S. business interests here.

Specifically, these forces are understood to be arguing for retaliatory expropriation of U.S. holdings in Peru's pivotal copper mining industry. Should that happen the effect would be to open up a Pandora's box unlike anything seen in Latin America since Fidel Castro's

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purge of U.S. interests in Cuba during the early 1960s.

Threat to Credit

Such a move would destroy Peru's credit and investment standing with the international financial community, cripple the country's ability to exploit its mining resources and plunge the economy into chaos.

What would happen then is anyone's guess. But more than a few people here predict a wave of national unrest verging on anarchy and civil war or a turn toward the Communist bloc for the financial support necessary to weather the loss of traditional sources of capital and credit.

This grim prospect is still far from becoming a reality. But, as of now, all parties to the dispute seem locked into inflexible positions that prevent them from finding grounds for an accommodation.

Dispute Over Title

At the root of this situation is the decades-old resentment among Peruvian nationalists of the special ownership title rights and tax status held by IPC over an oil field in northern Peru. For the past five years, this resentment had embroiled IPC, a subsidiary of Standard Oil of New Jersey, in a running feud with Peruvian officialdom.

Last August, the government of civilian President Fernando Belaunde Terry reached an agreement with IPC under which the company agreed to surrender its claim to the disputed field. However ,the agreement immediately came under fire from nationalists who charged that the concessions made by Belaunde in exchange represented a betrayal of the national interest.

On Oct. 3, the armed forces, using the IPC issue as its pretext, overthrew Belaunde and replaced him with an all-military government headed by Velasco, the army commander. The new regime immediately announced its devotion to "nationalistic principles," and, six days later, it summarily seized the IPC installations on the disputed field and the company's adjacent refinery at Talara.

Big Tax Debt Alleged

In announcing the expropriation, the regime said compensation for the seized assets would be computed in accordance with debts allegedly owed by IPC for back taxes and illegal enrichment. Since the regime contends that these debts amount to $974 million, the implication (actively encouraged by many ranking regime figures in their public utterances) has been that IPC cannot expect a penny in payment for its lost property.

But the company points out that the legality of its special status had been confirmed by international arbitration. It therefore charges that the expropriation was a violation of international law and that it is entitled to compensation for the depreciated value of its lost assets.

This dealock has now directly involved the U.S. government because of the so-called Hickenlooper amendments to the U.S. foreign aid and sugar amendment acts. These provide for the cutoff of direct U.S. financial aid and sugar quota benefits to any government expropriating property belonging to U.S. citizens or corporations without making prompt and adequate compensation.

Aid at Low Ebb

Since a succession of previous difficulties had reduced direct U.S. aid to Peru to a rather low ebb, the first of these provisions is not expected to have much impact on the dispute. The sugar quota, though, is something else again.

Sugar is one of Peru's most important crops, annually reaching about 800, 000 tons. Of this amount, about 300,000 tons is consumed domestically, and the balance is sold abroad, most of it to the United States under Peru's share of the U.S. sugar quota.

On Nov. 19, for example, Secretary of Agriculture Orville Freeman announced that Peru's tentative quota for 1969 would be 354,253 tons. Normally that amount could be expected to increase substantially as quota readjustments are made throughout the year (Peru began 1968 with an initial quota of 345,417 tons but will end the year with actual sales to the United States of around 493,000 tons).

The advantage to Peru of being able to sell almost all of its exportable sugar surplus to the United States is underscored by the spread between the premium U.S. quote price (currently about 6.5 cents a pound) and the depressed world market price (now 1.75 cents). In short, Peru earns approximately $35 million a year more by selling the bulk of its sugar under the U.S. quota rather than on the open world market.

Threat to Industry

In the view of most economic observers here, the loss of this windfall would drive many Peruvian growers and refiners out of business and virtually wreck the industry. At the very least, it would cause widespread unemployment, drive up the price of sugar for the domestic Peruvian consumer and create a demand for the financially hard-pressed Velasco government to spend money it doesn't have on subsidizing the industry.

Two weeks ago, the U.S. Embassy here quietly handed the Velasco government a note affirming that the United States recognizes Peru's right to expropriate property under its sovereignty. But, the note also said, the U.S. Government considers that such expropriations carry with them the responsibility for prompt and adequate compensation and that Washington reserves the right to make "diplomatic representations" in such cases.

The Hickenlooper amendments were not mentioned in the note. However, the reference to "diplomatic representations" is known to have been intended as a reminder of their provisions and a warning to the Velasco regime of the potential consequences involved in an intransigent attitude toward compensating IPC.

No Choice Seen

The State Department is understood to be taking the position that the language in the applicable U.S. laws is so explicit that Washington has no choice other than to apply the Hickenlooper sanctions if Peru fails to reach a satisfactory resolútion of its dispute with IPC.

As spelled out by the amendments, these sanctions are supposed to go into effect six months from the date of the actual expropriation. In the case of IPC, this theoretically means that a continued impasse would confront Peru with the loss of its U.S. aid and sugar quota next April.

Privately, however, U.S. officials concede that the language of the amendments would allow the Nixon Administration some discretion in postponing application of the sanctions if it decided that the matter was still under negotiation at the end of the six-month period.

Power Limited

At the same time, though, these officials stress that there are short and distinct limits to this discretionary power. Although there are no real precedents (the Hickenlooper amendments have only been applied once previously), the prevailing legal view seems to be that the U.S. Administration could decide for diplomatic reasons to delay indefinitely imposition of the sanctions.

As of now, this relative rigidity in the U.S. position is being matched by the Peruvians. The U.S. note, which was kept secret by the regime for almost two weeks, is known to have provoked some stormy and emotional reactions within the Peruvian government.

The Cabinet is believed to contain a moderate faction that favors making peace with IPC in order to avoid new difficulties for the country's already troubled financial situation. However, this group is counterbalanced by a nationalistic faction which believes that any backing down over IPC would undermine the basis for the October coup and the rationale of the regime's existence.

Reprisal Threatened

To this group, the threat of Hickenlooper sanctions represents a U.S. attempt to interfere in Peru's internal sovereignty, and its members argue that such pressures should not be allowed to go unchallenged. Well-informed political sources here sum up the nationalists' attitude by quoting a remark that reportedly has been repeated in government circles with great frequency the past few days: "If they take away the sugar quota, we take Toquepala."

This is a reference to the Toquepala copper deposit—the biggest mining operation and the largest single source of U.S. investment in Peru. The Toquepala concession is held by Southern Peru Copper Corp., one of the U.S. consortiums that dominate the mining sector of the economy.

However, the hint of reprisals against the seemingly vulnerable American mining companies overlooks the fact that this is a road that could cost Peru dearly. To escape from its current financial difficulties, Peru must greatly increase its exports, and increased copper production offers its only sustained hope of achieving this end.

But, expanded copper mining activity requires both outlays of capital and applications of technical expertise far in excess of what Peru can generate internally. For the Velasco government to retaliate against the United States by expropriating U.S. copper interests would be somewhat akin to economic suicide.

Talk Persists

Yet, the talk about "taking Toquepala" continues unabated in many quarters of the Peruvian government and armed forces. Political sources give several explanations of the reason.

Some of the generals, they say, are so inexperienced in diplomatic and economic matters that they simply cannot comprehend the potential consequences of such an act. Others regard the dispute as one involving fundamental considerations of sovereignity and national honor and feel that the regime cannot back down, whatever the damage to the economy.

Still others seem to have a somewhat fuzzy idea that Peru, which long had a close political and economic relationship with the United

States, can begin the old cold war neutralist game of playing the super-powers off against each other.

Many Red Missions

The recent heavy traffic here in missions from Eastern European Communist countries seeking diplomatic and trade relations with Peru lends some surface credence to this suspicion. However, there is no real evidence that the Velasco regime regards these negotiations as anything but an opportunity for some main chance explorations or that it plans to follow the example of Cuba and mortgage the Peruvian economy to the Communist countries.

Despite all the tough talk going on, the regime seems to be taking pains to keep its public relations with the United States punctiously correct.

On Thursday, Foreign Minister Edgardo Mercada Jarrin finally revealed the existence of the U.S. note and made public his reply to U.S. Ambassador J. Wesley Jones.

Reply Revealed

In his answer, Mercado sarcastically inquired why the United States was so concerned about a company "that maintains itself in a country other than your own." (IPC originally was a Canadian firm and still lists itself as incorporated in Toronto, although more than 90 per cent of its shares are controlled by Jersey Standard Oil).

But Mercado also said the government was evaluating the worth of the expropriated IPC assets and pointed out that IPC is now exercising its "full freedom and right to defend its interests through the legal remedies offered by the judicial power."

This has prompted some speculation that the government might be preparing to unbend a little from its former unyielding stance.

Since the coup the Peruvian judiciary has been excessively responsive to the Velasco government's wishes. Most prominent lawyers here privately admit that IPC has little hope of getting a fair hearing from the Peruvian courts.

For the present, at least, the Velasco government seems to be standing pat on its contention that the IPC controversy is closed.

Meanwhile, Peru and the United States appear to be moving closer and closer to a confrontation whose effects will be felt in every corner of Latin America.