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LEGAL AND ECONOMIC STATUS OF FOREIGN INVESTMENTS IN SELECTED COUNTRIES OF LATIN AMERICA

Prepared by the Secretariat

POLICIES AFFECTING FOREIGN INVESTMENTS IN COLOMBIA

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INTRODUCTION

Foreign direct investments are of considerable importance in certain branches of the Colombian economy. Foreign-owned enterprises account for all the production of petroleum, more than half the output of gold, the bulk of the production and all the export of bananas, and most of the insurance business.

The United States accounts for about four-fifths of total foreign direct investments. United States direct investments were valued at $118 million in 1943, of which almost two-thirds represented investments in the petroleum industry. The distribution of the investments by industries is shown in Table 1.

Table 1

United States direct investments in Colombia by industries, 31 May 1943

(In millions of United States dollars)

Manufacturing	5.8
Mining and smelting	4.7
Petroleum production	75.5
Public utilities and transportation	17.7
Agriculture	1.9
Trade	6.3
Finance	1.5
Miscellaneous	4.3
Total	117.7

Source: United States Treasury Department, Census of American-Owned Assets in Foreign Countries, (1947), page 70.

The inflow of United States capital for direct investment in the post-war period has been of limited importance. The net inflow in the years 1945-1948 was $32 million, of which only $7 million was

/invested

invested in 1947 and 1948. Most of the inflow represented additional investments in the petroleum industry.

The income from United States direct investments in Colombia was $4.5 million in 1947,[1/] or about 3.1 per cent of the value of the investments, compared with almost 12 per cent earned by United States direct investments in Latin America as a whole. The low figure in Colombia is due to the fact that the petroleum investments yield much less than such investments elsewhere in Latin America.[2/]

British direct investments in Colombia are small compared to those of United States nationals. The nominal value of Colombian securities, exclusive of government bonds, traded on the London Stock Exchage was £3.5 million in 1943 and £3.2 million in 1947.[3/] More than half of the total consists of railway securities. Other important British investments are in petroleum and mining. The

1/ Excluding reinvested earnings of subsidiaries, which amounted to only $2.7 million in 1945 and $1.3 million in 1946 (see United States Department of Commerce, The Balance of International Payments of the United States, 1946-1948. 1950, page 262).

2/ The ratio of total earnings, including reinvested earnings of subsidiaries, to invested capital of United States petroleum enterprises in Latin America as a whole was 25.2 per cent in 1947.

3/ South American Journal (London), 24 April 1948, page 212. These estimates are not directly comparable with those of United States direct investments, since they represent nominal values (The United States figures represent book values) and include portfolio investments. They may include some securities held by other than British nationals; on the other hand they probably exclude certain closely-held investments not traded on the Exchange, such as those in petroleum.

/Colombian

Colombian government was authorized in 1945 to undertake negotiations for the purchase of the remaining important British-owned railway. The yield of British investments compares favourably with that on United States holdings. In 1947 the yield was 3.0 per cent on railway securities and 6.5 per cent on investments in other industries.

The total external public debt of Colombia amounted to about $184 million at the end of 1949. Most of this consisted of privately-held dollar bonds, amounting to some $153 million. The balance comprised $22.3 million lent by the United States Export-Import Bank, and pound sterling bonds equivalent to $8.7 million.

Borrowing in foreign capital markets by the national government and other public authorities in Colombia occurred largely during the late 1920's. Total external debt rose from about $23 million at the end of 1923 to approximately $200 million by the end of 1928. Colombia defaulted on service of this debt from 1931 to 1933 when pressure on the balance of payments resulted from the world depression.

/Partial

Partial service was maintained on some of the bond issues until 1941, when the first step toward permanent readjustment was taken. From 1935 to 1941 inclusive only $2.5 million was paid on external debt service, compared with contractual requirements of $133 million. Since 1941 debt adjustments have been made of all the defaulted issues of the national government as well as of other public authorities. The last of these adjustments, affecting some $73 million of bonds of local governments, was made late in 1949. Under these settlements, new bonds were in most cases exchanged for the equivalent nominal value of old bonds, and a portion of the interest in arrears was funded.

A considerable amount of the $153 million of outstanding dollar bonds has been repatriated. Only $70.1 million were held in the United States at the end of 1948. The market value of these bonds, $33.9 million, was less than half their nominal value.[1/]

Loans received by Colombia from the United States Export-Import Bank from 1941 to the end of 1949 amounted to $52 million, of which about $15 million was granted since the end of the war. The balance of credits remaining to be disbursed by the end of 1949 was $17.4 million. In August 1949 the International Bank for Reconstruction and Development granted Colombia a loan of $5 million to finance the import of agricultural machinery. In addition the International Bank has at present under consideration applications for loans for the financing of several hydro-electric projects.

1/ United States Department of Commerce, op. cit., page 268.

I. GENERAL CONTROLS

A. Entry and legal status of foreign enterprises

With certain minor exceptions, Colombian law does not specifically restrict foreign ownership of business enterprises. The exceptions relate to air transport, coastwise shipping and frontier land. At least 51 per cent of the shares of air transport companies must be owned by Colombian nationals or by enterprises controlled by such nationals.[1/] Coastwise shipping is limited to vessels owned by Colombian nationals or by companies domiciled in Colombian with a maximum of 40 per cent stock ownership by aliens.[2/] Temporary exemptions from this limitation may be granted if national companies do not maintain adequate shipping services. For security reasons, public lands situated within two kilometres of the coast or land frontiers may be allotted only to native-born Colombians and may not be transferred to foreigners under any form of title.

Although no substantial statutory limitations are imposed on the entry of foreign capital, permission is required from the exchange control authorities before capital, whether in the form of foreign exchange or equipment, may be brought into the country. The regulations provide that foreign capital must be invested in an "agricultural, commercial, or industrial operation" of benefit to the Colombian economy, as determined by the Ministry of National Economy (Resolution No.175 of 20 August 1947). Thus each foreign investment is subject to

1/ Law No. 89 of 1938

2/ Law of 30 December 1936

/scrutiny

scrutiny on an individual basis.

Foreign investors may operate either by forming local companies or by registering agencies or branches of companies organized abroad. In either case, certain formalities must be complied with, but once they have been fulfilled, permission to operate is granted automatically. As of 31 May 1943, branches of foreign companies accounted for about 78 per cent, and locally organized corporations for 22 per cent, of United States direct investments in Colombia.[1/]

The Colombian Constitution guarantees the inviolability of private property. Private property may be expropriated only for reasons of public welfare and subject to prior indemnification.[2/] However, the legislature "may, for reasons of equity, determine the cases in which there may be no indemnification, through a favourable vote of the absolute majority of the members of both Houses". The President-elect, scheduled to take office in August 1950, has indicate in a special interview that one of his first steps upon assuming office will be to clarify the constitutional question of expropriation without prior indemnification.[3/]

A recent instance of expropriation of a foreign-owned enterprise occurred in 1947, when electric distribution facilities of a subsidiary of the American and Foreign Power Company were expropriated by the municipality of Cali. The provisional indemnification originally granted was considerably less than the subsidiary's valuation of its

1/ United States Treasury Department, op. cit., page 72.

2/ Article 30, as amended in 1936

3/ See New York Times, 27 December 1949.

/properties

properties. In mid-1949, however, the company reported that an "amicable settlement" of its claim had been arranged. Prior to the final settlement, permission had been granted by the exchange control authorities for transfer of the provisional amount received by the company to the extent of one-half within one year and the balance over a period of six years.[1/]

Under Colombian law the final authority for the judicial review of disputes arising from contracts between private enterprises and the government is the Supreme Court of Colombia. This is of importance in relation to foreign investment in that it applies to concession contracts relating to the exploitation of minerals, including petroleum. It may be observed that it is on the basis of similar legislation that several Latin American countries have entered reservations to certain provisions in the draft Economic Agreement of Bogotá (signed at the Ninth International Conference of American States in May 1948), relating to the principles of compensation to be applied in the event of expropriation of foreign investments.

B. Transfer of earnings and capital

Control over transactions in foreign exchange has been in effect in Colombia since 1931. It has been applied with varying degress of strictness depending upon the extent of balance of payments difficulties. During the greater part of the post-war period, imports have exceeded exports, the balance of payments has been under strain, and stringent

1/ American and Foreign Power Company, Twenty-Fifth Annual Report, (New York: 1948), page 9; and Financial Report, 30 June 1949, page 3.

/exchange

exchange controls applied.

The present system of exchange control, in effect since December 1948,[1/] involves fixed official rates (buying rate 1.95 and selling rate 1.96 pesos to $1) and a fluctuating rate (about 2.872 pesos to $1 at the end of 1949) determined in a free market. With a view to restricting certain types of imports, taxes are imposed on almost all purchases of foreign exchange, varying between 4 and 34 per cent, with the lower rates applying to the more "essential" transactions. Most foreign funds derived from exports, from the inflow of foreign capital or otherwise entering the country, must be sold to the exchange control authorities at the official rate. However, the proceeds of certain categories of exports, for example gold, and, in certain special conditions, incoming foreign capital may be converted at the free market rate yielding higher peso equivalents. Foreign mining and petroleum companies are partly exempt from the provisions requiring the surrender of foreign exchange to the authorities. Foreign petroleum companies may retain abroad between 75 and 100 per cent of the proceeds of exports of petroleum depending on the state of the balance of payments. Foreign mining companies may retain abroad up to 60 per cent of the proceeds of exports of gold, platinum and silver.

As already observed, the import of capital is subject to prior approval by the exchange control authorities. Provided such capital is registered upon entry, income from it may be remitted abroad six months after the date of entry, "subject to availability of exchange".

1/ Law No. 90 of 16 December 1948, which affected a devaluation of slightly more than 10 per cent.

/After five years

After five years permission may be given to transfer the principal if the business in which the investment was made has been liquidated or if the tranfer "will not affect the stability of the enterprise". The transfer will be effected at the official rate if the incoming capital was originally converted at that rate, and is subject to an exchange tax of 4 per cent. The exchange tax applicable to the most essential private imports is 10 per cent. Exchange regulations accord a high priority to the transfer of earnings on registered capital, which is second only to service on the external debt. In practise however, this high priority is reported not to have been consistently granted. Thus it is reported that in November 1949 "exchange releases for commercial transactions were relatively prompt... but applications for remittances for dividends, profits and royalties and for the re-exportation of capital remained blocked.[1/]

The transfer of earnings and capital of non-registered foreign investments and of all capital which entered the country before 1935 may be made only at the "free rate" of exchange. At present, however, it is reported that no foreign exchange is being made available for the transfer abroad of capital invested prior to February 1935. The above exchange control regulations do not apply to the transfer of earnings of the foreign mining and petroleum companies whose exchange transactions are largely independent of the exchange control system.

1/ United States Department of Commerce, Foreign Commerce Weekly, 23 January 1950, page 17. This was reported at a time when import licensing policies were being liberalized as a result of some improvement in the foreign exchange position.

/Furthermore

Furthermore, these companies are exempt from the requirement that capital may not be repatriated until five years after its entry.

In June 1949 the Minister of Finance announced that new regulations governing capital imports and remittances abroad on account of foreign capital would be presented for consideration by the Congress.[1/] It may be assumed that the new regulations would be aimed at encouraging foreign investment by providing more liberal transfer provisions. The introduction of new regulations has been delayed, however, apparently as a result of a difference of views within the country concerning the extent of facilities to be accorded to foreign capital. In particular, concern has been expressed by local industrialists who fear competition from foreign investors and by others on the ground that the import of foreign capital might be offset by "mortgaging" the future development of the economy.[2/] In April 1950, however, the Minister of Finance announced that immediate steps would be taken to revise the existing exchange control regulations so as to guarantee the transfer of the profits and capital of foreign investments without limit, and without any delay after the entry of the capital, as presently required.[3/]

The recent restrictions on remittances of the earnings and capital of foreign investments have been due to the persistent strain on the Colombian balance of payments since the end of the war. Gold and

1/ Ibid., 15 August 1949, page 14.

2/ See editorial in El Tiempo, (Bogotá), 26 June 1949.

3/ See statement by Finance Minister Jaramillo-Ocampo, as reported in the New York Times, 6 April 1950.

/foreign

foreign exchange reserves declined from $177 million at the end of 1945 to $84 million at the end of 1948. During 1949, however, the situation improved, largely owing to higher prices received for coffee, and the value of exports exceeded that in 1948 by 15 per cent. Imports declined, with the result that an export surplus developed, and gold and foreign exchange reserves rose to $111 million at the end of 1949.

In recent years income remitted on account of direct investments, mainly of United States origin, is reported to have been about $5 million annually. It is not clear, however, whether this includes all the earnings of the petroleum and mining companies which as was pointed out above, do not obtain exchange from the Colombian authorities. The annual service of the external debt during the next few years will require $10 - $12 million annually. The annual transfer on account of interest, dividends, and regular amortization, during the next few years will amount, therefore, to somewhat more than $15 million. The latter sum was equal to 6 per cent of the value of exports during 1949.

C. Employment and labour

In enterprises having payrolls exceeding 1,000 pesos a month (about $510 United States currency), not more than 10 per cent of the manual wage earners engaged continuously for more than three months, and not more than 20 per cent of the salaried employees, may be aliens and at least 80 per cent of the wages and 70 per cent of the salaries

/must be

must be paid to Colombians.[1] Exemptions may be granted for the hiring of indispensable technical personnel but only for as long as is required to train Colombians to do the work. Nationals and aliens performing the same kind of work must be given equal remuneration and working conditions.[2] There are no restrictions on the employment of foreign managerial personnel.

The costs of business operation in Colombia are affected by extensive social legislation which provides, for example, for minimum wages and for profit-sharing with employees.[3]

D. Taxation

Colombia's tax laws contain no discrimination on the basis of nationality. Taxes are imposed on personal and business incomes and on profits in excess of 12 per cent of the value of capital. There is also a tax on all business assets with a value of more than 20,000 pesos. The rate varies from 1.35 pesos per thousand to 15 pesos per thousand on property in excess of 1 million pesos ($500,000).

The tax on business incomes ranges from 1 per cent on taxable income below 2,000 pesos (about $1,025) to 22 per cent on income above 5 million pesos (about $2.6 million), recently there has been added a surcharge of 35 per cent on the total tax due. An additional levy of

1/ Law No. 149 of 31 October 1936; Decree of 6 August 1937; and Resolution of 2 May 1939.

2/ Law No. 10 of 20 November 1934.

3/ Under Decree-Law No. 2474 of 19 July 1948, a progressive scale of profit-sharing applies to profits in excess of 12 per cent of "net worth" of an enterprise. The rates range from 5 per cent on profi between 12-15 per cent of net worth to 20 per cent on profits in excess of 35 per cent.

/5 per cent

5 per cent on net income after taxes above 10,000 pesos (about $5,100) was imposed in 1946 for a period of ten years to provide funds for low-cost housing projects.[1/] The excess profits tax, is additional to the profit-sharing requirement referred to above, ranges from 12 per cent of profits between 12 and 15 per cent of capital to 33 per cent on profits in excess of 50 per cent. A surcharge of 55 per cent of the tax due is added at present.

Exemption from the taxes on excess profits and property are granted to capital invested in gold, silver and platinum mines and in the cultivation of coffee and bananas. Gold mining and banana cultivation are carried on largely by foreign enterprises. Exemption from the property tax may also be accorded for five years to companies engaged in certain industries, e.g., the processing of domestic raw materials, and to companies in certain industries in which at least 20 per cent of the capital is subscribed by the government or its Institute of Industrial Development.

E. Commercial policy

Since the early 1930's and especially since the war, Colombia has increasingly adapted its commercial policy to protect domestic industries. For this purpose use has been made of customs duties, quantitative restrictions and mixing regulations. Protection has also

1/ Law No. 85 of 1946 and Decree No. 0722 of 28 February 1947. Alternatives to payment of this tax are investment in certain government bonds issued to secure funds for housing projects or private construction by business enterprises of low-cost housing facilities.

/been afforded

been afforded as by-product of exchange control.

The 1936 Reciprocal Trade Agreement between the United States and Colombia was terminated as of 1 December 1949, and most rates of duty reverted to what they had been before 1936. Import quotas and licencing are applied to certain agricultural and manufactured products, including textiles. Mixing regulations are applied to promote domestic production of a number of raw materials.[1/]

As a result of these measures the profitability of a number of domestic industries has been increased. Nevertheless, foreign investments in manufacturing remain small, representing probably not more than 5 per cent of all direct foreign investments.

II. CONTROL OF THE PETROLEUM INDUSTRY

The future of foreign participation in Colombia's petroleum industry, the major outlet for direct investments at present, is uncertain. In August 1948 the Minister of Mining and Petroleum announced that the government would not renew the most important concession, operated by the Tropical Oil Company, a subsidiary of the Standard Oil Company of New Jersey, which expires in 1951.[2/] It was indicated at that time that a Colombian company with joint governmental and private capital would take over and exploit the properties. In November 1949, the Tropical Oil Company confirmed that it would discontinue production upon the expiration of its concession and it

1/ Decree No. 206, published 23 February 1949, and Resolution 184 15 March 1949. Included among the raw materials are cotton, rubber, sulphur, sugar, tanning extracts, tobacco and rayon yarn.

2/ New York Times, 4 August 1948.

/discontinue

discontinue production upon the expiration of its concession and it was reported that other foreign petroleum companies had declined to participate as minority stockholders in the proposed joint state and private company planned, but would participate if allowed to do so on the basis of ownership of a minimum of 50 per cent of the shares.[1/]

Under Colombian petroleum law,[2/] exploitation concessions are granted for a period of thirty years, subject to extension for ten years. The law contains no limitations regarding the nationality of concessionnaires. Companies holding such contracts are regarded as Colombian for both "national and international purposes", and as indicated above, recourse to any external authority is thereby excluded in the event of controversies arising from the contracts. Concessions may not be transferred to foreign governments.

In general, preference in employment in the industry is to be given to Colombians. The minimum percentage of nationals to be employed by any petroleum enterprise is determined in each contract.

The petroleum industry is subject to general taxation, as already described, as well as to the payment of royalties. Foreign petroleum companies operating in Colombia have charged that certain features of the taxation of the industry constitute a deterrent to investment.[3/] The criticism has related to the allegedly insufficient deductions of exploration costs allowed for purposes of computing income, to

1/ New York Times, 27 November 1949.

2/ Law No. 37 of 4 March 1931, amended by Law No. 60 of 1936.

3/ See New York Times, 12 January 1950.

/inadequate

inadequate depletion allowances[1/], and to the policy of taxing separately operations in various fields within the country without allowing losses arising from one field of operations to be charged against profit of others. Royalty payments on petroleum extracted from government-owned lands range from 2 per cent to 11 per cent of the value of production, varying in inverse proportion to the distance from the point of production to the port of shipment. Production taxes on petroleum extracted from privately owned lands range from 0.5 per cent to 7 per cent of the value of production, varying according to the same principle.

Incentive is provided for the refining of petroleum within the country. All machinery, materials and equipment imported for the installation of refineries or the production of refined products are exempt from import duties. Locally produced crude petroleum is totally exempt from payment of royalties or taxes if refined for domestic consumption and exempt to the extent of 20 per cent from royalties or taxes for a period of ten years if refined for export.

III. GOVERNMENT PARTICIPATION IN INDUSTRY

In 1943 authorization was granted to the government to issue bonds up to 50 million pesos to be used for the nationalization of telephone, transportation, electric power, and other public utility companies.[2/] By that year approximately half the electric generating

1/ Maximum depletion allowance under the law is 10 per cent of the net income per annum.

2/ Law No. 7 of 2 March 1943, article 13.

/capacity

capacity was municipally-owned. In 1946 the National Institute for the Utilization of Water and for Electrical Development was created to stimulate further development of electric power resources by constructing facilities on its own account or by financing other enterprises. The most important railways of the country are publicly-owned and administered by an Administrative Council of National Railroads, established in 1931. Foreign-owned lines together account for less than ten per cent of the country's railway mileages. As was indicated above, the government was authorized in February 1945 to negotiate for the purchase of the most important of these, the British-owned Dorada Railway. In 1946 the government, in association with the governments of Ecuador and Venezuela, formed a merchant fleet, the Great Colombian Merchant Fleet (Flota Mercante Grancolombiana), and much of the trade in coffee has been diverted to this line by the National Federation of Coffee Growers, a semi-official agency controlling the marketing of Colombian coffee. Reference has already been made to the possibility of the participation by the government with private Colombian and perhaps foreign capital in petroleum extraction.

The Institute of Industrial Development was established in 1940 to provide capital and to act as "promoter and partner in basic industries requiring costly preliminary surveys and large capital that may not be within the immediate reach of private parties".[1/]

1/ Decree No. 1157 of 8 June 1940.

/Its capital

Its capital was initially provided by the national government and the Central Mortgage Bank. Private investors may also subscribe to its capital. The plans of the Institute call for the sale of its holdings to the public once the enterprises in which it has invested are operating satisfactorily, thereby obtaining funds for investment in other enterprises. As already indicated, certain enterprises in which the Institute participates to the extent of at least 20 per cent are accorded exemption from the property tax. The Institute has initiated or participated in the initiation of a wide variety of enterprises. Among them are concerns engaged in mining, in the production of iron and steel, chemicals, automobile tires, glass, woollen goods, dairy products and river craft, and in the processing of forest products. In some instances the Institute has participated jointly with United States capital in the formation of new enterprises, but in each case the foreign participants have been limited to a minority interest. Outstanding among such cases are "Unión Industrial, S.A.", which operates shipyards, and "Industria Colombiana de Llantas, S.A." which manufacturesrubber tires.

The Central Government exercises long-standing monopolies in the extraction of salt and emeralds. Processing of salt may, however, be carried on by private enterprise. The distribution of alcoholic beverages is a monopoly exercised by local government authorities. Monopolies on the purchase and sale of rubber and platinum were established by the Central Government as war-time measures in 1942.
