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Memorandum From the Acting Executive Secretary of the Department of State (Walsh) to the President's Assistant for National Security Affairs (Kissinger)

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Nota de Archivo: *Summary: Walsh outlined the ramifications of the agreement between the Government of Chile and the Anaconda copper company. Source: National Archives, Nixon Presidential Materials, NSC Files, Box 773, Country Files, Latin America, Chile, Vol. I. Confidential. Kissinger sent this memorandum to the President under cover of a July 11 memorandum drafted by Vaky, apprising him of the Anaconda agreement. The memorandum is printed as Document 17 in Foreign Relations, 1969–1976, vol. XXI, Chile, 1969–1973. Enclosures 1 and 2 are attached but not published.*

Chile-Anaconda Agreement

Proximate Causes of Chilean Action against American Copper Companies

The historical background of the importance of copper and American copper companies for Chile and Chilean/U.S. relations is dealt with in Enclosure 1. Several factors contributed to the Chilean decision to proceed against the American companies in May 1969 and are essential to understanding the agreement reached with Anaconda on June 26:

—The Christian Democrats (PDC—the Government party) lost badly in the March Congressional elections and faced a Presidential election in September 1970 divided into quarreling factions and aware that nationalization would again be an important Marxist issue.

—Anaconda had recently aroused the Government and public opinion by feuding over customs duties on capital imports, suing against Government-established sales prices to domestic processors, and staking out extensive non-copper mineral claims while failing to establish an earlier agreed-upon joint exploration company. These acts led on April 30 to unprecedented, unanimous and rapid Congressional action depriving Anaconda of its new claims.

—Copper prices have risen steadily since 1964 and have been at extraordinarily high levels for the third year in a row, averaging over 60¢ a pound this year. Chile believed it had provided the American companies windfall profits and cheated itself of its proper share in the Chileanization program by agreeing to lower taxes guaranteed for twenty years with no escalation clause pegged to copper prices.

—Peru's expropriation of IPC, although not a major factor, probably contributed to pressures against Anaconda.

The Negotiations—President Frei sent a letter to President Nixon on May 4 designed to reassure the U.S. that Frei wished to maintain good relations and would abide by international norms in obtaining greater tax revenue and Chilean participation in the American companies. Anaconda and Kennecott were approached on May 9, primarily on the tax issue. Anaconda was forthcoming on taxes but balked at allowing more than 25% participation in its wholly owned subsidiaries.

Kennecott was intransigent, citing its earlier sale of 51% equity. Frei's State of the Nation speech on May 21 publicly stated the goals previously set forth to the companies and the U.S. His proposals for a negotiated settlement, rather than outright nationalization, and his defense of Chileanization were received coldly in Congress. By early June, even the PDC had formally called for full recovery of minerals from Anaconda's subsidiaries.

Serious high-level negotiations with Anaconda began on June 2. They continued virtually uninterrupted until agreement was reached on all major issues on June 26. A summary of the agreement and related U.S. Government actions is enclosed (Enclosure 2). Ambassador Korry played a brilliant, imaginative and essential role throughout as a behind-the-scenes go-between. His contribution was highly praised by both sides. He achieved the essential U.S. objective: a negotiated, mutually acceptable settlement, without any public attacks on the United States or any indication of the U.S. role.

Significance of Agreement

(A) Contrast with IPC Case, and Anaconda Case as a Model for Future Acquisitions of American Companies: The U.S. press has contrasted the Anaconda settlement most favorably with the IPC case. This is really valid only if the settlement as such is contrasted with the last spasm in the IPC negotiations when the military government came to power in Peru, and if the comparison ignores the long history of negotiations under Belaunde, during which the IPC continued to operate. Anaconda did negotiate under great pressure and very limited time constraints imposed by Chile, in contrast with the pace of the earlier IPC negotiations. Moreover, Anaconda was being asked to divest itself of complex properties valued at perhaps $800 million, far exceeding the value of IPC.

The method adopted—negotiation rather than outright nationalization—is, however, obviously preferable. Furthermore, in the Anaconda negotiations, the United States through its Ambassador played a most important behind-the-scenes role. In the early years of the IPC negotiations, the U.S. took a distant position in the negotiations themselves, but did curtail aid to Peru.

Further problems arise if the Anaconda settlement is taken as a model for future agreements on acquisition of American companies by Latin American governments. The basic requirements for an Anaconda-type settlement are, on one side, moderation of the Government's appetite and the Government's political power to sustain a negotiated settlement; and, on the other, adequate corporate reasons for settling. Many special factors led Anaconda to sign. Anaconda's initial 51% equity is being sold at book value, hardly an acceptable valuation for most companies, as evidenced even by Chilean agreement to pay a multiple of earnings for the remaining 49%. The atmosphere of pressure and the very limited time constraints have been mentioned. Copper is so central to the Chilean economy and Anaconda is such a large factor in the industry that the company knew it would be nationalized if it did not agree. Moreover, the earlier Kennecott settlement had established minimum terms for Anaconda. Few companies would consider acceptable the extremely high taxes on profits and dividends accepted by Anaconda; they are tolerable only because of the extraordinarily high world copper prices and the profitability of Anaconda's operations, which have been largely amortized over forty years. Also, the importance of Chile's contribution to Anaconda's total earnings (about 66%) cannot be overlooked; without at least a brief transition, Anaconda's corporate position would be seriously affected.

(B) Anaconda Settlement and AID Legislation: If the Chilean script leading to a negotiated settlement under pressure of nationalization is followed by other developing countries, this will undoubtedly discourage U.S. private investment in such countries, particularly in natural resources. The AID guaranty program will of course alleviate the effect of such potential action insofar as it can be directly equated to expropriation with inadequate or no compensation and where such guarantees are in force. The Anaconda problem and other problems that might develop over time should not, however, have an immediate effect on the pending AID legislation or on the legislation for the Overseas Private Investment Corporation. The Anaconda situation is clearly differentiated from Kennecott. Anaconda chose not to have expropriation guarantees in force

during 1969, but rather to go on standby, i.e., to give up its right to coverage for an insurable event (expropriation) in order to save the insurance fees during that year. Consequently, regardless of the outcome of the Anaconda-Chilean negotiations, Anaconda would not have been able to make a claim for expropriation based on Chilean action during 1969. Kennecott is expected to be the next American company negotiating with Chile. Although Kennecott has its insurance on current status, the AID guaranty of this investment is solely on Kennecott's long-term debt interest and not on Kennecott's 49% equity interest. Moreover, the guaranteed debt would probably not be affected by a nationalization of Kennecott's equity because the debt servicing payments do not commence until 1972. Therefore, it is highly unlikely that a substantial guaranty claim would be presented in the near term.

There is a further problem with regard to the AID legislation. The illustrative country programs prepared four months ago show an AID program for Chile for FY-70 of $75 million, with $40 million in program loans and other sums for sector loans. Members of Congress may well ask why the U.S. is planning to provide balance of payments assistance to Chile while that country is using its foreign exchange to buy out U.S. copper interests. This question will have to be reviewed as part of the over-all analysis of Chile's balance of payments situation late this year. No program loan was provided to Chile this year, although negotiations for a $20 million loan were completed in March.

(C) For Chilean/U.S. Relations: The chief significance of the agreement, if it holds, is that it removes an abrasive, historical legacy. Anaconda, for decades the primary U.S. representative in Chile in economic, psychological and political terms, symbolized to Chileans their inferiority to and dependence upon the United States. Anaconda's after-tax earnings in the last three years exceed U.S. economic aid, although much of these earnings were plowed back in new investment in Chile. There is no longer a vast foreign state within a state dominating much of northern Chile, affecting significantly both Chile's foreign exchange and budget receipts, and permeating all aspects of Chilean economic life through its purchases.

(D) For Chile's Domestic Politics: Frei's Christian Democrats pre-empted one of the most important issues which could have been used by opposition parties of all shades from right to extreme left in the 1970 Presidential election. The agreement has unified the Christian Democrats around a "victory" for their leader and government and strengthened their hand for the 1970 Presidential campaign. It has provided a platform on which the dissident Party leader, Radomiro Tomic, widely conceded to be the Party's best votegetter and most likely standard bearer in 1970, can make his peace with Frei and go into the Presidential race with unified Party support.

(E) Anaconda Agreement May Not Hold: The positive advantages for U.S. policy occur only if the Anaconda agreement is carried out. For many reasons, the agreement may not hold. Caught unprepared by the sudden announcement of the agreement, the Marxist opposition parties have been very restrained so far and have not settled on a line of attack. They can be expected, however, to attempt to frustrate Frei's move to preempt the copper issue by finding or fabricating deficiencies in the agreement. They may well push even more vociferously than ever for outright nationalization or expropriation on terms less favorable to Anaconda. The left could be joined by the right-wing National Party, seeking to carve out an election plank for themselves by improving the terms of the agreement for Chile. The pressures of next year's campaign preclude the hope that the issue can be removed from the political arena.

What is more, negotiations are about to begin with Kennecott. Its position to date has been that it has already ceded majority ownership of its subsidiary to Chile, and it is intransigent on payment of higher taxes. If Kennecott maintains this position in negotiations or in the Chilean courts, standing on the twenty-year tax guarantees in its present investment decree and other agreements, the Chilean Government has told our Ambassador that it is prepared to move to expropriate Kennecott. It will negotiate first, but is ready to introduce whatever legislation is necessary to obtain higher taxes. Any legislation might easily be amended on the floor to include a modification of the present Anaconda agreement or outright nationalization with only token or no compensation. All the political parties in Chile have come out for nationalization. The issue would then be whether President Frei would veto the amended legislation, and whether he could sustain such a

veto. The 1970 Presidential election would loom large in such decisions.

No one can predict the 1970 election with certainty. It is likely that there will be three candidates: conservative former President Jorge Alessandri, supported by the Nacionales, independents, and voters of many persuasions; a Christian Democratic candidate, possibly Tomic; and a leftist or Marxist candidate, who could be Socialist Salvador Allende. The Christian Democrats obtained only 30% of the vote in March and could finish last. Anaconda is hoping that Alessandri will win and that the agreement can be re-negotiated on more favorable terms. While he may win, this hope seems illusory, given the political trends and strengths in Chile and Latin America. Salvador Allende was beaten by Alessandri by only 34,000 votes out of 1.2 million in the multi-candidate race in 1958, and Allende received 39% of the vote in an essentially two-man race with Frei in 1964. Should Allende win, his government might as its first act introduce copper nationalization measures to solidify his support.