



**Much Ado About Nothing:  
Expropriation and  
compensation in Peru and  
Venezuela, 1968-75**

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# Much Ado About Nothing: Expropriation and compensation in Peru and Venezuela, 1968-75\*

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Peru provided the penultimate major expropriation crisis before the institutionalization of the investment guarantee program under the Overseas Private Investment Corporation or the accession of any Latin American countries to the International Centre for the Settlement of Investment Disputes. It also provided the incoming Nixon Administration with a concrete example of the danger of using American power in defense of private enterprise in the context of the Cold War. The ultimate resolution was favorable to the American companies, but getting there was messy and involved, from Nixon's point of view, undue geopolitical risks. Those risks, however, grew from domestic pressures that prevented Nixon from abandoning American companies at a reasonable political cost, no matter how much he would have preferred to do so for reasons of state.

In 1968, a military coup brought a left-wing government to power in Peru. That government proceeded to nationalize American investments. In a counterfactual world without the Soviet Union, the U.S. government would not have hesitated to impose severe sanctions. The world of 1968 did, however, contain a hostile Soviet Union, and the new Peruvian government (while avowedly anti-Communist) made it clear to the Nixon Administration that it would not hesitate to turn to the Soviets for aid if the American cut it off. (In the clearest possible signal, the Peruvian junta did in fact purchase weapons from the Soviet Union—and accept Soviet trainers to learn how to operate them.)

The Nixon Administration tried to treat the Peruvian government with forbearance — but domestic pressure to bring down the hammer meant that it came very close to failing. The Peruvian economy of the 1960s relied heavily on primary products — mining, cotton, fishing, and petroleum — with most of these commodities produced or marketed through U.S.-owned companies. One particular company, however, stood out in the minds of Peruvian policy makers: the International Petroleum Company (IPC). The IPC was originally incorporated as a Canadian subsidiary of Standard Oil of New Jersey in 1914 to operate the La Brea y Pariñas oil fields near the Ecuadorian border. Unusually for Latin America, both the surface and the subsurface title to these fields were privately held. In 1826, the Peruvian government granted the subsoil rights of

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what was then a pitch mine to a Peruvian aristocrat, Don José de Quintana, in return for his help in funding the Bolivarian revolution. The resulting conflicts over this concession (detailed in Chapter 3) only ended when President Augusto Leguía signed a 1922 agreement giving IPC special tax concessions for 50 years in return for a one-time payment of \$1 million and help arranging foreign loans from private American banks, which were just beginning to get back into the business of lending to Latin American governments after the default wave of the 1930s.<sup>1</sup>

As the Peruvian economy expanded, more and more of IPC's production went to the domestic market, where the price of gasoline was fixed by the government. In 1957, IPC proposed to renegotiate a concession from the business friendly administration of President Manuel Prado. IPC offered to give up its private property rights in return for a standard long-term concession (with an expiration date) and higher gasoline prices. The Prado government agreed in principle, raising gasoline prices on July 25, 1959 and opening discussions with IPC's management. The price hike immediately mobilized an ideologically diverse opposition, uniting leftists, centrists, conservatives, and most tellingly, the Peruvian military. The renegotiation failed. In 1962, the military staged a coup against when the general elections indicated that a right-left coalition would install former Peruvian president Manuel Odría in office. The military allowed elections in 1963, in which the centrist candidate Fernando Belaúnde received more than a third of the vote, leading to a Belaúnde presidency and an opposition Congress.<sup>2</sup>

The delicate political situation in Peru, therefore, led to a ratchet effect in Peruvian policy, with each faction competing to put forward more nationalist proposals regarding IPC. Divided government, however, prevented the policies from being enacted. After his election, Belaúnde put forward a plan that IPC return the oil fields to Peru, in exchange for a 25 year concession. With no *quid pro quo* on retail prices, IPC refused. Belaúnde then sent the Peruvian congress a proposal to change the IPC's property and tax status. Congress refused to pass Belaúnde's gradualist proposal, instead passing its own legislation annulling the terms of the 1922 agreement. Belaúnde, in turn, refused to implement the Congressional legislation.

By the end of 1964, the Johnson Administration began to worry that the IPC would be nationalized as a way to break the domestic political impasse. Assistant Secretary of State Thomas Mann attempted to dissuade the Belaúnde government against this

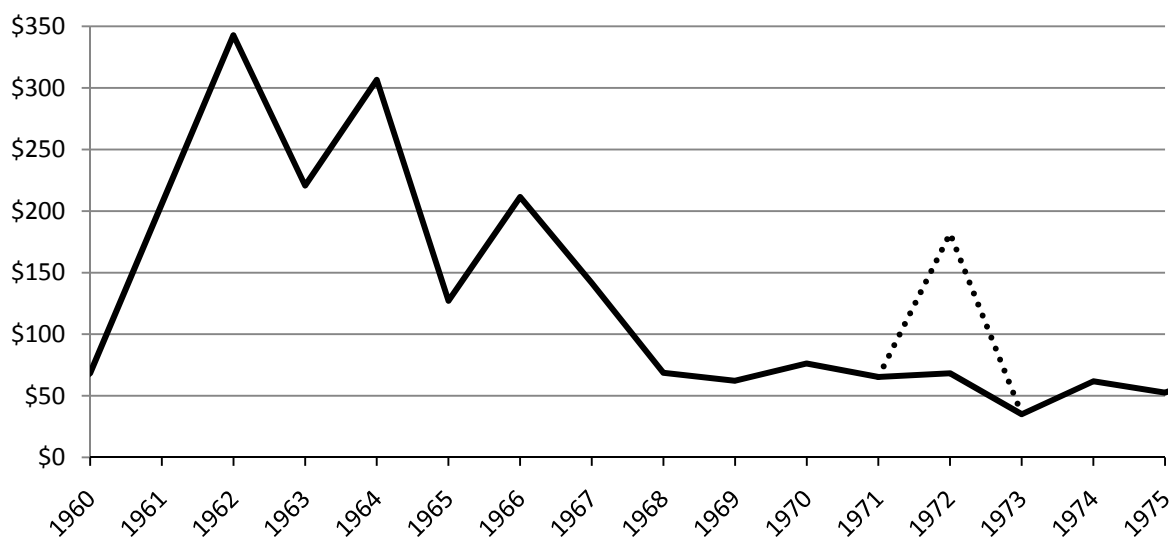
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<sup>1</sup> Paul E. Sigmund, *Multinationals in Latin America: The Politics of Nationalization*. Madison: University of Wisconsin Press, 1980, pp. 184-185; Richard N. Goodwin, "Letter from Peru," *The New Yorker*, May 17, 1969, pp. 44-46.

<sup>2</sup> Paul E. Sigmund, *Multinationals in Latin America: The Politics of Nationalization*. Madison: University of Wisconsin Press, 1980, pp. 186-187.

course of action by stalling economic aid to Peru. “The idea was to put on a freeze, talk about red tape and bureaucracy, and they’d soon get the message,” explained one anonymous U.S. aid official.<sup>3</sup> Unfortunately, the Peruvian government did not get the message. Aid to Peru dropped by more than half in 1965, but it was not cut off, and the variation was well-within previous swings. President Belaúnde was honestly shocked when National Security Advisor Walt Rostow personally offered him a *quid pro quo* in 1966: a resumption of aid to Peru in return for the non-expropriation of IPC.<sup>4</sup> This had the effect of convincing Peruvian leaders that the United States was attempting to strong-arm the Peruvian government on the IPC issue, which of course it was. It was not the Johnson Administration’s finest hour.

**FIGURE: U.S. assistance to Peru, 1960-75, millions of 2009 dollars**



*Note:* The 1972 spike in aid shown by the dotted line consisted entirely of emergency spending of \$113 million for humanitarian relief after severe an earthquake and severe flooding in Lima.

*Source:* USAID Green Book.

The IPC itself realized its position in Peru was increasingly shaky. Three days before Belaúnde’s State of the Nation address on July 28, 1968, the IPC told Belaúnde that it was willing to hand over the La Brea y Pariñas fields to the Peruvian state oil company in return for marketing and refining concessions and the right to participate in new exploration elsewhere in the country. This willingness may have been prompted by recent oil discoveries in the Amazonian regions of Ecuador: trading a mature and increasingly unprofitable field to Peru in exchange for the possibility of new fields in the Peruvian

<sup>3</sup> The account appears in a *New Yorker* article authored by Richard Goodwin, a journalist and a former special assistant to President Johnson himself. Richard Goodwin, “Letter from Peru,” *The New Yorker*, May 17, 1969, p. 60.

<sup>4</sup> Richard Goodwin, “Letter from Peru,” *The New Yorker*, May 17, 1969, p. 60.

Amazon seemed like a rational exchange. IPC's terms were in fact *more* generous for Peru than the terms Belaúnde offered IPC in 1963. After a series of all-night negotiation sessions in the Presidential Palace, Belaúnde and the IPC came to an agreement — the Act of Talara — and the Peruvian government formally took possession of the La Brea y Pariñas fields on August 13, 1968.<sup>5</sup>

Politically the IPC agreement turned out to be a disaster for Belaúnde. The Act of Talara quickly became a focus for domestic political resentment. Carlos Loret de Mola, the head of the Peruvian state oil company, resigned on September 7, 1968. Three days later he appeared on national television to announce that the official copy of the Act of Talara was missing a final page (the eleventh) on which he had penned an addendum to the contract which stated that the IPC would compensate Peru a favorable minimum price per barrel in U.S. dollars.<sup>6</sup> The resulting split within Belaúnde's party seemed to guarantee the election of the leftist Víctor Raúl Haya de la Torre, whom the Peruvian Army despised. On October 3, a military coup led by the chief of the Peruvian Armed Forces Joint Command, General Juan Velasco Alvarado, deposed Belaúnde. Six days later, on October 9, the coup leaders renounced the Act of Talara and occupied IPC's principal refinery, in addition to the La Brea y Pariñas fields.

In a less contentious transfer of power, Richard Milhous Nixon was elected the thirty-seventh president of the United States on November 5, 1968. Nixon would choose former Attorney General and longtime legal advisor William Rogers as his Secretary of State, and the Harvard political scientist Henry Kissinger as his National Security Advisor. This was part of Nixon's strategy to rein and diminish the influence of the State Department, which Nixon deeply distrusted. Nixon instead preferred to use multiple competing agencies as extensions of his executive power, using Rogers to keep the State Department in line, while relying on Kissinger for his foreign policy and domestic advice. As a result, Kissinger would come to occupy a prime minister-like position within the Nixon White House, while Nixon was insulated from the traditional pressures exerted by the cabinet.

Peru was not Nixon's chief foreign policy concern in 1969. (This should not be surprising, considering that the Vietnam War was still in full swing.) Peru was not even Nixon's chief foreign policy concern in Latin America. Nixon's problem was that the clock of the Hickenlooper Amendment (and related anti-expropriation legislation)

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<sup>5</sup> Paul E. Sigmund, *Multinationals in Latin America: The Politics of Nationalization*. Madison: University of Wisconsin Press, 1980, pp. 188-189; George Philip, *Oil and Politics in Latin America: Nationalist Movements and State Companies*. Cambridge: Cambridge University Press, 1982, pp. 252-253; Richard N. Goodwin, "Letter from Peru," *The New Yorker*, May 17, 1969, pp. 80-82.

<sup>6</sup> Richard N. Goodwin, "Letter from Peru," *The New Yorker*, May 17, 1969, pp. 82-88.

however, mandated that within six months — specifically, before April 9, 1969 — the United States would have to automatically cut its Peruvian aid and its imports of Peruvian sugar. Within days of Nixon's inaugural, the State Department advised Kissinger, "Suspension of aid and the sugar quota will have a serious adverse impact on the Peruvian economy, probably lead to reprisals against other U.S. investments, alienate the Peruvian people and stimulate an actively hostile policy toward the U.S., perhaps push Peru further toward economic and diplomatic relations with the Soviet bloc, and damage U.S.-Peruvian relations for a long time to come — all with repercussions harmful to our interests elsewhere in the hemisphere."<sup>7</sup> Kissinger considered the new military government in Peru — despite its ominous name of the Revolutionary Government of the Armed Forces — to be a friendly anti-Communist regime, and he agreed with the State Department's assessment. Kissinger advised Nixon to meet personally with the U.S. ambassador to Peru for a full appraisal of the situation. Nixon preferred that Kissinger meet with the ambassador instead "and bring him in to say hello at end of conversation," but the discussion took place as scheduled.<sup>8</sup>

The Revolutionary Government of the Armed Forces under President Juan Velasco continued to expropriate the remaining properties of IPC in Peru, including the Esso gas stations located throughout the country. The takeover went smoothly, since most of the IPC's personnel were already Peruvian, and IPC's focus had been on the Peruvian domestic market.<sup>9</sup> The Revolutionary Government refused to pay compensation. Moreover, in February 1969 the Revolutionary Government adopted a proposal of the senior lawyer of the Lima bar, Alberto Ruiz Eldredge, of *revindicación*: requiring restitution from IPC for the value of the petroleum it had already extracted.<sup>10</sup> This totaled an astonishing \$690 million (\$3.4 billion in 2009 dollars)—calculated as the total output of the La Brea y Pariñas fields from 1924 to 1968 at East Texas prices, minus production and shipping costs.<sup>11</sup> For its part, IPC valued its holdings in Peru at \$200 million, although it soon dropped that number to \$85 million. On February 6, President Velasco assured the

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<sup>7</sup> *Foreign Relations of the United States, 1969–1976*, Volume E–10, Documents on American Republics, 1969–1972, Document 576, Briefing Memorandum Prepared in the Department of State for the President's Assistant for National Security Affairs (Kissinger), Washington, January 28, 1969.

<sup>8</sup> *Foreign Relations of the United States, 1969–1976*, Volume E–10, Documents on American Republics, 1969–1972, Document 577, Memorandum From the President's Assistant for National Security Affairs (Kissinger) to President Nixon, Washington, February 6, 1969.

<sup>9</sup> Paul Sigmund, *Multinationals in Latin America: The Politics of Nationalization*. Madison: University of Wisconsin Press, 1980, pp. 190-191.

<sup>10</sup> George Philip, *Oil and Politics in Latin America: Nationalist Movements and State Companies*. Cambridge: Cambridge University Press, 1982, pp. 254-255.

<sup>11</sup> Paul Sigmund, *Multinationals in Latin America: The Politics of Nationalization*. Madison: University of Wisconsin Press, 1980, p. 365n8.

world, "The case of the International Petroleum Company is unique. It is a singular case."<sup>12</sup> Less than two weeks later, Peru signed a trade pact with the Soviet Union.<sup>13</sup>

Kissinger may have believed that the Peruvian government was on-side in the Cold War, but Velasco's actions had the effect of igniting a wave of American concern about the emergence of a second, Andean, Cuba in the Western Hemisphere. At a press conference on March 4, Nixon explained to reporters the administration position on Peru: "Now, if they do not take appropriate steps to provide for that [expropriation] payment, then under the law—the Hickenlooper amendment, as you know—we will have to take appropriate action with regard to the sugar quota, and also with regard to the aid programs. I hope that is not necessary; because that would have a domino effect, if I can be permitted to use what is supposed to be an outworn term—a domino effect all over Latin America."<sup>14</sup> Meanwhile, the National Security Council (NSC) examined a set of immediate "hard-line" and "soft-line" options regarding Peru, ranging from an extremely strict set of economic sanctions in the hardest to virtually nothing in the softest variation, as long as Velasco could provide the U.S. government a "fig-leaf" for inaction. (With the Vietnam War in full-swing and the U.S. barely able to maintain sufficient forces in West Germany and South Korea, military action was a non-starter, and the fact that Peru was *already* under a military government appears to taken covert action off the table.) In the opinion of the NSC's analysts, "Selection of this [softest] option would imply a judgment that adverse effects from invoking these sanctions would inflict unacceptable damage to our long-range hemispheric foreign policy interests. *The decision would clearly reject the future use of Hickenlooper-type devices for protecting U.S. investment abroad, at least in Latin America.*" (Emphasis added).<sup>15</sup>

Nixon sent John Irwin II as a special envoy to Peru in mid-March. Irwin had a great deal of experience in Latin American affairs, having served as the deputy assistant secretary of defense for international security affairs under Eisenhower, and more recently the U.S. representative for Panama Canal negotiations in the Johnson Administration. Irwin suggested to the Peruvians that they use international arbitration to resolve the IPC dispute. Arbitration would give the U.S. its needed fig leaf, calm domestic pressures to impose stronger sanctions or otherwise intervene, and allow the Peruvians to present a case that Irwin believed to be strong. The Peruvians rejected this, since it vi-

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<sup>12</sup> Richard Goodwin, "Letter from Peru," *The New Yorker*, May 17, 1969, p. 43.

<sup>13</sup> *New York Times*, February 18, 1969, page 1, "Peruvians and Soviet Sign Their First Trade Accord".

<sup>14</sup> *New York Times*, March 5, 1969, page 8, "Transcript of the President's News Conference on Foreign Affairs and His Trip".

<sup>15</sup> *Foreign Relations of the United States, 1969–1976*, Volume E–10, Documents on American Republics, 1969–1972, Document 581, Study Memorandum Prepared by the National Security Council Interdepartmental Group for Inter-American Affairs, Washington, March 7, 1969.

olated the Calvo Doctrine. The Peruvians in turn suggested that IPC use Peruvian administrative channels to appeal the \$690 million judgment. After several meetings with Velasco himself, Irwin returned to the United States on April 3, six days before the Hickenlooper deadline, pessimistic that the situation could be resolved.<sup>16</sup>

Nixon waited until the last days of the Hickenlooper deadline to come to a decision. On April 5, the Saturday morning before the deadline, Kissinger phoned Nixon at his compound in Key Biscayne, Florida, to discuss the Peruvian situation. Kissinger informed Nixon that his advisors agreed on the usefulness of extending the deadline, but “we’ve got to have some excuse unless we just say that the negotiations which have been going on for two weeks, and we’ll give them another 30 days as a sign of leaning backwards.” Nixon disagreed. “No, that won’t do. I don’t think that will do. My inclination is to give them more time than that. Have in mind the purpose is not to negotiate, but purpose is to fight. Line up the troops and go after them every which way we can. Maybe it will take three months.” Nixon thus extended the Hickenlooper deadline not because he “blinked,” but in order to confront Velasco at a time of Nixon’s choosing. “Don’t move it to his [Velasco’s] timetable, that’s for sure,” said the President. Kissinger agreed, commenting, “IPC has been a lousy company, but that isn’t the issue now.” Nixon replied, “No, it sure isn’t.” Nixon postponed the imposition of sanctions until August 6, using the IPC’s tentative acceptance of the Peruvian terms for administrative appeal as the “fig-leaf.”<sup>17</sup>

On April 6, Irwin met with Nixon in Key Biscayne for an hour, after the Nixon family attended Easter church services.<sup>18</sup> Irwin then returned to Peru to inform Velasco that the IPC would follow the Minister of Finance’s appeal process against the \$690 million. On Monday, Secretary of State Rogers announced at a press conference that the appeal process and negotiations satisfied the Hickenlooper Amendment’s requirement of “appropriate steps” towards compensation.<sup>19</sup> It is highly doubtful that Senator Bourke Hickenlooper (R-Iowa) would have considered an appeal to a court controlled by a revolutionary military government hostile to the expropriated company to be an “appro-

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<sup>16</sup> Paul E. Sigmund, *Multinationals in Latin America: The Politics of Nationalization*. Madison: University of Wisconsin Press, 1980, pp. 192-193.

<sup>17</sup> *Foreign Relations of the United States, 1969–1976*, Volume E–10, Documents on American Republics, 1969–1972, Document 589, Transcript of Telephone Conversation Between President Nixon in Key Biscayne, Florida and the President’s Assistant for National Security Affairs (Kissinger) in Washington, April 5, 1969, 9:45 a.m.

<sup>18</sup> President Richard Nixon’s Daily Diary, April 6, 1969, accessed via: <http://www.nixonlibrary.gov/virtuallibrary/documents/dailydiary.php>

<sup>19</sup> Paul Sigmund, *Multinationals in Latin America: The Politics of Nationalization*. Madison: University of Wisconsin Press, 1980, p. 193.



ropriate step.” Perhaps fortunately for the Nixon Administration, Hickenlooper had chosen not to run for reelection in 1968.

The confrontation with Peru over the IPC seems to have crystallized a personal foreign policy doctrine for Nixon. In a letter sent to Secretary of State Rogers on April 12, the Saturday following the Hickenlooper deadline, Nixon wrote, “I believe we need to give very serious and careful thought to our relation to countries in the developing world. I do not believe we understand how our aid programs and our policies, in general, actually affect the political and economic development of these countries and their orientation on foreign policy matters of concern to us ... Our concern, I believe, should be primarily with their foreign policies, insofar as they affect our own interests. We should be concerned with the domestic affairs of other countries only as they may affect their foreign policies in ways of critical importance to us.”<sup>20</sup> The implications for Peru, and for the rest of the developing world, were obvious. Insofar as a nation did not “subordinate itself” to the Soviet bloc or Communist China—eight years after the Sino-Soviet split, Nixon distinguished between the two, but still considered both to be enemies—a nation could follow whatever domestic economic policies it wanted, whether socialist, capitalist, or kleptocratic. It could even negotiate trade or arms deals with the Soviet Union. But should the Nixon Administration believe a nation was subordinating itself to the Communist bloc in its *foreign* policy, it would not matter whether that nation gave ground over American investment disputes or not: that nation would be a target.

Nixon was aided in his position by the fact that the IPC’s owners did not want sanctions prematurely imposed on Peru. In June 1969, Standard Oil of New Jersey contacted the State Department regarding the fate of its Canadian subsidiary in Peru, IPC. (Standard Oil of New Jersey, then generally called “Jersey Standard,” would be renamed Exxon in 1973.) Jersey Standard told the department that it *preferred* a long deferral of the application of the Hickenlooper Amendment, believing that “internal pressures will build and force moderation if sufficient time is allowed.”<sup>21</sup>

The only parties who now wanted a strict enforcement of the Hickenlooper Amendment were *members of Congress*. Jack Edwards (R-Alabama) had entered the House dur-

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<sup>20</sup> *Foreign Relations of the United States, 1969-1976*. Vol. 4, Foreign Assistance, International Development, Trade Policies, 1969-1972. Washington: U.S. G.P.O., 2002, pp. 258-259. While this letter was drafted by National Security Council member Morton Halperin, later at the top of one of Nixon’s enemy lists, whose phones Nixon had tapped by the FBI, there is no evidence that this letter does not reflect Nixon’s political views, and in fact Nixon’s sense of betrayal towards Halperin may have been spurred by his candor in front of Halperin.

<sup>21</sup> *Foreign Relations of the United States, 1969-1976*, Volume E-10, Documents on American Republics, 1969-1972, Document 604, Memorandum From the President’s Assistant for National Security Affairs (Kissinger) to President Nixon, Washington, July 1, 1969.

ing Goldwater's 1964 sweep of the Deep South. Edwards believed in the "knuckle" theory of geopolitics: "Neither Peru nor any other country is going to stop harassing the United States so long as we knuckle under to every outrage perpetuated on us, calling it a new and greater triumph. Let us use some commonsense in our dealings with other countries, for once."<sup>22</sup> Nixon ensured that representatives like Edwards were well-appraised of the State Department report and Jersey Standard's preferences, "so that he can cool off Congressional critics of deferral."<sup>23</sup>

By July 22, Nixon had agreed to a set of policies drafted by the NSC with regard to IPC. First, the U.S. would "continue to maintain non-overt economic pressures on Peru to provide a framework for settlement and constructive change." In practice, this translated into an unofficial suspension of international development lending to Peru. Second, the U.S. would "defer applying the Hickenlooper Amendment so long as any plausible basis to do so can be found." Third, Washington would "actively seek a basis for such deferral even beyond the end of the administrative appeal process."<sup>24</sup> In other words, Nixon intended to permanently punt on the issue of the IPC and the sanctions mandated by the Hickenlooper Amendment.

The August 6 deadline of the Peruvian administrative appeal passed without incident. Two weeks later, the Peruvian government expropriated the last of IPC's assets. IPC continued to appeal through the Peruvian courts and to the Peruvian cabinet, even though further judicial appeals were unlikely to work: Velasco would replace all but two members of the Peruvian Supreme Court in December 1969, as well as creating an executive council to suspend or remove any judge. The United States exerted "non-overt" economic pressure on Peru to resolve the dispute, in the form of pressuring the World Bank and the Inter-American Development Bank to withhold or delay loans to Peru, while postponing bilateral aid projects, in much the same way the Johnson Administration had attempted to influence Belaúnde.<sup>25</sup>

The CIA did not believe that Velasco's moves towards the Soviet Union were anything more than a negotiating tactic. In March 1969, it reported, "Peru's recent moves to establish diplomatic and economic relations with the USSR and other European Communist countries, which were begun last year under President Belaúnde, probably are

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<sup>22</sup> 115 Cong. Rec. 17355-6 (1969), House of Representatives - Wednesday, June 25, 1969.

<sup>23</sup> *FRUS, 1969-1976*, Volume E-10, Documents on American Republics, 1969-1972, Document 604, Memorandum From the President's Assistant for National Security Affairs (Kissinger) to President Nixon, Washington, July 1, 1969.

<sup>24</sup> *Foreign Relations of the United States, 1969-1976*, Volume E-10, Documents on American Republics, 1969-1972, Document 607, National Security Decision Memorandum 21, Washington, July 22, 1969.

<sup>25</sup> Paul E. Sigmund, *Multinationals in Latin America: The Politics of Nationalization*. Madison: University of Wisconsin Press, 1980, pp. 193-4.

more a show of independence from the U.S. than a serious intention to develop a firm and close relationship ... [Velasco's] personal entourage is composed of men whose views cover the political spectrum from extreme right to extreme left ... There is no evidence so far that the advice or support of the Peruvian Communist parties has been important to Velasco." The CIA went on to report that despite their nationalist and left-wing economic views, "The officers now in the regime ... have uniformly anti-Communist backgrounds."<sup>26</sup> The CIA took a sanguine view of Peru's motions towards the Soviet Bloc. Its fear was not that Velasco might respond to American sanctions by switching sides in the Cold War. Rather, the CIA's fear was that the economic sanctions might cause the Peruvian government to collapse. "It seems likely that as economic strains mounted, the regime and the populace would become increasingly frustrated and emotional. With Velasco in power, the regime could become more radical and begin attacking entrenched Peruvian economic interests, with the result that a revolutionary situation could emerge."<sup>27</sup>

Kissinger had to work to convince Nixon that Velasco was sincere in his anti-Communism. On the Friday after Thanksgiving in 1970—a work day in the Nixon White House—Kissinger sent Nixon a summary of a recent speech Velasco had given on Communism, bringing a particular passage to Nixon's attention: "Intolerance, totalitarianism, bureaucratization are, in the unimpeachable light of history, structural failures of Communist societies and not simply secondary deformations. Therefore, such societies cannot serve as a model for our Revolution. And, therefore, in regard to Communism ... we place ourselves in opposition." This was enough for Nixon, who commented, "Makes sense—perhaps we should make a gesture toward him—as we continue our coolness toward [Chile's] Allende."<sup>28</sup>

Nixon's obsession with executive control led him to establish methods to circumvent the legal requirements of the Hickenlooper Amendment. In this, of course, he was merely continuing a tradition established by Theodore Roosevelt. No one in the Nixon Administration wanted to drive Velasco into the arms of the Soviets over what was, in Kissinger's words, "a lousy company." Nixon's policy towards Peru aimed to ensure the Velasco government did not become a foreign policy ally of the Communist bloc (or worse yet, collapse and be replaced by an openly Communist government) regardless of the fate of the IPC. The threat of applying the Hickenlooper Amendment became a

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<sup>26</sup> Central Intelligence Agency, "Peru and the US: The Implications of the IPC Controversy," *Special National Intelligence Estimate*, March 6, 1969, pp. 3 and 13-14.

<sup>27</sup> Central Intelligence Agency, "Peru and the US," p. 25.

<sup>28</sup> *Foreign Relations of the United States, 1969–1976*, Volume E–10, Documents on American Republics, 1969–1972, Document 621, Memorandum From the President's Assistant for National Security Affairs (Kissinger) to President Nixon, Washington, November 27, 1970.

means to that end, not the end itself. By 1970, the Nixon Administration believed that Velasco was a sound enough anti-Communist to ignore his economics in favor of his politics. The Peruvian government would continue to expropriate American firms—including Harold Geneen’s ITT—and the United States would continue to pressure Peru covertly for a settlement, but the automatic mechanism of the Hickenlooper Amendment had been defused by Richard Milhous Nixon.

The Revolutionary Government’s nationalizations did not end with the IPC. In August 1969—six months after it announced that IPC owed Peru \$690 million—it nationalized the sugar industry. Most Peruvian sugar lands were domestically held, but W. R. Grace and Company held a substantial stake. In 1970, it opened negotiations with the Cerro Corporation over the sale of its copper assets. When those failed, the government nationalized Cerro in January 1974. Eighteen months later, in July 1975, it nationalized the Marcona iron mines. All these investments enjoyed USAID insurance against capital controls; the U.S. did not, however, have an agreement with Peru that would have allowed USAID to offer expropriation insurance.<sup>29</sup>

Nixon could afford to sacrifice IPC on the altar of keeping Peru stable—he could not, however, afford to abandon all American interests in the country. In essence, the Nixon Administration sacrificed IPC in order to secure compensation for these other investments and prevent further instability in Peru. Richard Nixon was too good a politician—and too personally appalled by uncompensated expropriation—to believe that he could sacrifice American investments to geopolitical concerns without undue consequences.

**TABLE 1: Peruvian expropriation settlements, 1000s of current dollars**

	Date of loss	Company claim	Nov. 1973 minimum settlement	Share in lump sum	Individual payments	Total
Brown and Root	Feb 1, 1970	\$ 1,234		\$ 100		\$ 100
Cargill Peruana, SA	May 7, 1973	\$ 4,724	\$ 1,300	\$ 1,300	\$ 48	\$ 1,348
Cerro Corporation	Jan 1, 1974	\$ 175,000	\$ 65,000	\$ 10,000	\$ 58,000	\$ 68,000
IPC: La Brea and Pariñas fields, Talara complex, 50% Lobitos refinery, Lima concession, marketing assets	Nov 9, 1968 & Feb 14, 1969	\$ 85,000	\$ 20,000	\$ 22,000		\$ 22,000
General Mills	May 7, 1973	\$ 2,574	\$ 1,100	\$ 1,200		\$ 1,200
Gold Kit SA	May 7, 1973	\$ 3,037	\$ 1,800	\$ 600	\$ 2,242	\$ 2,842
H.B. Zachry Company	Feb 1, 1979	\$ 3,000	\$ 1,000	\$ 1,200		\$ 1,200
International Proteins Company	May 7, 1973	\$ 11,279	\$ 8,600	\$ 8,900		\$ 8,900
Morrison-Knudsen	Feb 1, 1970	\$ 6,991	\$ 2,000	\$ 2,000		\$ 2,000
Socal-Chevron in Conchan refinery	Jun 16, 1972	\$ 3,000	\$ 2,000	\$ 2,000		\$ 2,000
Star-Kist	May 7, 1973	\$ 15,000	\$ 7,175	\$ 7,300	\$ 1,318	\$ 8,618
W.R. Grace and Co.	Feb 14, 1974	\$ 60,185	\$ 20,000	\$ 19,200	\$ 2,805	\$ 22,005
<b>TOTAL</b>		<b>\$ 371,024</b>	<b>\$ 129,975</b>	<b>\$ 75,800</b>	<b>\$ 64,413</b>	<b>\$ 140,213</b>

<sup>29</sup> CIA, “Peru and the US.”

Source: Victor Arnold and John Hamilton, "The Greene Settlement: A Study of the Resolution of Investment Disputes in Peru," 13 *Tex. Int'l L. J.* 263 1977-1978, pp. 286-87.

Nixon, characteristically, bypassed the State Department when sending a negotiating team to Peru. He tapped James Greene, the senior VP of Manufacturers Hanover Trust, to head the negotiations. Greene had been responsible for negotiating large loans to the Peruvian government, and he knew both Spanish and the key players in the Peruvian government. He arrived in Lima on February 19, 1973, without the knowledge of the local U.S. embassy.<sup>30</sup>

Greene canvassed the companies to collect their minimum acceptable compensation levels. In some cases, those levels were significantly below the companies claim before the Peruvian government. Cerro Corporation, for example, initially claimed that its investments were worth \$175 million (\$626 million in 2009 dollars). In July 1972, it offered to sell its operations to the Peruvian government for \$30 million in cash, \$49 million in sales revenue over the next five years, a \$96 million claim on profits over the next seven, and a management fee of \$3.9 million for 15 years.<sup>31</sup> At the 1972 ten-year rate on corporate bonds (7.2%), the net present value of this offer was \$178 million. (In retrospect, inflation would have cut that significantly—even at 1972's inflation rate of 3.3%, the NPV would have come to \$133 million. At the inflation rates which the United States actually wound up experiencing over the next decade, the NPV of the deal would have fallen to \$109 million.) When Greene inquired, however, the company reported that it would accept anything above \$65 million. (See Table 1.)

How did the company arrive at the figure of \$65 million? There are no public records, but there are two ways to estimate the value of the company's Peruvian assets, both of which yield numbers lower than that figure. The book value of the company's fixed assets in 1971 was only \$16.4 million.<sup>32</sup> Book value, of course is an almost meaningless way to determine the value of a company. In 1971, Peru generated 40% of the company's net operating income: 40% of the Cerro Corporation's market capitalization came to \$58 million. (In 1972, Peru generated 45% of the net income: an equivalent calculation would have yielded \$57 million.) Cerro's stock price was depressed by 1972, but so were the share prices of all the major copper companies, most of which had no exposure to Peru and relatively less to Chile. (See Figure 1.)

The ultimate settlement consisted of \$76 million transferred by Peru to the U.S. government, which then doled it out to the claimants, and \$64 million in payments made di-

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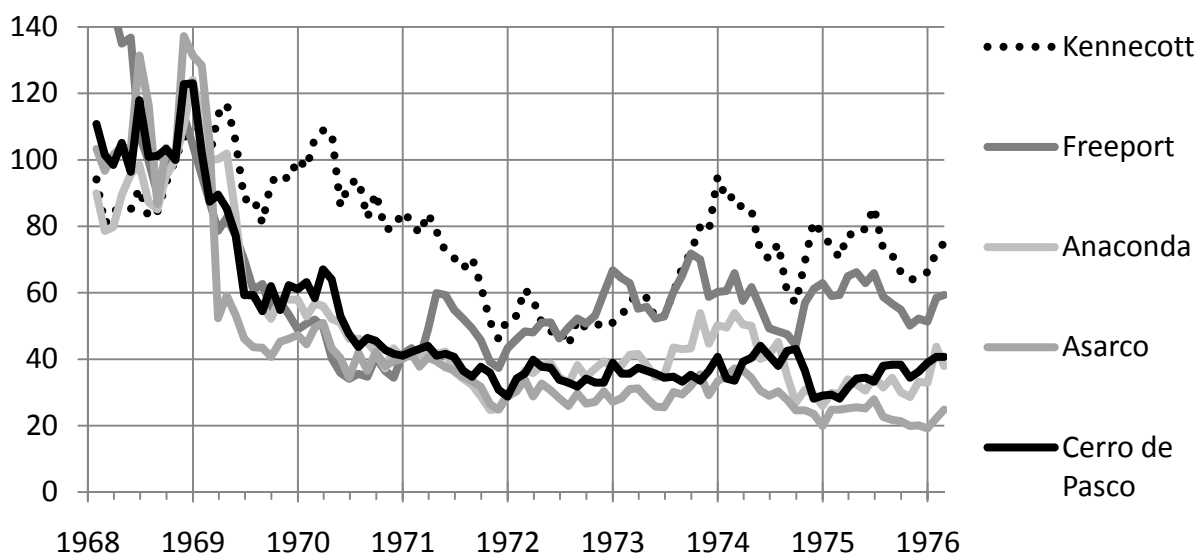
<sup>30</sup> Victor Arnold and John Hamilton, "The Greene Settlement: A Study of the Resolution of Investment Disputes in Peru," 13 *Tex. Int'l L. J.* 263 1977-1978, p. 281.

<sup>31</sup> Arnold and Hamilton, "The Greene Settlement," p. 278.

<sup>32</sup> *Cerro Corporation Annual Report*, 1972.

rectly to the expropriated companies. Most of the companies received close to the reservation compensation that they reported to the U.S. government. IPC received what it claimed for its share in the Lobitos refinery, its unexplored concessions, and its retail distribution assets, but it was not (in theory) compensated for the La Brea and Pariñas fields, or the Talara industrial complex. In the negotiations, the Peruvian government insisted the Nixon Administration not to transfer any of the \$76 million to IPC; the Nixon Administration did not follow through.

**FIGURE 1: Indexed share prices for major copper companies, 1968-76 (October 31, 1968 = 100)**



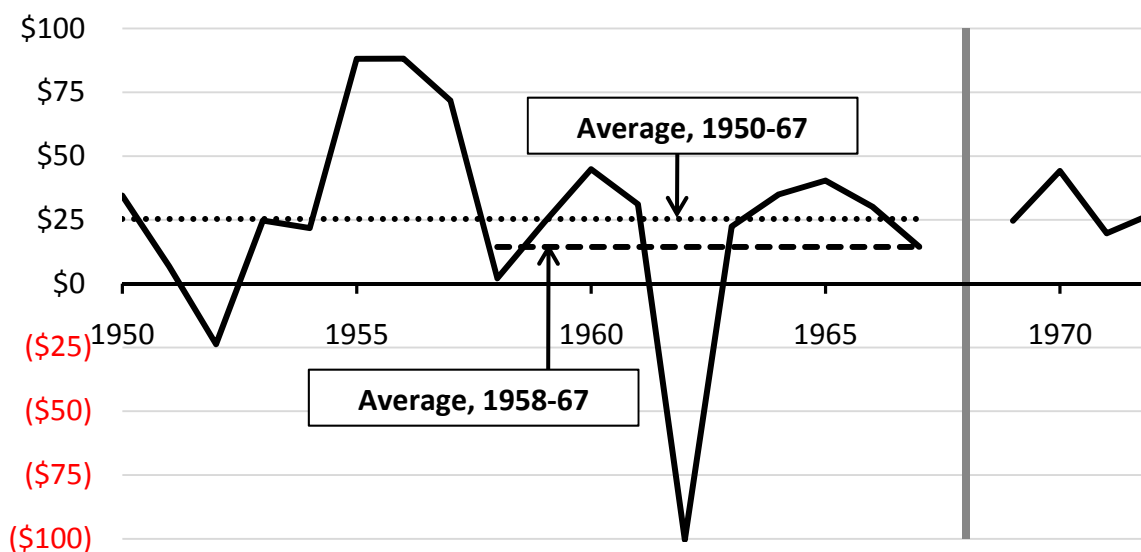
Source: New York Stock Exchange.

The Nixon Administration, of course, managed to extract such a favorable settlement because it wielded a very credible threat against the Peruvian government: the economy was in a parlous state in 1973, and desperately required foreign credit from the World Bank and IMF (or private sources) to keep its economy ticking over. Congressional anger at the expropriations was strong; all sides knew that if they did not come up with something to satisfy the companies, sanctions would crush the Peruvian economy. In order to give Peru the cover it needed, however, the U.S. ultimately hung out IPC out to dry. Stiffing a “lousy” oil company (and an officially Canadian one at that, albeit owned by Exxon) was an acceptable price to pay to get fair compensation for other American assetholders.

Cerro Corporation may have received a market-based compensation—but how badly did IPC lose? The Peruvian government expressed public anger that the U.S. transferred even \$22 million to the company. (It is hard to believe that the Peruvians were unaware that the U.S. government intended to transfer a portion of the settlement to IPC’s coffers.) In nominal terms, the company’s average annual profit over the decade preceding the nationalization was \$1.9 million. Given the riskiness of oil companies in general (small in-

dependent American oil companies enjoyed price-earnings ratio as low as five during the late 1960s), \$22 million appears more than fair. The problem is that such a calculation does not account for inflation. U.S. inflation was low in the 1960s, but it was not zero—in the decade between 1958 and 1967, the U.S. GDP deflator rose 24%. Moreover, compensation did not arrive until 1974, by which point American prices had risen a further 39%. Once inflation is taken into account, IPC’s compensation came to 4.5 times its average annual earnings over the preceding ten years. (See Figure 2.) By that metric, then, IPC was compensated at an adequate rate for a risky oil investment—and it would hard to argue, *ex ante* or *ex post*, that the company’s Peruvian investments were not very high risk.

**FIGURE 2: IPC annual earnings, million 2009 dollars (PetroPerú for 1969-72)**



Source: IPC earnings calculated from data in Rosemary Thorp and Geoffrey Bertram. *Peru, 1890-1977: Growth and Policy in an Open Economy*. New York: Columbia University Press, 1978, p. 278. Depreciation and amortization estimated by the author, using a 9-year average for non-refining investments and 10-years for refineries. PetroPerú earnings from “Economía política de la privatización,” *Revista de la Facultad de Ciencias Económicas de la UNMSM*, No. 2, Vol. 2, Dic 1996, pp. 13-50.

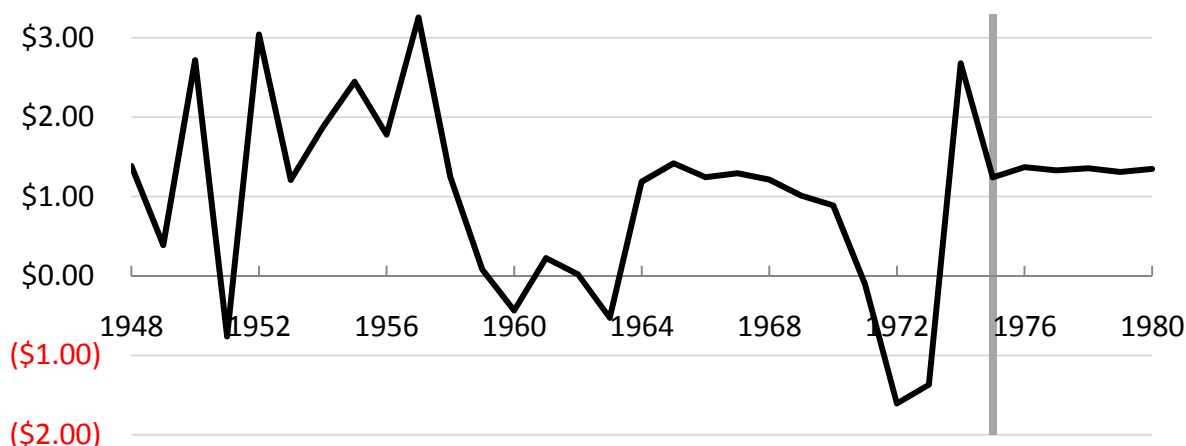
*Venezuela*

Peru was not the last major nationalization of oil assets. Over the course of the early 1970s, most Middle Eastern oil producers (the UAE was a major exception) nationalized the oil companies operating under their jurisdiction. The United States never enjoyed the same freedom of action in the Middle East that it enjoyed in Latin America. The Soviet Union was closer. American pressure could easily push the region’s more radical regimes into Soviet arms. Until 1975, Egypt was effectively a Soviet ally, and Iraq tilted in that direction. Finally, Arab demands for “participation” in the oil business occurred in a climate of rapidly escalating world oil prices, at a time when even a small reduction in supply could

trigger large price increases. In a sense, then, the U.S. avoided the empire trap in the Middle East (at least the economic one described in this book) simply because it was not sufficiently powerful for imperial defenses of American property to be on the table.

Venezuela, however, was in Latin America. American oil investments in that country were not insured by OPIC. Nor had Venezuela signed on to ICSID. Yet when the Venezuelan government nationalized the American oil companies in the country, the result was remarkably uncontentious. Why did the decision to take American property attract so little opposition in the United States? Gerald Ford had taken over the presidency from Richard Nixon on August 9, 1974, after Nixon resigned, but the Ford Administration could nonetheless have taken a much more active stance against the takeover. Since Venezuelan oil was particularly heavy, it could only be refined in specialized facilities, most of which were located in the United States.<sup>33</sup> Moreover, the Venezuelan oil industry required a great deal of investment maintain production, let alone expand it—and foreign capital would be required to finance that expansion. Finally, it is true that in the context of rapidly escalating oil prices, Venezuela did not need American aid, but its government was vulnerable to American diplomatic pressure (and, potentially, covert action)—and unlike Peru, there was little risk that American actions would trigger a move towards the Soviet Union.

**FIGURE 3: Operating income per barrel, private oil companies in Venezuela, 2009 dollars**



*Note:* Post-nationalization income includes the expropriation payments, calculated as the value of the compensation (\$3.15 billion) multiplied by the short-term U.S. interest rate on ordinary funds. By this measure, the value of the expropriation payments came to approximately 19% of post-nationalization revenue.

*Note:* The decline in profitability during the early 1960s and the decline in the early 1970s have different causes. The late 1950s decline was due to the extreme overvaluation of the bolívar; when it was devalued in 1964, operating costs fell precipitously and profits rebounded. The fall in the early 1970s was mostly due to increases in taxes.

*Source:* Data from Manzano and Monaldi and Philip.

<sup>33</sup> Philip, *Oil and Politics*, p. 475.



Why then were the Americans so complacent about Venezuela's nationalization? The reason, quite simply, is that they did not need to oppose the nationalization, because there was almost nothing at stake. The Venezuelan government compensated the oil companies in a manner quite similar to the "participation" agreements worked out with most of the Middle Eastern oil producers. First, the companies received a lump-sum payment for their assets. It is far from clear how the parties involved calculated compensation, but we do know its value: \$1.02 billion in nominal terms, or \$3.15 billion in 2009 dollars.<sup>34</sup> Second, the companies received a per barrel fee for all oil produced that ranged between 16¢ and 19¢, or 49¢ - 59¢ in 2009 dollars (depending on the company). Third, the companies received annual technology licensing payments of 700 million bolívars, or \$163 million (\$503 million in 2009 dollars). The companies also received marketing contracts to sell Venezuelan oil in international markets.<sup>35</sup>

It is important to note that under the Oil Act of 1943 all Venezuelan oil concessions were scheduled to expire in 1983, with *no* right to compensation.<sup>36</sup> The companies were not, therefore, negotiating over their right to enjoy income from their property; rather, they were negotiating over the returns that they would earn for an eight-year period between 1975 and 1983.

Unsurprisingly, given these terms, per barrel revenues for the major oil companies that had been operating in Venezuela did not decline after nationalization. According to Osmel Manzano and Francisco Monaldi, "Former multinational oil executives interviewed argue that nationalization was at that point almost promoted by the oil multinationals. Their goal was to obtain lucrative distribution agreements that they thought would be more stable."<sup>37</sup> In effect, Venezuela designed a non-expropriation expropriation that guaranteed the oil companies their income for at least as long as their concessions would have lasted.

### *Conclusion*

The iconic Latin American expropriations of the late 1960s and early 1970s turn out to have been far less revolutionary than they appeared on the surface. In Peru, the Nixon Administration defanged the automatic sanctions mandated by Congress in regard to IPC, but once the Revolutionary Government moved against other American

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<sup>34</sup> Manzano and Monaldi, "The Political Economy of Oil Contract Renegotiation in Venezuela," mimeo.

<sup>35</sup> Philip, *Oil and Politics*, p. 475.

<sup>36</sup> The Oil Act of 1943 was not a nationalistic piece of legislation. In fact, it extended most of the foreign oil concessions several decades beyond the date at which they would have otherwise expired. Manzano and Monaldi, "Political Economy," pp. 14-15.

<sup>37</sup> Manzano and Monaldi, "Political Economy," p. 23fn37.

assets it quickly reversed itself and extracted a fair compensation—using market values as the definition of fair—from the Peruvian government. In Venezuela, conversely, the Ford Administration had no need to try to reach into the deep toolkit available to all American governments—ranging from diplomatic pressure to covert action—because the settlement offered by the Venezuelan government was extremely favorable to the oil companies. In Latin America, at least, the seeming decline of American hegemonic power in the face of economic nationalism was a mirage.