

ISSUE BRIEF

No. 3695 | AUGUST 7, 2012

Ecuador Should Forfeit U.S. Trade Preferences

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Recently, Ecuador opened a new chapter in its long-running legal campaign against U.S.-based Chevron Corporation. Government-backed lawyers purporting to represent residents of Ecuador’s Amazon rain forest filed a lawsuit to seize Chevron’s assets in Brazil in an attempt to collect a multi-billion-dollar award won last year in an Ecuadorian court.¹ Regrettably, the Chevron case is but one of many recent examples of the destructive anti-free market and anti-democracy policies being pursued by Ecuador’s President Rafael Correa.

Correa Has Weakened Rule of Law in Ecuador. As soon as President Correa was elected in 2006, he began laying the groundwork to bring “21st Century Socialism” to Ecuador. Following the playbook of his political mentor, Venezuelan President Hugo Chávez, Correa

quickly convened a constituent assembly to rewrite the constitution—the 20th in the 182-year history of the Republic of Ecuador.

Former George W. Bush Administration official Jose R. Cardenas noted recently that the “hallmarks of [Chávez and Correa’s] reigns have been class warfare, polarization and intolerance of dissent, and both have rammed through new constitutions that trample on separation of powers and rule of law.”²

Correa also immediately ended anti-narcotics law enforcement cooperation with the U.S. According to the U.S. Department of State’s *2012 International Narcotics Control Strategy Report*, the Correa government closed the door on extending a decade-long agreement to permit U.S. military aircraft to patrol the region from an airbase at Manta, Ecuador, looking for air- and ship-borne illegal drugs. Simultaneously, the report notes that Correa opened the door to “Mexican, Colombian, Russian, and Chinese transnational criminal organizations [that] are present and actively working in Ecuador.”³

Additionally, Correa’s reign has created a nation of corruption and distress:

- Over 50 percent of Ecuador’s population lives below the poverty line,
- Constitutional amendments passed in 2011 increased Correa’s control of the media and the judicial system, and
- Correa has also worked to undercut the Inter-American Human Rights Commission and is working with Chávez to broaden Ecuador’s links with Iran.

Environmentalism and the End of Free Trade. Re-elected in 2009, Correa has ended free trade negotiations with the U.S. He has also ramped up claims against U.S. companies. In the case of Chevron, Ecuador claims that the rain forest was contaminated by oil operations in the Ecuadorian Amazon dating back to the 1970s involving Texaco, which Chevron bought in 2001. Chevron makes a compelling case that the \$18.2 billion judgment against it by an Ecuadorian court was obtained fraudulently and notes that in filing the case in Brazil (after already filing a similar case in Canada), the Republic of Ecuador is in direct violation of an award by an international tribunal at The Hague.

This paper, in its entirety, can be found at <http://report.heritage.org/ib3695>

Produced by the Center for International Trade and Economics (CITE)

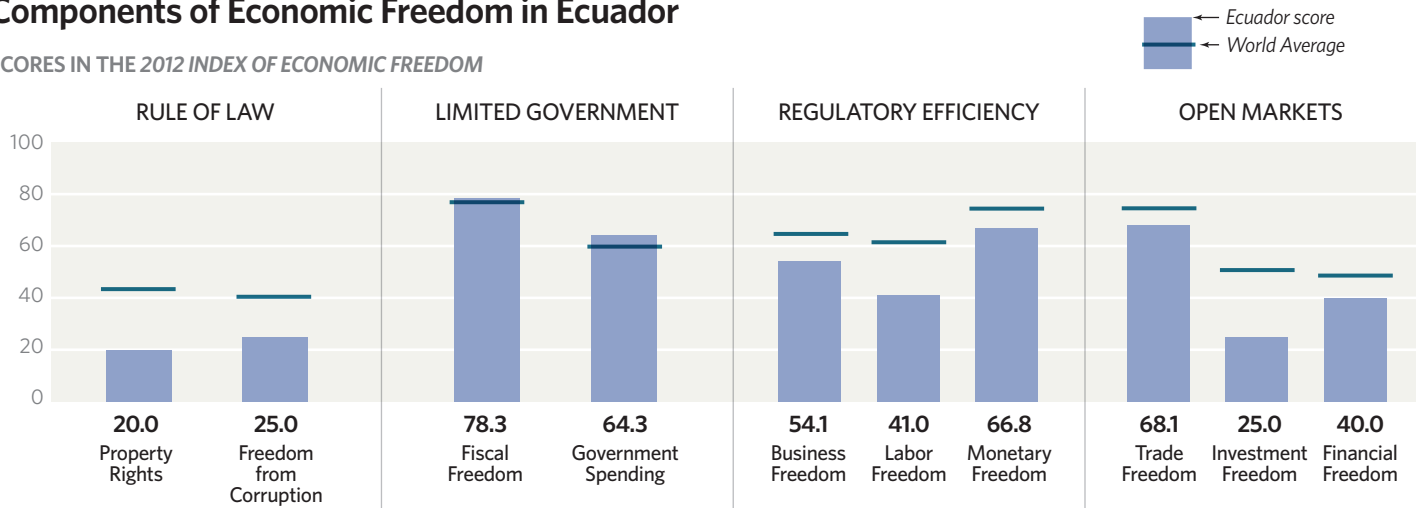
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CHART 1

Components of Economic Freedom in Ecuador

SCORES IN THE 2012 INDEX OF ECONOMIC FREEDOM



Sources: Terry Miller, Kim R. Holmes, and Edwin J. Feulner, *2012 Index of Economic Freedom* (Washington, D.C.: The Heritage Foundation and Dow Jones & Company, Inc., 2012), at <http://www.heritage.org/index>.

IB 3695 heritage.org

The two enforcement actions were filed in the face of the tribunal's Second Interim Award ordering the Republic of Ecuador—and all of its branches, including the judiciary—to prevent enforcement and recognition of the \$18.2 billion “Lago Agrio” judgment both “within and without Ecuador.”²⁴ The second award expanded on a prior award requiring Ecuador to “take all measures at its disposal to suspend or cause to be suspended the enforcement or recognition within and without Ecuador of any judgment.”²⁵ Both binding awards were mandated under the terms of the U.S.–Ecuador Bilateral Investment Treaty (BIT).

Ecuador has had many opportunities to fulfill the binding award mandated by the BIT arbitration panel in The Hague. To date, however, it has not taken *any* measures, let alone “all measures necessary” to meet its obligation. Instead, Correa has denounced the arbitral award, and an appellate court in Ecuador has taken steps to continue the judicial process against Chevron, essentially repudiating the arbitral award. Rather than acting in good faith, Ecuador has acted with contempt for the arbitral process and for the award favoring a U.S. firm.

Ecuador's disregard for the award amounts to encouragement to the

plaintiffs in the case, who have now sought to enforce the fraudulent judgment in Canadian and Brazilian courts. Yet Ecuador has still taken no steps to forestall enforcement of the judgment in order to preserve the status quo while the BIT arbitration proceeds.

Moreover, Chevron is not the only one complaining about the treatment of American companies in Ecuador. In testimony before the Senate Foreign Relations Committee on July 31, Jodi Bond of the U.S. Chamber of Commerce noted that “not only has Ecuador withdrawn from the World Bank's Convention on the Settlement of Investment Disputes between

1. Cassandra Sweet, “Update: Ecuador Plaintiffs Sue Chevron in Brazil,” *Nasdaq*, July 27, 2012, <http://www.nasdaq.com/article/update-ecuador-plaintiffs-sue-chevron-in-brazil-20120627-01495> (accessed July 31, 2012).
2. Jose R. Cardenas, “Meet Latin America's Next Hugo Chavez,” *The Washington Times*, April 6, 2012, <http://www.washingtontimes.com/news/2012/apr/6/meet-latin-americas-next-hugo-chavez/> (accessed August 2, 2012).
3. U.S. Department of State, *2012 International Narcotics Control Strategy Report*, March 7, 2012, <http://www.state.gov/j/inl/rls/nrcrpt/2012/vol1/184099.htm#Ecuador> (accessed August 2, 2012).
4. *Chevron Corporation and Texaco Petroleum Company v. The Republic of Ecuador*, PCA case 2009-23, Arbitration Tribunal, February 16, 2012, <http://www.chevron.com/documents/pdf/ecuador/SecondTribunalInterimAward.pdf> (accessed August 6, 2012).
5. *Ibid.*

States and Nationals of Other States and stated its intention to terminate the U.S.–Ecuador BIT,” but Ecuador’s “disregard for international standards of justice and its own treaty obligations...sends a negative message to the global business community contemplating making investments in Ecuador.”⁶

The U.S. State Department, in its “2012 Investment Climate Statement” about Ecuador, warns that “the legal complexity resulting from the inconsistent application and interpretation of its existing investment laws complicates enforcement of contracts and increases the risks and costs of doing business in Ecuador.”⁷ Ecuador’s scores were very low on the rule of law indicators in the 2012 *Index of Economic Freedom*, published annually by The Heritage

Foundation and *The Wall Street Journal* (143rd in property rights and 129th in freedom from corruption out of 179 countries).⁸

Restore U.S. Influence. The actions (and inactions) of the Ecuadorian government provide strong justification for removing Ecuador’s trade preferences under the Andean Trade Promotion and Drug Eradication Act (ATPDEA) and the Generalized System of Preferences (GSP) program. In late 2011, ATPDEA was extended by Congress through July 2013. In March 2012, similar behavior by Argentina led the U.S. government to suspend its GSP benefits. Similarly strong action should now be taken against Ecuador.

The rise of Hugo Chávez and his protégés has signaled a depressing

return to the days of leftist “caudillos” (strongmen) who ruled Latin America in decades past. Correa may have seemed an unlikely caudillo, but his actions to date demonstrate a blatant disregard for international standards of justice.

In response, the U.S. should increase its influence in the region through additional support for democratic, market-based institutions. A strong and resolute U.S. government should seek to encourage true reform in the region.

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6. Jodi Bond, “Doing Business in Latin America: Positive Trends but Serious Challenges,” testimony before the Subcommittee on the Western Hemisphere, Peace Corps and Global Narcotics Affairs, Committee on Foreign Relations, U.S. Senate, July 31, 2012, http://www.foreign.senate.gov/imo/media/doc/Jodi_Bond_Testimony.pdf (accessed August 2, 2012).
7. U.S. Department of State, “2012 Investment Climate Statement,” June 2012, <http://www.state.gov/e/eb/rls/othr/ics/2012/191141.htm> (accessed July 31, 2012).
8. Terry Miller, Kim R. Holmes, and Edwin J. Feulner, *2012 Index of Economic Freedom* (Washington: The Heritage Foundation and Dow Jones & Company, Inc., 2012), p. 176, <http://www.heritage.org/index/download>.