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BRIEFING PAPER ON CHILE

Preliminary reports by Ambassador Davis indicate the following points concerning the new Chilean junta's attitude toward the United States. General Pinochet, in a meeting with the U.S. Military Group Officer, indicated (1) a fundamental desire to strengthen and further traditionally friendly ties with the U.S., (2) to work out a mutually acceptable solution with the U.S. on the issue of copper compensation, and (3) to break relations with Cuba, USSR, North Vietnam and North Korea.

This memorandum explores three points concerning future policy toward Chile:

- (1) Nationalization problems,
- (2) Debt rescheduling, and
- (3) Multilateral assistance.

1. Nationalization

We have been at loggerheads with the Allende Government over the expropriation without compensation of a large number of American-owned properties, especially the copper mines and the ITT Chile Telephone Company. After obtaining some commitments from the Chileans to repay debt and negotiate on compensation through the Paris Club, we have had an extended series of bilateral meetings with the Chileans in an effort to work out a framework for beginning to talk about compensation. The Chileans offered to use a fact finding commission under a 1914 Dispute Settlement Treaty which we considered to be a stalling technique. We, in turn, offered binding arbitration which the Chileans said they could not accept.

As a result of our inability to reach any kind of agreement on expropriation issues and because of the mess which Allende made of the Chilean economy, the World Bank and the IDB have held back on lending to Chile. In these conditions, the Paris Club has limited or postponed granting debt relief to Chile.

A key to U.S. approval of IFI lending and to U.S. participation in multilateral debt rescheduling is a rapprochement on the expropriation issues. This memorandum proposes a future policy on these two issues assuming such a rapprochement. It then examines our policy options on the kind of commitment we should require from the Chileans on the expropriation issues.

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2. Debt Rescheduling

Since early 1972 the U.S. has been participating in the Paris Club group of creditors, which was convened by the Allende Government to consider debt relief. In April 1972, the Paris Club agreed to reschedule 70 percent of Chile's debt repayments due in the November 1971-December 1972 period. Chile is in default on 1973 debts, and is therefore enjoying 100 percent relief. In July, the Paris Club decided to postpone any consideration of formal debt relief until October when Chile is expected to present a stabilization program. Even with this relief, however, Chile is still faced with a considerable foreign exchange gap. Therefore, debt relief is an essential ingredient in restoring stability in Chile.

Assuming good faith negotiations on the nationalization issues, we can support new formal debt relief for Chile and sign a bilateral covering relief for 1972 already approved by the Paris Club. The importance of formal debt relief is that it is a necessary condition for Chile to obtain new credits from the U.S. and other countries. However, a bilateral agreement would require Chile to make a lump-sum payment of \$42 million and consideration would have to be given to avoiding this result.

We should use the Paris Club as the appropriate forum for providing debt relief, rather than extending it bilaterally. A multilateral forum is essential in order to (1) keep a low profile, (2) maintain the precedent of the multilateral approach thus assuring fair participation by all creditors, and (3) make Chile eligible for new assistance from the creditors who cannot make new assistance available in the current default situation.

As an essential part of debt relief, we should strongly urge an effective stabilization program, including an IMF stand-by or reasonable equivalent. The last Chilean Government wanted to avoid a stand-by, departing from the usual precedent for debtors seeking debt relief. A stabilization program is in any case a necessary condition of Chilean recovery. Agreement to undertake a stabilization program would also publicly demonstrate an even-handed approach on our part toward both the old and new government.

3. IMF Assistance

If Chile is willing to undertake an IMF stand-by agreement and stabilization program, Fund resources would become available to Chile, probably totaling \$86 million. In similar circumstances in the past, this was Managing Director Schweitzer's approach. New Managing Director Witteveen has yet to take a position. This balance of payments aid would go a part way toward meeting Chile's new financial needs estimated at over \$800 million by IMF for the coming year.

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#### 4. Multilateral Development Lending

There are a number of loans pending in the IBRD and IDB totaling about \$160 million. Again assuming good faith negotiations on compensation, some of these loans could be quickly moved forward for Board approval. However, since these are project loans, they can only be viewed as a source of longer-term assistance and not as a means of meeting some of the immediate needs of the Chilean balance of payments. The World Bank and the IDB could explore the possibility, however, that a fast disbursing program type loan might be negotiated to give Chile more immediate relief.

The IBRD Board is scheduled to vote on two loans for \$8.3 million after the next Paris Club meeting (which is now scheduled for late October). These two loans were negotiated by the Bank management with the previous Chilean Government for the purpose of refinancing loan repayments to the Bank due in 1973-74. They were originally placed on the Board agenda for September 4. We strongly opposed having these loans considered by the IBRD before the Paris Club had had an opportunity to review Chile's stabilization package. As a result of our opposition, consideration of these loans was postponed until after the next Paris Club meeting. Assuming a satisfactory arrangement on negotiating compensation and a reasonable stabilization program, the U.S. should be able to support these loans. Assistance through debt rescheduling, the IMF, and through the development banks (to the extent that it can be provided) can only provide a part of the financial assistance which Chile needs. U.S. bilateral programs can make a contribution. In addition, we should also look for substantial assistance from other countries such as Spain, the U.K., Japan and other Paris Club countries and from Brazil, Argentina and perhaps Mexico, as well as from the private banking community.

#### 5. Options on Good Faith Negotiations

The following approaches might be considered as acceptable evidence of Chile's willingness to enter into good faith negotiations. The existence of good faith negotiations obviates the need to apply the President's expropriation policy as well as legislative sanctions in case of expropriation without compensation.

- (1) Accept our offer of binding arbitration or some variation of it whereby they will agree to implement an international judgment, or
- (2) Agree to review President Allende's determinations of excess profits, or

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- (3) Initiation of negotiations on compensation with the copper companies, or
- (4) A public statement of willingness to negotiate with the U.S. a mutually acceptable solution to compensation issues.

Binding arbitration would clearly meet our requirements in that it would establish a procedure leading to a definitive solution. A promise to review and reduce President Allende's finding of excess profits might also be considered acceptable since it could allow the original Chilean determinations of compensation to stand and could provide our companies with a fair arrangement. A public statement of willingness to negotiate with the companies or with the United States is a minimum step. It should be acceptable only if the Chilean Government clearly understands that expropriation policy would be reapplied if speedy progress was not made toward achieving a settlement.

We should, at least as a tactical matter, raise the ITT compensation issue as among those issues covered by the Chilean good faith negotiations commitment. The new government may be willing to tackle this problem. However, if they cannot do so at this time, we should be willing to avoid the issue for the time being through a general Chilean statement on good faith negotiations, while making it clear to the Chileans that this problem must also be solved.

Our position in Peru could serve as a precedent for guiding our actions in Chile. In Peru, we have taken a broad statement of willingness to negotiate as evidence of good faith negotiations. However, we warned the Peruvians that unless a prompt settlement is reached, we would have to reapply our expropriation policy. Assuming the same kind of good faith commitment from the Chilean military, we could be willing to resume normal financial relations.

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