To the Graduate Council:

I am submitting herewith a thesis written by Christopher David Kane entitled "The Effect of Offshore Securities Operations on Third World Development: The Case of Costa Rica." I have examined the final copy of this thesis for form and content and recommend that it be accepted in partial fulfillment of the requirements for the degree of Master of Arts, with a major in Political Science.

Robert L. Peterson
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We have read this thesis and recommend its acceptance:

Accepted for the Council:

Vice Chancellor
Graduate Studies and Research

THE EFFECT OF OFFSHORE SECURITIES OPERATIONS ON THIRD WORLD DEVELOPMENT: THE CASE OF COSTA RICA

A Thesis

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ABSTRACT

In this study, the relationship between the International Controls Corporation and the government of Costa Rica was examined in an effort to determine the extent to which certain transnational actors affect the process of development in certain Third World states.

The method used to examine this relationship was the case-study. After identifying both the Costa Rican Government and the International Controls Corporation, and delineating their respective resources and points of access, an analysis of their relationship was attempted. This analysis revealed that although International Controls, in the person of Robert Vesco, was able to capture the Costa Rican executive, it was unable to co-opt other sectors of the Costa Rican political establishment. Specifically, the legislature, the judicial branch, the opinion leaders, and the political parties rejected International Controls, fearing that its demands upon domestic political resources outweighed any potential economic benefits.

From the perspective of the study of transnational relations, the broader implications of this study are most significant. While transnational business enterprises operate throughout the Third Word, few Third World states possess the political resources necessary to control the

activities of the transnationals. It is feared that such states will sacrifice a measure of their political autonomy in an effort to secure the not inconsiderable economic benefits offered by transnational businesses.

The solution, as proposed in this paper, is some form of regulation of transnational businesses, particularly offshore securities operations. Because of the special characteristics of offshore securities operations and the states in which they operate, the most effective form of regulation would be a type of international securities and exchange commission. The existence of such a body would allow the Third World to take advantage of the regulatory expertise of the industrialized states and to enjoy the economic advantages of hosting a transnational business without suffering any direct political dislocation.

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CHAPTER I

INTRODUCTION

In this paper, the relationship between the International Controls Corporation and the government of Costa Rica will be examined in order to advance the study of transnational relations, which Keohane and Nye define as, "contracts, coalitions, and interactions across state boundaries that are not controlled by the central policy organs of governments."[1] Though transnational relations take many forms, scholars have largely limited their attention to a few select areas. According to Strange:

> . . . scholars who have written about transnational relations in recent years have discriminated. They have not been much interested in the many, varied (and often colorful) transnational relations of the world of fashion, sport, or entertainment. They have been particularly interested in economic transactions and activities taking place across state limits, and especially those perceived to affect state policies and inter-state relations.[2]

Insofar as it concerns one type of transnational actor, a transnational business enterprise, and one state, Costa Rica, this paper can be viewed as an extension of this

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[1]Robert O. Keohane and Joseph S. Nye, eds., Transnational Relations and World Politics (Cambridge, MA: Harvard University Press, 1970), p. xi.

[2]Susan Strange, "The Study of Transnational Relations," International Affairs (London), July, 1976, p. 334.

concern. Before proceeding with the background of this study, it is first necessary to state its theoretical foundations.

A. Theoretical Foundations of the Study

Given that the central issue of this study is the relationship between a transnational business enterprise and a sovereign state, it is necessary to specify certain basic concepts and assumptions. The specification of these concepts and assumptions derives from two important theoretical foundations: the traditional "state-centric" paradigm and the "transnational actor" paradigm proposed by Keohane and Nye.

Lijphart, in his discussion of the theoretical revolution in international relations, contends that the field is rich in theory. Using Kuhn's terminology, he identifies the various paradigms upon which the field relies:

> The traditional paradigm in international relations revolves around the notions of state sovereignty and its logical corollary, international anarchy. The sovereign states, recognizing no higher authority, are in an international state of nature; the resulting security dilemma forces them to live in a condition of mutual competition and conflict.[3]

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[3]Arend Lijphart, "The Structure of the Theoretical Revolution in International Relations," International Studies Quarterly, March, 1974, p. 43.

The notion of sovereignty is central to this study. As there presently exists no form of world government to which the various states have relinquished their sovereignty, international anarchy still exists. In the modern world, international anarchy takes several forms; among the most serious is the dislocation which results from interstate conflict. However, another, equally serious form of international anarchy results when transnational actors, such as transnational business enterprises, take actions which adversely affect the various states in which they operate. Thus, the traditional paradigm must be complemented by another paradigm which accommodates both the notion of sovereignty and the existence and inevitability of transnational actors, particularly transnational business enterprises. Keohane and Nye have proposed such a framework:

> Nye and Keohane sketched out possible methods as well as the chief purposes they conceived for the study of transnational relations. It could be done by analyzing them in specific "issue areas" (areas of government policy and activity); by case studies of particular transnational "actors"; by analyzing the interaction or linkage between issue areas in which transnational relations forces or actors played a significant part. Mostly, the purpose of such studies was to consider the effects on states, on the objectives and policies of governments, and on intergovernmental organizations. One of the five sets of questions they proposed for consideration suggested, in general terms, that "who gets what" in the world system—in terms of welfare, security, relative autonomy—should also be included in the objectives of international

> political economy of which they correctly saw transnational relations as one aspect or part.[4]

Having looked at the development of scholarly interest in transnational relations from a theoretical perspective, three basic questions arise:

1. Are the activities of transnational actors legitimate?
2. Do certain states, or certain categories of states, have political or legal resources to limit or control the activities of transnational actors? If so, what are these resources?
3. Do certain transnational actors, or certain categories of transnational actors, have negative or positive effects on the sovereignty of these states? If so, what are these effects?

In an effort to answer these questions, this study will focus upon the relationship between the International Controls Corporation and the government of Costa Rica, using the case-study method, as Keohane and Nye suggest. The specific objectives of this study are stated below:

1. To identify and describe the International Controls Corporation and its activities and to locate this firm among the universe of transnational business enterprises,

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[4]Strange, p. 336.

2. To examine the configuration of political, legal, and economic resources from which Costa Rica may draw in dealing with a transnational business enterprise,
3. To provide a descriptive analysis of the relationship between International Controls Corporation and Costa Rica, and
4. To draw conclusions about the nature of state-transnational actor relationships by answering the questions posed above.

Before sketching the background to this study and reviewing the literature, it is first necessary to take a brief look at the historical development of scholarly interest in transnational relations, noting the evolution from state-centric approaches to the accommodation of transnational actors, particularly transnational businesses, within the field.

B. Historical Development of Scholarly Interest in Transnational Relations

The scope of the field of international relations prior to 1920 was limited to the study of the conduct of diplomatic relations among individual states. This seemingly narrow area of concern was inevitable, for prior to the present century, nation-states were the only recognized actors in the international system. Those transnational entities

which did exist, such as transnational religious and labor organizations, were limited in scope and of little interest to the scholarly community.

With the demise of the European balance of power after the first World War, the resulting development of the League of Nations turned the attention of scholars to transnationalism. Despite the League's early demise and its failure to achieve its goals, the study of transnational organizations continued to flourish and became a legitimate subfield of international relations. The establishment of the United Nations and the various regional and functional organizations after World War II ensured that the study of transnational entities would remain a respectable and current area of study.

While the study of transnational governmental organizations continues to be a viable field, the rise of a new type of transnationalism has caused specialists in international relations to focus their attention in yet another direction. Recently, a body of literature has arisen which deals exclusively with the nongovernmental organization and its place in the international system.[5]

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[5]According to Keohane and Nye, two of the best examples of this literature are John W. Burton, Systems, States, Diplomacy, and Rules (Cambridge: Cambridge University Press, 1968), and James N. Rosenau, Linkage Politics: Essays on the Convergence of National and International Systems (New York: Free Press, 1969).

Though nongovernmental organizations take many forms, the most popular object of study has been the transnational business enterprise, often referred to as the multinational corporation. One of the questions which scholars have raised concerns the effects which transnational businesses have on the states in which they operate. As might be expected, the scholarly community is divided on the issue of the legitimacy of the transnational business enterprise. As Bennett points out:

> Projections of current growth trends indicate an increasing influence of the multinational corporation in world politics during the remainder of the century. Reactions to this future influence vary from welcoming the process as the key to an emerging world community to pointing with alarm to the prospect of irresponsible concentrations of economic power in the hands of an elite. The future role of the multinational business enterprise in perpetuating or closing the gap between rich and poor nations is also an area of interest and concern.[6]

Those who are chary of the motives of transnational business cite the example of the International Telephone and Telegraph Corporation's collaboration with the CIA in the overthrow of former Chilean president Salvadore Allende as proof of the irresponsible nature of transnational business. Defenders of the transnational business enterprise

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[6]A. Leroy Bennett, International Organizations: Principles and Issues (Englewood Cliffs, NJ: Prentice Hall, 1977), p. 361.

disregard the ITT case as an exception to the rule of nonintervention in national affairs.[7]

In addition, the latter group points to the role of international law in regulating the behavior of transnational businesses. Their contention is that the threat of expropriation, or nationalization, is an effective check on the latent interventionist tendencies of transnational businesses. Indeed, international law recognizes the right of states to expropriate the holdings of foreigners. According to von Glahn:

> Lay opinion to the contrary, every government possesses the right of expropriation, of eminent domain. The law of nations demands respect for private property, but it recognizes the right of the state to derogate from this principle when its superior interest so requires. Thus it allows expropriation in time of peace and requisition in war. Expropriated property may be foreign or domestic: no distinction need be drawn by the seizing government, except in the case of foreign-owned public (state-owned) property. This principle has been affirmed again and again by international tribunals.[8]

Despite the legality of nationalization, there are recognized limits upon its exercise. Von Glahn cites seven

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[7]For a staunch defense of the role of the transnational business enterprise in the international system, see Monroe E. Spaght, The Multinational Corporation: Manners, Methods, and Myths (Pittsburgh: Carnegie-Mellon University Press, 1978), and John K. Gailbraith, "In Praise of Multinationals," New Statesman, 10 February 1978, pp. 175-178.

[8]Gerhard von Glahn, Law Among Nations (New York: Macmillan Publishing Co., 1976), pp. 233-234.

such limits, the most important being that, "the taking must be by a foreign national government,"[9] and "Prompt, effective, and adequate compensation must be paid."[10]

Having noted that the host country does have a legal resort when dealing with a transnational business enterprise, it is important to emphasize that the decision to take action against such a firm often has extra-legal ramifications. In this regard, Berman notes that:

> The host government is caught in a love-hate syndrome. It wants the contributions to wealth and economic growth that the multinational enterprise can provide because they add to its power within the country, as well as internationally. At the same time it dislikes and fears the results: the incursions on national sovereignty and technological dependencies. The host government finds the multinational enterprise difficult to live with, but, so long as it seeks to increase national power, equally unpleasant to live without . . . . It appears to the host government that a trade-off may be required between sovereignty and greater wealth.[11]

In the case of many Third World states, this acquisition of greater wealth of which Berman speaks is inextricably bound up with the process of modernization, or national development. Though there is widespread disagreement about the precise definition of development, it is generally recognized to be a three-part process with political, social, and economic components. Many scholars contend that the

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[9]Von Glahn, pp. 233-234. [10]Ibid.

[11]Quoted in Bennett, p. 367.

economic aspect of development is most important. Representative of this perspective are Halper and Sterling, who assert:

> Generally the economic system has been credited with a clearly primary role; growth is spurred through investment and trade from the more developed centers (nationally and internationally) to the less developed areas . . . the resulting economic development is credited with promoting modernization in the social and political spheres by creating the resources for increased education and communication, an open system of status and mobility, and a general shift in the organizing principles of the society toward more "modern" principles of social action.[12]

However, the closer one looks at the process of national development and modernization, the more evident it becomes that the transnational business enterprise is not directly concerned with the situation of the host country. Commenting on the performance of U.S.-based transnational businesses in this regard, Halper and Sterling conclude:

> . . . one can hardly deny that American businessmen have been primarily motivated to increase their capital and profits, not necessarily to develop balanced national economies.[13]

Though Halper and Sterling's is fundamentally a Marxist argument, its theme has been echoed by other scholars concerned with the relationship between national development and the transnational business enterprise.[14]

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[12]Stephan A. Halper and John R. Sterling, Latin America: The Dynamics of Social Change (New York: St. Martin's Press, 1972), p. vi.

[13]Ibid., p. xvi.

[14]Raymond Vernon has been perhaps the most consistent critic of transnational business in this regard. See his Sovereignty at Bay (New York: Basic Books, 1971).

In brief, many scholars in recent years have observed the activities of transnational actors, particularly transnational businesses, and have noted the impending clash of interests between such entities and sovereign states. There have, however, been few efforts to develop a systematic theory about such behavior; in that regard, the work of Keohane and Nye is notable.

Among the methods suggested by Keohane and Nye for determining "who gets what" in an international system characterized by frequent interaction between transnational actors and sovereign states, the case-study is perhaps the most useful. Though case-studies focus on one state-transnational actor relationship, there are instrumental in the development of categories and classifications by which the theory of transnational relations can be enriched. In the following section, the case-study of the International Controls Corporation activities in Costa Rica will be sketched.

C. Background of the Case-Study: International Controls Corporation in Costa Rica

In 1971, Robert Vesco, the owner of a group of disparate, debt-ridden American businesses called the International Controls Corporation, acquired a controlling interest in the Investors Overseas Service. Investors Overseas Service, or IOS, ostensibly a Swiss mutual fund, was actually a series

of four investment trusts located in Luxemborg, Canada, and the Netherlands Antilles in which thousands of investors worldwide had entrusted over 200 million dollars. By locating the funds "offshore," in states and territories where regulations governing the management and dispersal of investment securities were minimal, IOS founder Bernard Cornfeld was able to employ questionable management practices, withholding investors dividends and reinvesting them surreptitiously for his own profit.

When IOS issued a request for emergency capitalization in 1971, Vesco offered to provide the necessary financing. In a series of deft manuevers, Vesco wrested control of IOS from Cornfeld, using the four investment trusts as a pool of capital to service the debts of the less profitable International Controls subsidiaries.

From the perspective of this study, it is significant to note the manner in which the IOS dollars were "reinvested." Evidence suggests that Vesco, realizing the vast profit potential in the unregulated offshore world, intended to create an autonomous offshore haven in the Carribean or Central America. To that end, he made sizeable investments in the Bahamas, Panama, and Costa Rica, claiming that his interest in Third World development prompted the transactions; actually, the investments were designed to gain the favor of the various governments, to act as inducements to participate

in Vesco's plan to create an international "free-trade" zone in the region.

From the United States, Vesco's activities were viewed with increasing alarm. The Securities and Exchange Commission began an investigation which culminated in the suspension of trading of International Controls' stock and the placement of the company in receivership. In addition, political scientists expressed concern for the viability of the governments of the states in which Vesco had invested. It was feared that, in states plagued by troubled economies, Vesco's holdings would translate into political power.

This concern was particularly acute in the case of Costa Rica. Long recognized as a bastion of stable, popular government, Costa Rica has received high marks for its political development. For example, in a work on comparative legislatures, Mezey asserts that the Costa Rican Legislative Assembly is second only to the United States Congress in independence of the executive branch.[15] Almond and Coleman, in a study of political modernity, determined that Costa Rica had a competitive political system with a "mixed" degree of political modernity.[16]

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[15]Michael J. Mezey, Comparative Legislatures (Durham, NC: Duke University Press, 1978), chapter two, "Comparing Legislatures."

[16]Gabriel A. Almond and James S. Coleman, The Politics of Developing Areas (Princeton, NJ: Princeton University Press, 1960), pp. 532-534.

Despite the remarkable state of Costa Rica's political development, efforts at achieving overall development have been frustrated by a worsening economy. With no significant natural resources and a two-crop agricultural economy, Costa Rica is forced to rely heavily upon foreign investment to maintain economic viability. In an effort to attract foreign investment, Costa Rica offers tax incentives to those willing to participate in the country's economic development plan. Upon hearing of Vesco's sizeable investments in various Costa Rican businesses and in the government itself in the form of bond purchases, political economists feared that Vesco was attempting to exploit his privileged status as an investor and eventually establish an autonomous offshore zone in Costa Rica.

Within Costa Rica, Vesco's presence met mixed reaction. While the business community hailed him as the country's economic savior, others claimed that his presence contributed to corruption and political dislocation. In a statement typical of the allegations against Vesco, Jose Figueres, former president of the republic and himself a recipient of a loan from Vesco's firm, asserted:

> Many members of the congress in this country as well as the current president were elected with Vesco's money. President Daniel Oduber had a large part of his campaign paid for by Vesco.[17]

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[17]"Don Pepe," New Republic, 23 April, 1977, p. 14.

In this paper, an effort will be made to examine the relationship between the International Controls Corporation and the government of Costa Rica, not as an isolated case, but as one instance of the broader phenomenon of the clash of interests between a sovereign state and a transnational actor.

D. Review of the Literature

For the nonlawyer, there are virtually no sources available on offshore securities operations. One's information must be gleaned from occasional articles in business publications such as Fortune, Forbes, and Business Week. This paper relies heavily upon these sources.

On the International Controls Corporation and Investors Overseas Service, two book-length sources proved invaluable in identifying the industry as a whole and the two firms in particular. These are Raw, Page, and Hodgson's, Do You Sincerely Want to Be Rich: The Story of Bernard Cornfeld and the IOS,[18] and Robert Hutchison's, Vesco.[19]

Lamentably, political scientists in the United States have been inattentive to Costa Rican political developments.

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[18] Do You Sincerely Want to Be Rich: The Story of Bernard Cornfeld and the IOS (New York: Viking Press, 1971).

[19] Vesco (New York: Praeger Publishers, 1974).

Few works are available, and many of those which are available are dated. Furthermore, few works by Costa Rican authors are available in the U.S., and much of what can be found suffers from a lack of objectivity which makes it unfit for inclusion in a project of this nature.[20] Consequently, the chapter on Costa Rican politics relies mainly upon journal articles by March, Busey, and Anderson.

For the most part, the case-study was compiled from various periodical sources, the New York Times and Wall Street Journal foremost among them. Also, Charles Ameringer's biography of Jose Figueres, Don Pepe: A Political Biography of Jose Figueres of Costa Rica,[21] provides a great deal of information on the period under investigation, as did the previously cited work by Hutchison.

In short, this study is an attempt to relate two phenomena about which little is known, or at best, little has been published. Consequently, a great variety of sources, some unconventional, have been employed. It is hoped that the diversity of the source material has enhanced the quality

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[20]For example, Harold H. Bonilla's, Figueres and Costa Rica: An Unauthorized Biography (San Jose: Imprensa Nacional, 1973), contains a great deal of material on both Jose Figueres and Costa Rican politics, but its uneven quality and overwhelming bias render it useless.

[21]Don Pepe: A Political Biography of Jose Figueres of Costa Rica (Albequerque: University of New Mexico Press, 1978).

of the project; it is also hoped that future research in this area will result in an expansion of the existing literature.

The remainder of this paper is divided into four chapters, which correspond to the objectives above (supra, pp. 4-5). Hence, Chapter II is an examination of transnational business, with particular emphasis on International Controls Corporation. Chapter III is devoted to a review of the configuration of domestic political, legal, and economic resources from which Costa Rica draws when dealing with transnational businesses. Chapter IV consists of the case-study. Finally, Chapter V is an attempt to suggest some implications of the study and to offer suggestions for future research.

Conder

CHAPTER II

THE OFFSHORE SECURITIES INDUSTRY EXAMINED

A. Transnational Business: An Overview

1. Defining Transnational Business

As suggested in the previous chapter, scholarly interest in the field of transnational relations has largely been limited to the subject of transnational business. However, despite the attention devoted to this subject, no single definition of transnational business has been agreed upon.

> Pages of argumentation can be devoted to the problem of defining a multinational company. For working purposes, a satisfactory definition considers a firm "multinational" when it maintains major production facilities in two or more countries outside its country of principle incorporation, and which derives a significant proportion of its income from international operations. It probably does not make much difference whether such business entities are termed "international," "transnational," or "multinational."[1]

This definition, offered by the Center for Multinational Studies, points out that in addition to the problem of definition, there is also some confusion about terminology. While the Center asserts that the three most commonly-used terms for transnational business can be used interchangeably,

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[1] U.S., Congress, Senate, Committee on Finance, The Benefits and Problems of Multinational Corporations, submission of the Center for Multinational Studies (Washington, D.C.: Government Printing Office, 1973), p. 87.

there are those who believe that the term transnational is most precise.

> The UN tends to favor the term transnational rather than multinational on the grounds that the former is more descriptive of the concept of a parent firm based in one country with operating affiliates in a number of countries. Actually, the preference for transnational is not merely technical; it also rests on the belief that the term more accurately reflects the quality of "domination" inherent in the parent-subsidiary relationship in contrast with the implication of coequality in multinational.[2]

In addition, by using the term transnational, one can more readily identify such firms as one category of transnational actors about which Keohane and Nye theorize.

2. Categorizing Transnational Business Enterprises

One method of categorizing transnational business enterprises is by classifying them according to principal country of incorporation. Such a scheme reveals that most transnational businesses are headquartered in the United States. Indeed, despite the recent growth of European investment, the U.S. remains the principal foreign investor in most countries. This is due, in large measure, to the cumulative effect of U.S. investment following World War II. However, if current trends persist, foreign investment by the Japanese and Western Europeans will continue to increase rapidly.

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[2]Isiah Frank, Foreign Enterprise in Developing Countries (Baltimore: Johns Hopkins University Press, 1980), p. 8.

Another method of categorizing transnational businesses is classification according to function. Indeed, for the purposes of this paper, the functional scheme is most useful. According to such a scheme, firms can be placed into three broad categories: those engaged in extractive operations such as mining and farming, those engaged in manufacturing and assembling, and those engaged in the provision of services. Similarly, still narrower categories result when firms are classified according to commodity extracted, good produced, or service rendered. For example, a major subdivision of the services sector is the financial services industry, which includes those banks, insurance companies, brokerage houses and securities dealerships which maintain operating affiliates in several countries. As it was by the acquisition of a transnational financial services corporation, the Investors Overseas Service, that Robert Vesco entered the world of transnational business, it is necessary to examine the history of that particular firm and the milieu in which it operated.

3. The Offshore Phenomenon

While many financial institutions are truly transnational in the sense that they are incorporated in one country while maintaining operating affiliates in many others, there are also those firms which are more properly classified as "offshore," meaning that the location of their headquarters

has been moved in order to avoid regulation by a national government. By reincorporating in a state where laws governing their behavior are minimal or nonexistant, offshore firms maximize profits through business practices which would be considered questionable, if not illegal, in other states.

Raw, Page, and Hodgson summarize the distinction between transnational firms and offshore firms and conclude that:

> Offshoreness is not quite the same thing as corporate internationalism. Companies like General Motors, Shell or Phillips conduct relations with national governments. They may well take advantage, when they can, of oddities in the international legal system. But when they do, it is an incidental activity.[3]

On the other hand, "The essence of offshoreness lies in turning an enormous number of loopholes into a viable, but unregulated, corporate structure."[4]

Perhaps the most successful offshore financial operation ever launched was the Investors Overseas Service, a mutual funds organization created by Bernard Cornfeld in the early 1960's. Within ten years, Cornfeld had used the advantages of "offshoreness" to great advantage, and the IOS was immensely profitable with annual earnings in excess of one hundred million dollars. By the early 1970's, however, Cornfeld's IOS encountered legal and financial difficulties,

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[3]Raw, Page, and Hodgson, p. 62.

[4]Ibid., p. 63.

and additional operating capital was sought by the board of directors. This capital was eventually provided by Robert Vesco, an American businessman whose International Controls Corporation was itself ridden with debt. In a series of deft manuevers, Vesco gained control of the vast IOS resources and reinvested them in Panama, the Bahamas, and Costa Rica in direct violation of the IOS charter. Before these funds could be recovered, however, Vesco had used them in attempts to gain influence throughout Central America and the Caribbean, where he hoped to eventually establish an international "free-trade zone," a legitimized haven for offshore business.

The corporate vehicle by which Vesco hoped to accomplish this goal was his own International Controls Corporation; however, the ICC in its ultimate form was actually a combination of IOS capital and ICC structure. Hence, in order to understand the operating style of International Controls, one must first examine that of the Investor's Overseas Service.

B. The IOS in the Cornfeld Era

In his description of offshore mutual fund operations, Harry Schultz observes:

> The peculiarity of offshore funds is that, although they depend upon non-American investment situations, for the most part the fund managers have been

> Americans who have attempted to bring the philosophy and expertise of the immense mutual fund industry to other countries.[5]

One such individual was naturalized American Bernard Cornfeld. Born in Istanbul in 1927, Cornfeld was to become one of the most visible figures in the world of offshore finance.

Cornfeld began his career in finance as a salesman for the Investors Planning Corporation, a U.S. mutual fund dealership. After several years with Investors Planning, Cornfeld realized that a vast untapped market for mutual funds was to be found outside the United States, and in 1955 he moved to Paris where he became the exclusive representative of the Dreyfus Investment Programs. As a result of his financial acumen and his ability to inspire salesmen, Cornfeld's organization, Investors Overseas Service, was an immediate success. In addition, his flambouyant personal style attracted the attention of the popular press, which portrayed him as a benevolent socialist-turned-capitalist who believed that everyone who invested in his organization could be wealthy. In a 1962 interview with Time magazine, Cornfeld claimed that his was, ". . . a preventative agency. We find our people before they're destitute and do something about it."[6]

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[5]Harry D. Schultz, Financial Tactics and Terms for the Sophisticated International Investor (New York: Harper and Row, 1974), p. 127.

[6]"The Profitable Peace Corps," Time 17 August 1962, p. 74.

Though Cornfeld had developed a successful vehicle for selling mutual funds, he obviously had greater objectives in mind. Believing that he could not be completely successful selling only the funds of other companies, he was determined to start his own. Hence, IOS, Ltd., came into existence. Chartered in Panama, IOS, Ltd., became the cornerstone of Cornfeld's offshore ediface. Shares of IOS, Ltd., were offered to Cornfeld's associates as early as 1960. Raw, Page, and Hodgson contend that this first offshoot of IOS was fundamentally unsound.

> This early prospectus was remarkable sketchy. For one thing, it did not offer any explanation of how the money raised was to be used. For another, nowhere did it tell these first subscribers where the company in which they were buying shares had its legal home.[7]

The first fund to emerge from IOS, Ltd., was the International Investment Trust (IIT). By the time shares of IIT were ready for sale, most respectable European financiers had been made aware of the questionable nature of IOS, Ltd. As a result, Cornfeld experienced difficulty in finding a bank to act as custodian of securities and depository of cash. The reluctance of the banks stemmed from a professional distrust of companies such as Cornfeld's.

> Basically the problems flow from the very nature of the assets of investment companies. The assets of such companies invariably consist of cash and

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[7]Raw, Page, and Hodgson, p. 62.

> securities, assets which are completely mobile, and readily negotiable. Because of these characteristics, control of such funds offers manifold opportunities for the unscrupulous management of some companies. These assets can and have been easily misappropriated by such types of managements, and have been employed to foster their personal interests than the interests of the public security holders.[8]

Faced with such intransigence on the part of the financial community, Cornfeld's only alternative was to locate the management division of the IIT in Luxembourg, an offshore haven where laws governing the sale and management of securities are virtually nonexistant. In this liberal environment, International Investment Trust prospered.

On the strength of IIT, three more funds were eventually established. The Funds of Funds and the Transglobal Growth Fund were incorporated in Canada and the Venture Fund was chartered in the Netherlands Antilles. Of these, the Fund of Funds was the most ambitious. As a securities holding company, it was, in a sense, Cornfeld's fait accompli:

> The notion of one investment or holding company filling its portfolio with shares of another is hardly new. In the 1920's for instance, huge investment trusts existed through which holding companies held shares in other holding companies. And of course, IOS founder Bernard Cornfeld took the idea, refined it, and made it the corner of the mutual fund complex.[9]

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[8]Senate Report 1775, 76th Cong., 3d sess., 1940, quoted in Raw, Page, and Hodgson, p. 68.

[9]"The SEC Puts a Bite on Fund of Funds," Business Week, 27 February 1971, p. 70.

Thus, by merely channelling monies from one IOS fund to another and charging a management fee for doing so, Cornfeld and his associates made IOS an immensely profitable venture. By way of comparison, it can be noted that, "During the summer of 1969 . . . the volume of cash collected by IOS in one month exceeded the volume collected by the entire domestic mutual fund business."[10]

Improbable though it may seem, shortly thereafter, in 1971, IOS developed what was thought to be a cash-flow problem. Though this problem was largely illusory, the board of directors, led by Sir Eric Wyndham White, sought financial assistance from a number of sources. This relief came eventually from Robert Vesco's International Controls Corporation in a transaction which introduced Vesco to the world of offshore finance. This transaction, and its aftermath, are traced below.

C. The Vesco Era: IOS Is Assumed by International Controls Corporation

In his analysis of the status of IOS at the time of its assumption by International Controls, Robert Hutchison concludes that the "crisis" feared by the board of directors was indeed illusory. He notes, "Actually liquid assets were available, but the IOS board was dominated by sales executives

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[10]Raw, Page, and Hodgson, p. 254.

with little financial sophistication who seriously feared they could not meet the next payroll."[11] Consequently, they sought interim financing from a number of sources and were ultimately rejected. Eventually, only International Controls Corporation would be willing to provide the five million dollars necessary to "rescue" IOS.

Robert Vesco had neither a college degree nor any significant financial resources when he assumed control of International Controls Corporation in the mid-1960's. He did, however, have a considerable degree of financial acumen, and most importantly, was willing to take risks. Says Hutchison:

> Vesco is a man of humble origin who understood the cupidity—and innocence—of people who want to get rich quickly. A self-taught engineer, he started his career as a free-lance promoter at twenty-four. Seven lean years later, in 1966, he pieced together his first deal of any consequence by merging two little companies into the Florida-registered shell of Cryogenics Inc., whose public ownership made it a suitable vehicle for Vesco's operations. This corporate hodgepodge he renamed International Controls Corp.[12]

By 1967, Vesco had turned International Controls into a profitable venture. According to Forbes:

> . . . Vesco picked up International Controls . . . when it was grossing $300,000 a year and netting

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[11]Robert A. Hutchison, "The Looting of IOS," Fortune, March 1973, p. 128.

[12]Ibid.

> nothing. After two years, IC boasted . . . sales of $6.8 million and nearly $700,000 in profits, but less than $500,000 in cash.[13]

Vesco continued to expand his conglomerate, adding Intercontinental Industries, Electronic Specialty and Golden West Airlines by 1969. However, Vesco's strategy of acquiring debt-ridden companies for their paper value left International Controls with soaring interest costs on the debts which it assumed. Consequently, when he learned of IOS' predicament, Vesco saw an opportunity to use the vast resources of the four funds to service his own company's debts and to strike out into the vastly profitable offshore world.

The manner in which Vesco gained control of IOS is a unique example of financial legerdemain. With only three million dollars in the ICC account at the Bank of America, Vesco was two million dollars short of the minimum amount required by the IOS board. Furthermore, none of those funds were available for withdrawal. In desperation, Vesco contacted Allan Butler, whose Bahamian bank had total assets of only slightly more than five million dollars. Vesco promised that Butlers Bank would be the recipient of much-needed business if it would cooperate in the plan to "rescue" IOS. Butlers then cabled IOS headquarters in Geneva, confirming that International Controls had the required

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[13]"Company on the Make," Forbes, 15 June 1973, p. 29.

funds on account, ready for loan to IOS. On the basis of this information, an agreement was drafted which gave Vesco, as chairman of International Controls, real control over the vast IOS offshore empire.

That the IOS board was deceived is beyond question. Hutchison explains that:

> Vesco had International Controls lend IOS $5 million—which International Controls itself had to borrow. Then . . . he arranged for IOS to collateralize the loan by maintaining cash deposits in segregated accounts at Butlers Bank. In effect, IOS had "rescued" itself with its own money. This demonstrated that Vesco already knew something about IOS that its own directors apparently did not know: the company may have needed a lot of things, but money was not first among them.[14]

This accomplished, all that stood between Vesco and total hegemony over IOS was Bernard Cornfeld's personal holdings in the company. To wrest control of Cornfeld's six million shares of IOS stock, Vesco employed two offshore shell corporations. Through intermediaries, Vesco arranged for Linkink Progressive Corp., a Panamanian-registered shell, to buy Cornfeld's shares at ninety-two cents each. Linkink was then sold (its only assets were the IOS shares) by its owner, Red Pearl Bay, S.A., another Panamanian company, to a nonresident Canadian corporation, which in turn sold the IOS shares to International Controls for the meager sum of fifty thousand dollars. In short, Vesco was able to gain

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[14]Hutchison, "The Looting of IOS," p. 130.

control of all IOS assets for a minute fraction of their total value.

The details of Vesco's seizure of the IOS assets are significant because they illustrate the liquidity of offshore holdings. However, even more important from the perspective of this paper is the distribution of the funds after they came under ICC control. As might be expected, a great deal of money was diverted to International Controls subsidiaries to service their mounting debt.

> For example, in August, 1972, $60 million from the Fund of Funds, once the pride of IOS, was invested in something called Inter-American Capital, S.A., of Costa Rica. Inter-American used all the money to buy controlling interest of Phoenix Financial Corp., S.A., in Panama. Phoenix, in turn, deposited the $60 million in Bahamas Commonwealth Bank, a Nassau-based bank controlled by Vesco, in the name of a nominee, Trident Bank.[15]

Even more significant is the fact that innumerable IOS dollars were invested in Panama, Costa Rica, and the Bahamas, where it was alleged that they conveyed vast political power upon those responsible for their dispersion. Business Week estimates that,

> Vesco has pumped upward of $50 million into the Bahamas, much of it in 100 percent loans. This figure becomes even more impressive when compared with the Bahamas budget, which for 1974 is only $122.5 million.[16]

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[15]"What Robert Vesco Is Doing in the Bahamas," Business Week, 30 March 1974, p. 79.

[16]Ibid.

The magnitude of Vesco's investment in the Bahamian political economy gave rise to allegations of his informal participation in the government of former prime minister Lynden O. Pyndling. Similar allegations have been made in Costa Rica, shere Vesco's corporate and personal investments were said to have exceeded one hundred million dollars. According to the Economist:

> The most controversial (investment) involved a $2 million unsecured loan to a company founded and still owned by President Figueres. Mr. Vesco also has admitted buying $5 million worth of Costa Rican government bonds and is believed to have acquired interests in coffee plantations, an oil distribution company, a San Jose hotel, and a local newspaper. And now, of course, gossip attributes every other major business transaction in Costa Rica to him.[17]

As the Economist implies, some of the allegations about Vesco may be unfounded. However, it is in the interest of the political scientist to determine the nature and extent of this influence and to examine the political resources of those states in which offshore securities firms invest.

D. Summary

In attempting to locate the IOS/ICC conglomerate among the universe of transnational business enterprises, one encounters some difficulty. Though each firm remained nominally viable in its own field after the merger, the

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[17]"Costa Roberto," The Economist, 21 April 1973, p. 80.

management style of the hybrid corporation was unique. As it was Vesco's ultimate goal to establish a permanent offshore haven for flight capital, he began immediately to use the resources of both IOS and International Controls to achieve that goal. By "laundering" IOS funds through shell corporations and International Controls affiliates, Vesco was able to offer hugh amounts of capital to enterpreneurs throughout Central America and the Caribbean, where he hoped to establish his offshore financial fiefdom.

Without a doubt, many of Cornfeld's and Vesco's activities were blantantly criminal; as such they are atypical of transnational business executives. Indeed, while no attempt is made here to assert that the criminal activities of the offshore financial world are the responsibility of the transnational business community, it must be borne in mind that the advantages of offshore status are exploited regularly by transnational businesses for tax and investment purposes. On those occasions when unscrupulous promoters like Vesco cause political dislocation as a result of their abuse of offshore investment situations, criticism of transnational business in general is inevitable.

From the perspective of the host country, the decision to accept or reject offshore financing is difficult. Officials in developing countries are frequently aware of the origin and movement of offshore funds, but faced with

failing domestic economies, admit offshore enterpreneurs hoping that the infusion of capital will overshadow any adverse political consequences.

In attempting to assess the vulnerability of a particular state to offshore enterpreneurs, a range of political and economic resources must be taken into consideration. In the following chapter, the Costa Rican political economy is examined in an effort to determine the factors which contributed to that state's initial vulnerability to Vesco's operations and those which eventually contributed to the expulsion of International Controls from Costa Rica.

CHAPTER III

A SOCIOECONOMIC AND POLITICAL ANALYSIS OF COSTA RICA

Among those who study the relationships between transnational business enterprises and host countries, there are two conflicting schools of thought: those who contend that the cost of hosting a transnational business enterprise outweighs the benefits and those who make the opposite assertion, that the benefits to the host exceed the costs. Despite the fundamental differences between the two schools, both agree that a number of variables are involved in the cost-benefit equation. Among the most significant variables are those involving the business enterprise itself. For instance, Leonard contends that the type of industry involved, the firm's previous behavior in the host country, and the firm's behavior in other host countries are factors which must be taken into consideration when attempting to analyze the cost-benefit mix.[1]

While it is important to view this relationship from the perspective of the transnational business enterprise, it is

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[1]H. Jeffrey Leonard, "Multinational Corporations and Politics in Developing Countries," World Politics, April 1980, p. 458.

important to realize that various factors within the host country affect the cost-benefit ratio. According to Leonard:

> The level of economic development within a country is likely to affect the impact of MNC's on the polity, as are its existing patterns of domestic political alliances and cleavages. The indigenous resources offered by a country and the capital resources offered by foreign companies as well as international economic conditions, will also determine just how profoundly multinationals may alter or influence domestic political factors.[2]

A. The Domestic Resource Configuration

Having examined the IOS/ICC complex in the previous chapter, it is now necessary to examine the cost-benefit question from the Costa Rican perspective, analyzing certain socioeconomic and political variables in an effort to determine the extent to which domestic factors affect the transnational business enterprise-host country relationship.

In all, six variables will be analyzed. These are: (1) Overall Development, (2) Economic Development, (3) Constitutional-Legal Development, (4) Structure of Government, (5) Political Parties, Electoral Trends, and Voting Behavior, and (6) Leadership.

1. Overall Development: Selected Indicators[3]

Considering the reputation which Costa Rica enjoys among

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[2]Ibid., p. 458.

[3]Comparability was the primary criterion used in selecting these indicators. For example, while number of

those concerned with the process of national development, it is not surprising that several indicators chosen from the statistical evidence presented in the Statistical Yearbook for Latin America[4] show Costa Rica to be the most developed state in Central America. For example, Costa Rica leads all Central American states in life expectancy (68.2 years) and has the lowest illiteracy rate in the region (11.6% of population over age 15).

In the area of communications, Costa Rica also ranks high with 56 telephones per 1,000 inhabitants. (Only Panama, with 85 telephones per 1,000 inhabitants has more.) Perhaps more importantly, Costa Rica leads in the consumption of newsprint (5.0 kilos per inhabitant per year) with Panama a distant second (3.3 kilos).

Costa Rican social services are clearly superior to those of its neighbors. The total length of Costa Rica's road network (8,159 kilometers) is over three times greater than that of Guatemala (2,765 kilometers) which ranks second in this area. In public expenditure on education, the

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book titles published might be a good indicator of development, figures were available only for three states in the region. Hence, this indicator was rejected because meaningful comparisons could not be made. Also, these indicators are thought to be representative of most areas of national development.

[4]United Nations, Economic Commission for Latin America, 1978.

figures are somewhat deceiving showing Panama first with 5.9% of GNP at current prices and Costa Rica with 5.7%. However, the figure for Panama includes expenditures by provincial and local governments as well as the central government, while the Costa Rican figure is for the central government only.

In the area of health care services, Costa Rica's ability to provide for its citizens is notable. For example, Costa Rica has the greatest number of hospital beds in Central America (7,539), the most auxiliary medical staff (5,412) and an impressive ratio of inhabitants to doctors (1,550:1). In addition, Costa Rica has the lowest child mortality rate (1.5 per 1,000) in the region. This last statistic is a particularly significant indicator of medical sophistication and it shows the extent to which Costa Rica has gone to eliminate one of the major health problems of the Third World. In short, Costa Rican social services are second to none in the region.

2. Economic Development

Assuming that the difference between the total value of exports ($375.6 million at 1970 prices) and total value of imports ($498.6 million at 1970 prices) is roughly equal to the balance of payments, Costa Rica is seen to have a trade deficit in excess of one hundred million dollars. Indeed, despite a 7% increase in the growth on manufacturing, a 6.1%

increase in employment, and a 20.4% increase in the rate of gross national saving, Costa Rica is still faced with serious economic problems.[5]

In large measure, the problem can be attributed to Costa Rica's total dependence on foreign energy sources and the continued fluctuation of the world market prices of coffee and bananas. In the early 1970's, it was hoped that Costa Rica's membership in the Central American Common Market would aid in price stabilization. Unfortunately, these hopes were dashed when the CACM failed to achieve its stated goals. At present, Costa Rica's economic future is tied to the world price of coffee. To that end, it has joined Mexico, Brazil, and several other Latin American states in the formation of Pan Cafe, an international coffee cartel. There is, however, an increasing awareness among economists that a one-crop economy is not consistent with the goal of economic development:

> Coffee for the foreseeable future will remain an important crop, but Costa Rica wisely desires to lessen dependency upon coffee by moving marginal land into other crops and by seeking to encourage new, "non-traditional" exports. In contrast to coffee, the beef cattle industry clearly qualifies as a major growth industry, with an assured market for the foreseeable future in the United States, and recently, good prospects for Europe and Japan.[6]

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[5]All statistics have been culled from the Statistical Yearbook for Latin America, ibid.

[6]"Two Major Trouble Areas Face Otherwise Buoyant Costa Rica," Commerce Today, 4 February 1974, p. 41.

Regarding the role of the United States in the process of economic development in Costa Rica, it is presumed that trading between the two states will continue to be considerable in volume. For example:

> In 1972 the U.S. supplied 33 percent of the Costa Rican market ($123 million, c.i.f.) and purchased 40 percent of its exports ($113 million, f.o.b.). The outlook is for trade to stay high and roughly in balance.[7]

Perhaps even more important than the volume of trade in commodities is the role of U.S. investment in Costa Rica. While Costa Rica has always encouraged American investment, there is a growing fear that the country is becoming a convenient depository for flight capital. Some observers believe that, "This growing American presence and particularly the activities of a few unscrupulous and insensitive promoters have given Costa Ricans pause and might lead to an attempt to regulate future investment."[8]

Ideally, Costa Rica would like to attract respectable corporate investors from the United States, Western Europe and Japan, but the worsening political situation in the rest of Central America seems to thwart these efforts. Commenting on the difficulty of attracting investment to Costa Rica, Finance Minister Hernan Saenz remarks:

> We have a job trying to tell them that it is a different country, that it is a country where

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[7]Ibid., p. 42.

[8]Ibid., p. 42.

> people can go unarmed, where there is no army, where human rights are respected. It is different on all those accounts. But one has to keep telling them.[9]

Indeed, any potential investor familiar with Central American politics would readily concede that Costa Rica has achieved a level of political development uncommon to the region. An analysis of Costa Rican constitutional development, political institutions, electoral trends and political parties, and leadership is presented below.

3. Constitutional Development: Distinctive Features of the 1949 Costa Rican Constitution

In order to grasp the significance of the 1949 constitution, it is necessary to review the revolution of 1948, considered the benchmark in Costa Rican political development and the genesis of the 1949 document. In that year, the government of Rapheal Angel Calderon Guardia refused to acknowledge the election of Utilio Ulate to the office of president. This unprecedented disregard of the electoral process prompted Jose Figueres, a formerly apolitical farmer and enterpreneur, to mount armed resistance against the Calderon Government. In union with intellectuals from the Center for the Study of National Problems, Figueres formed a small army which eventually

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[9] "The Image Problem of Costa Rica," Euromoney, April 1980, p. xxv.

defeated the Calderonistas. The "revolution," which was actually only a series of skirmishes, ended in the establishment of a provisional junta led by Figueres. Before relinquishing control of the government to the rightfully-elected Ulate, the junta undertook a series of basic reforms, one of which was the establishment of a commission to draft a new constitution.

The document produced by that commission is without peer in Latin America. In his work on Costa Rican politics, Busey notes:

> What is most striking about the Costa Rican Constitution is its inclusion of numerous substantial protections against either the infringement of individual guarantees or the undue exercise of strong presidential power.[10]

In contrast, he observes that,

> the constitutions of four republics of Central America and of Mexico make ample provision for the exercise of strong executive power, and demonstrate little concern lest that power impose its will over the legislative and judicial branches or make a mockery of the constitutional guarantees.[11]

Though the Somoza regime has been displaced in the intervening years since Busey wrote, this does not alter the conclusion that the Costa Rican constitution of 1949 is the most effective political instrument in the region.

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[10]James L. Busey, Latin America: Political Institutions and Processes (New York: Random House, 1967), p. 59.

[11]Ibid., p. 63.

Specifically, Busey cites five areas in which the Costa Rican constitution differs from those of other Latin American states. In the area of civil liberties, guarantees are specifically stated and suspension of those guarantees is an infrequent occurrence. Furthermore, it is the legislature, not the executive, which has the constitutional authority to suspend guarantees; a two-thirds majority of the Legislative Assembly is required and the suspension is only in force for thirty days. Only when the Assembly is not in session can the president order a suspension, and a unique constitutional device provides that the Assembly must reconvene immediately upon an executive order for suspension of guarantees of civil liberties.

Regarding the judicial branch, Busey believes that, "In its provisions for the judiciary, the Costa Rican Constitution reveals a singular solicitude for the independence of the courts."[12] Independence is guaranteed by the appointment process; the seventeen magistrates of the Supreme Court of Justice are appointed by the Legislative Assembly. After an eight-year term, they serve for life unless removed by a two-thirds vote of the Assembly. Thus, the process of judicial appointment is totally removed from the executive branch and subjected to the scrutiny of a highly-independent legislature.

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[12]Ibid., pp. 60-61.

Another area in which the Costa Rican constitution is particularly strong is protection of suffrage. In Costa Rica, suffrage is universal for all citizens over the age of twenty; in fact, a small fine is assessed for failure to vote. Martz notes that the adoption of obligatory voting in 1959 has resulted in continually-increasing voter turnout. "Participation rose under the new regulations from 67.2 percent in 1953 and 64.7 in 1958 to 80.9 in 1962 and 81.6 in 1966."[13] The constitution provides that all elections shall be overseen by the Tribunal Supremo Electoral. One year before, and six months after each election, the Tribunal, composed of five members, monitors the registration and voting processes. Since 1958, teams of observers from the Organization of American States have observed the Costa Rican elections and have pronounced them free from electoral fraud; as such, the Tribunal seems to be a most effective device.

The fourth and fifth areas in which the Costa Rican Constitution is distinctive involve the legislature, the executive, and the relationship between them. The Constitution grants the legislature not only legislative powers, but also the authority to censure ministers, and the authority to monitor the actions of the executive, even to the point of requiring the executive to seek the permission of the

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[13]John D. Martz, "Costa Rican Electoral Trends, 1953-1966," Western Political Quarterly, November, 1967, p. 895.

legislature before leaving the country. Also, the legislature has the right to determine the president's capability for continuing in office and may choose one of the two vice-presidents as his successor.

The executive, on the other hand, enjoys many traditional executive powers, but these are highly circumscribed. He can, however, appoint ministers and directors of the autonomous institutions of government, a most important source of executive power. A further limitation on executive power is the requirement that all expenditures be approved by the Comptroller General of the Republic, who is appointed by the legislature for an eight-year term. Finally, "the Costa Rican document limits the terms of the president, but with the ingenious proviso that he may be reelected to the office after the passage of an eight-year period subsequent to his term of office."[14] This insures that the phenomenon of continuismo, common in Latin America, cannot occur in Costa Rica.

In short, though the Costa Rican executive is by no means a figurehead, one cannot avoid the conclusion that in Costa Rica, the legislature is the dominant branch of government.

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[14]Busey, p. 63.

4. Structure of Government

For administrative purposes, Costa Rica is divided into seven provinces, 68 cantons, and 344 districts. Though there is government activity at all levels, the greatest amount of activity occurs at the national level.

As alluded to in the previous section, the constitution provides for three independent branches of government: the executive, the legislature, and the judiciary. The executive is composed of the president, two vice-presidents, the cabinet, and the Council of Government. The president serves a four-year term. He has the authority to appoint ministers and members of the Council of Government, which assists him in making policy recommendations to the executive.

The legislature, the Asamblea Legislativa, is unicameral and is composed of 57 deputies, all of which serve four year terms. Proportional representation applies in legislative elections. The functions and membership of the judiciary, the Supreme Court of Justice, have been described previously.

One special feature which distinguishes the Costa Rican government from others in the region is the heavy reliance upon autonomous institutions, or public corporations. Indeed, many governmental functions normally reserved for cabinet-level attention in other states are assigned to public corporations in Costa Rica.

> In 1969 there were over 200 of these agencies, which included such enterprises as the Electric

> Institute, the Pacific Electric Railroad, the Social Security Fund, and the University of Costa Rica. Also in this category were the country's schools, prisons, hospitals and co-operatives.[15]

Article 188 of the constitution gives the president the authority to appoint the directors of these institutions, a power which, when used wisely, can go a long way toward redressing the imbalance of power in favor of the legislature.

5. Political Parties, Electoral Trends, and Voting Behavior

Previously, it was suggested that the revolution of 1948 had a profound effect upon constitutional development in Costa Rica. In much the same way, the revolution also altered the structure of Costa Rican political parties. During the 1940's a tenuous balance was maintained among Calderon's Partido Republicano, the Communist Party led by Manuel Mora, and a loose coalition of conservatives. Though the Partido Republicano claimed both the presidency and a majority in the Asamblea Legislative during this period, a coherent idiological stance is difficult to discern. At times the PR appeared to favor the conservatives, while at others, it seemed to curry the favor of Mora and the Communists. Hence, it is only after the revolution and the

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[15]Howard F. Blutstein et al., Area Handbook for Costa Rica (Washington, D.C.: U.S. Government Printing Office, 1970), p. 120.

defeat of the Calderonistas that one begins to discern true party development.

After defeating the Calderonistas and installing Ulate in the presidency, Figueres and his colleagues at the Center for the Study of National Problems concentrated on the development of a coherent philosophy upon which to base the Partido Liberacion Nacional (PLN). The result was an,

> ideological party capable of conducting Costa Rica along the path of modern social and economic development while at the same time conserving and expanding the country's political democracy.[16]

The success of Figueres and his partisans in convincing the Costa Rican electorate of the superiority of the PLN program is evidenced by the sweeping PLN victory in 1953. Undoubtedly, one factor in the successful development of the PLN has been the breadth of its foundation. In his analysis of the PLN, Charles Anderson notes:

> The Liberacionistas, in justifying their program, appeal to the authority and inspiration of such disparate theories as continental social democratic thought; the leftist Latin American ideologies, including Aprismo and the Mexican revolution; Catholic social action ideals; and the intellectual left of the Democratic Party in the United States. While the Liberacionistas "emphatically reject" communism, they have "no objection" to using Marxist arguments and modes of analysis.[17]

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[16]Robert J. Alexander, quoted in James D. Martz, p. 890.

[17]Charles W. Anderson, "Politics and Development Policy in Central America," Midwest Journal of Political Science, November 1961, pp. 334-335.

Furthermore, one has only to glance at the structure of Costa Rican government and the shape of Costa Rican economic policy to determine the effect which Liberacionista thought has had upon each.

> In practice, Liberacion Nacional's program has been dominated by large scale economic and social planning, a moderately nationalistic attitude toward foreign investment, and state intervention in the economy, particularly through autonomous institutions (public corporations) in fields that range from electric power and tourism to banking.[18]

In short, contemporary Costa Rican political and economic thought have been shaped to a great extent by the PLN experience.

Unlike their Mexican counterparts, the Liberacionistas made no attempt to proscribe rival parties after their victory. Indeed, Costa Rica can be said to have a viable two-party system, consisting of the PLN and the ever-changing anti-PLN coalition. The 1966 election provides a good example of both the eclecticism and tenacity of the anti-PLN coalition. In that year, the Partido Republicano, the Partido Union Nacional, and the Partido Union Republicana Autentica, all minor parties, formed a coalition which resulted in the defeat of the PLN candidate, Daniel Oduber. Says Martz, "Recognizing the virtual impossibility of

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[18]Charles W. Anderson, "Central American Political Parties: A Functional Approach," Western Political Quarterly, March 1962, p. 128.

defeating the PLN if their forces were divided, the opposition chose to bury personal and party differences for the duration of the campaign . . ."[19]

In looking at Costa Rican electoral trends, one sees further evidence of the tenacity of the anti-PLN coalition. The first time that the PLN succeeded itself in the office of the presidency was in 1974. The fact that the PLN has not been able to dominate the electoral process is both a tribute to the dedication of the opposition and proof of the inviolability of the electoral process.

Concluding his study of electoral trends, Martz predicts:

> These factors all suggest a favorable outlook for the PLN in 1970, but the events of the next three years will obviously be crucial. Those trends which have emerged during the recent decade and a half suggest a growing polarization of public sentiment into pro-PLN and anti-PLN forces, and the contest in 1970 will likely center once again on this basic issue. For Costa Rica, a shiningly atypical political culture in the Latin American millieu, the workings of the party system and a politically literate electorate suggest a continuity and stability within which national development will continue to progress and flourish.[20]

From his 1967 vantage point, Martz was correct in two fundamental respects: first, he foresaw the 1970 PLN victory (and to an extent, the 1974 victory) and he highlighted the polarization phenomenon, which appeared to reach its zenith in 1974 during the Vesco affair.

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[19]Martz, p. 892.

[20]Ibid., pp. 908-909.

TABLE III-1

CHIEF EXECUTIVES OF COSTA RICA

Chief Executive	Term	Party	Control of A.L.[a]
Raphael Calderon	1940-1948	PR	PR
Jose Figueres	1948-1949[b]	PLN	PLN
Otilio Ulate	1949-1953	PUN	PLN
Jose Figueres	1953-1958	PLN	PLN
Mario Echandi	1958-1962	PUN	PLN
Francisco Orlich	1962-1966	PLN	PLN
Joaquin Trejos	1966-1970	UN	PLN
Jose Figueres	1970-1974	PLN	PLN
Daniel Oduber	1974-1978	PLN	anti-PLN coalition
Rodrigo Carazo	1978-	PUN	PLN

[a] Asamblea Legislativa

[b] Leader of Junta Fundadora de la Segunda Republica

Key: PR = Partido Republicano
PLN = Partido Liberacion Nacional
PUN = Partido Union Nacional
UN = Partido Unificacion Nacional

Referring again to Table III-1, two additional phenomena are noteworthy. First, the continued domination of the legislature by the PLN seems to be a further indication of that party's maturity, but little research is available to support this conclusion. Second, one is struck by the magnitude of the role played by Jose Figueres in Costa Rican politics. This phenomenon will be examined in the concluding section of this chapter.

Not surprisingly, voting behavior is the one facet of Costa Rican political activity which has persistently attracted the attention of American political scientists. Encouraged by the relative homogeneity of the population and aided by Costa Rican government agencies, scholars found Costa Rica conducive to empirical studies of political participation in general, and voting behavior specifically. Though many studies of this stype have been attempted, the most recent, and perhaps the best is Booth and Seligson's study of political activity among rural peasants. Dispelling the myth of the politically apathetic Latin American peasant, they conclude that:

> Costa Rican peasant political participation is multidimensional, consisting of six distinct modes —communal organizational activism, communal project activism, citizen-initiated contacts with local government, voting, campaign activism, and strike activism.[21]

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[21]John A. Booth and Mitchell A. Seligson, "Peasants As Activists: A Reevaluation of Political Participation in the Countryside," Comparative Political Studies, April, 1979, p. 48.

In addition, their analysis of voting behavior among peasants revealed that although peasants tend to vote less frequently than city-dwellers, environmental factors, not apathy, were the cause.

> Peasants must usually travel long distances on rural buses (which charge a high per-mile rate because of the poor conditions of rural roads) to vote, while residents of the metropolis seldom have to travel more than a few blocks . . . . Thus, the high costs incurred by the peasant stand between him and the exercise of the franchise.[22]

6. Leadership

Though various theories have been advanced which purport to explain the remarkable state of Costa Rican political development, no theory which discounts the role of leadership can be given much creedence. While the country's size, relative homogeneity of population, and colonial experience have undoubtedly been factors contributing to political development, the leadership of Jose Figueres is a catalytic element which cannot be overlooked. As organizer of the 1948 revolution, leader of the founding junta, chairman of the PLN, and two-term president of the republic, Figueres is a figure of unparalleled importance in Costa Rican politics. As such, any analysis which excludes Figueres is necessarily incomplete.

James McGregor Burns, in his encyclopedic work on leadership, offers some insight on this most elusive

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[22]Ibid., p. 43.

political phenomenon. Three aspects of this phenomenon which he treats in some detail are heroic leadership, party leadership, and ideological leadership. The first he describes as a relationship in which followers expressed:

> belief in leaders because of their personage alone, aside from their tested capacities, experiences, or stand on issues; faith in the leader's capacity to overcome obstacles and crises; readiness to grant to leaders the powers to handle crises; mass support for such leaders expressed directly; through votes, applause, letters, shaking hands—rather than through intermediaries or institutions.[23]

Without a doubt, it was this type of relationship which brought Figueres to power in 1948. As a farmer and an industrialist with no previous political experience, Figueres relied solely upon personal dynamism and the indignation of the Costa Rican people at the annulment of the election returns to propel him into a position of leadership. However, unlike the archetypal heroic leader who seeks to retain power once he achieves it, Figueres acceded to the rightfully-elected Utilio Ulate in 1949.

In the four years between the end of the revolution and the first Figueres presidency, a transformation occurred. During this period, the political maturation of Jose Figueres became evident as he emerged as leader of the National Liberacion Party. In this regard, Burns' observations on party leadership are important.

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[23]James McGregor Burns, Leadership (New York: Harper and Row, 1978), p. 244.

> Parties are the vehicles of collective leadership. Whether the party leaders are world-famous personalities or obscure local committee members, their political vocation is to recognize the wants and needs of present and potential constituents, to arouse and intensify expectations, to enlist more persons in the party cause, to win elections—and then to mobilize the party's influence within and outside government to satisfy rising demands, thereby winning more elections and remaining in office.[24]

The success of Figueres in this clearly organizational role is reflected in the electoral victories of the PLN not only at the national level, but the provincial and local levels as well. More important, however, is the fact that the party's success was not dependent upon the persona of "Don Pepe" Figueres, but rather, was the result of the efficient functioning of a party organization which Figueres had developed.

Almost from its inception Liberacion Nacional had been as much an ideology as a political party. Even by 1961, the orientation of the party was evident. Anderson notes:

> Liberacion Nacional quite self-consciously represents itself as an ideological movement, seeking to present the Costa Rican electorate with a coherent political doctrine. Next to Peru's APRA movement, the party has perhaps given more attention to the construction of a distinctive political philosophy than any other in Latin America . . .[25]

Though himself not an intellectual, but an hombre de acción, Figueres was nevertheless the leader of an ideological

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[24]Ibid., pp. 337-338.

[25]Anderson, pp. 333-334.

movement which commanded the respect of social democrats throughout Latin America. In an era marked by extremism, Figueres steered a moderate course as president, party leader and social democrat.

As Burns notes, "Most leaders combine both ideological and charismatic qualities, and great leaders combine them creatively."[26] The creative way in which Jose Figueres combined these qualities is recounted both by those who elevate him and those who criticize him. From the perspective of this paper, however, it is interesting to note that some students of Costa Rican politics, notably Ameringer,[27] date the "downfall" of Jose Figueres from the mid-1970's and link it to his involvement with Vesco. In light of the preeminence of Jose Figueres in Costa Rican politics, and his occupation of the presidency from 1970 to 1974, it is assumed that the personal relationship between Figueres and Vesco was a crucial determinant of the ICC's relationship with Costa Rica.

B. Summary

As stated at the beginning of this chapter, any attempt to assess the potential impact of a transnational actor on a state in which it operates depends to a great extent upon

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[26]Burns, p. 251.

[27]Ameringer, p. 280.

certain domestic factors within the host state. One such factor is the state of overall development, or the existence of social overhead capital such as public transportation, educational facilities, and health care. In this regard, Costa Rica is without peer in the region. However, there are indications that the government's ability to continue to provide such services is diminishing. According to the New York Times:

> Aggravating the uncertainty is the country's economic crisis, which has provoked a large devaluation of the currency and is forcing the Government to reduce public spending sharply to obtain help from the International Monetary Fund.[28]

Indeed, the economic crisis, to which the Times alludes is perhaps Costa Rica's greatest liability in dealing with transnational businesses. Increasing costs of imported energy, fluctuation in the world prices of major exports, and the instability of its currency have forced Costa Rica to depend upon foreign investment for economic viability. Hence, it is not unreasonable to assume that Costa Rica is willing, of necessity, to accept the costs associated with hosting transnational businesses in order to reap the economic benefits.

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[28]Alan Riding, "For Costa Rica, 2 Bombs Bring a Taste of Fear," New York Times, 22 March 1981, p. A17.

Assuming then that Costa Rica cannot be highly selective in determining which firms shall operate within its borders, it must use its considerable political and legal resources to ensure that the costs of hosting such firms are minimized. As described in sections A.3, A.4, and A.5 above, the Costa Rican Constitution of 1949 created three autonomous branches of government which have since maintained their independent character, successfully resisting capture by special interests.

In like manner, Costa Rican political parties have developed along ideological lines, with each party adopting a programmatic approach to social and economic issues. While the largest party, the PLN, has been able to predominate in the Legislative Assembly, it has been unable to dominate the presidency, largely due to the ability of the various smaller parties to form effective coalitions. In effect, Costa Rica can be said to have a two-party system.

Due in part to this polarization of political opinion and also due to the influence of the Tribunal Supremo Electoral, Costa Rican elections have been relatively free of fraud. As a result, there is great popular confidence in the electoral process and political participation is high. As Solomon points out, popular participation is a crucial variable in limiting the costs of hosting a transnational business enterprise.

> In a political process characterized by a lack of widespread participation, the ability of multinational firms to detach a national elite from the masses enables these entities to undermine national political autonomy and to diminish national identification.[29]

Finally, the phenomenon of leadership is the most difficult variable to evaluate. Though the PLN has shared the executive office with the opposition, one cannot discount the presence of Jose Figueres as a perennially symbolic, if not official, leader of Costa Rica since the revolution. Clearly, whether in office or in opposition, Jose Figueres is a major point of access for those who would affect Costa Rican government policy.

In sum, Costa Rica is a state with vast political and legal resources and a tradition of stable representative government. However, global economic conditions and domestic limitations require that the political system be constantly challenged by foreign investors seeking to ensure that the climate for investment remains hospitable. In the following chapter, the challenge posed by Robert Vesco's International Controls Corporation will be examined and the Costa Rican response noted.

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[29]Lewis D. Solomon, Multinational Corporations and the Emerging World Order (Port Washington, NY: Kennikat Press, 1978), p. 94.

CHAPTER IV

INTERNATIONAL CONTROLS CORPORATION IN COSTA RICA

In this chapter, the relationship between the government of Costa Rica and the International Controls Corporation is examined. The resulting case-study consists of four parts: the initial capital investments, the proposal to create an offshore financial district, the relationship between Vesco and president Figueres, and the U.S. Senate investigations. Before proceeding, however, several underlying assumptions must be made explicit.

The first such assumption is that Robert Vesco, as the architect of the merger which allowed International Controls to assume control of the IOS dollar funds, exerted practical control over all ICC and IOS operations. Though the nature and extent of his participation were obscured through an intricate web of shell corporations, he directed the entire ICC/IOS conglomerate during the 1970-1975 period.[1]

A second assumption related to the first is that it is impossible to draw a distinction between the actions of Vesco the individual, and Vesco the corporate executive. The importance of this point cannot be overemphasized; from

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[1]This assumption is based upon the conclusion reached by the SEC in its investigation. See SEC vs. Vesco.

the perspective of this paper, Vesco is to be regarded as one of a class of actors who merely represent, and to some extent, personify, the offshore securities industry. In turn, the offshore securities industry is but one type of transnational actor which needs to be identified, studied, and accommodated within the theoretical structure of the field. As of now, this remains to be done.

A. The Dispersal of the Funds

By the time Robert Vesco arrived in Costa Rica in July, 1972, the dispersal of the IOS dollar funds was well under way. Breifly, this procedure involved the sale of IOS securities to a shell corporation chartered in a recognized offshore haven such as Panama, the Cayman Islands, or the Netherlands Antilles. This shell would then be sold, in part or in its entirety, to another intermediary, usually a bank, which would then make unrestricted loans to International Controls.

As Figure IV-1 shows, there appears to be no pattern to the reinvestment process; indeed, the object, according to the SEC, was to obscure the location of the former fund dollars. Of interest from the standpoint of this paper are two substantial Costa Rican investments. As the figure indicates, a $2,150,000 unsecured loan was made to the Sociedad Agricola y Industria San Cristobal, a company owned

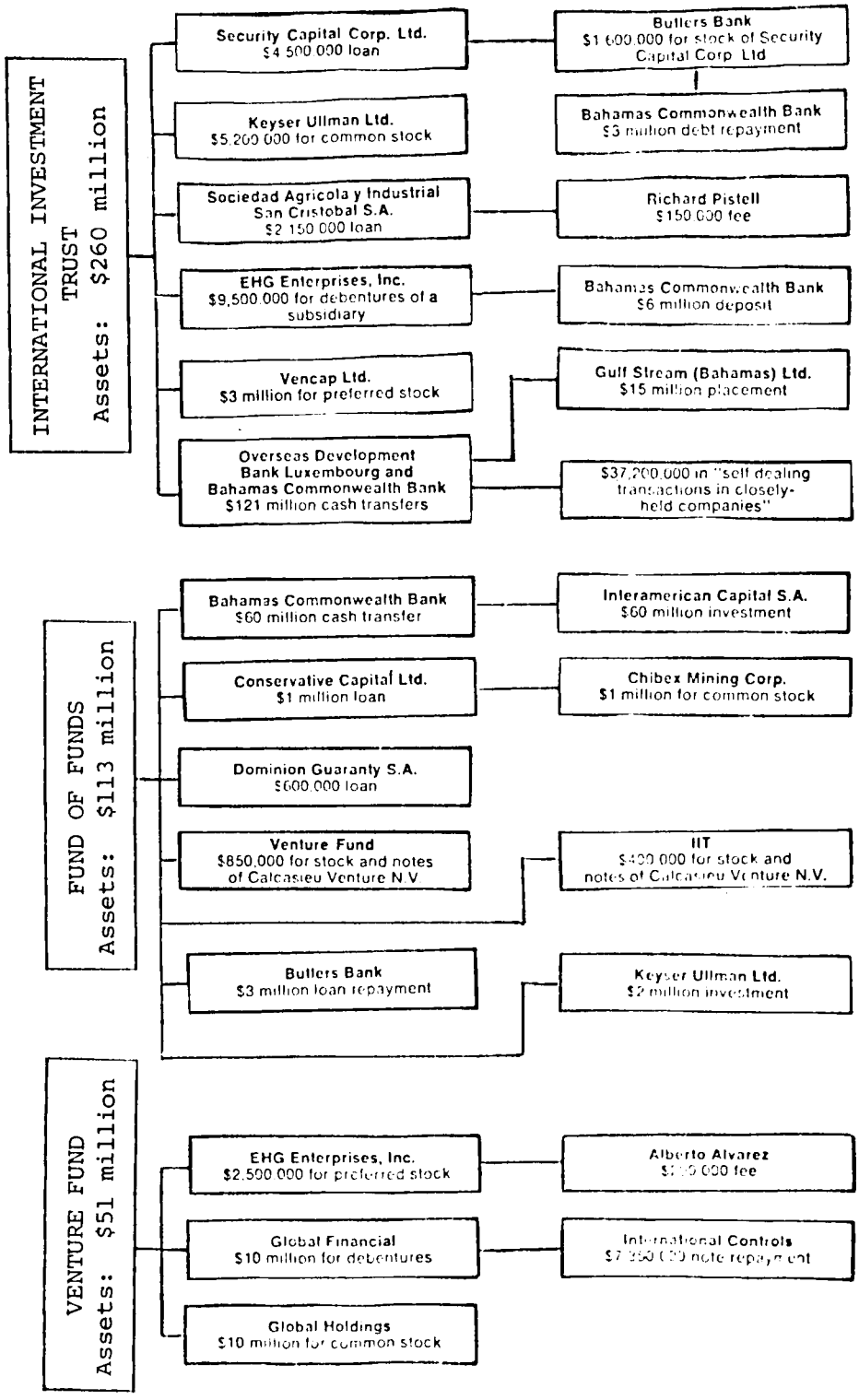


Figure IV-1. IOS Dollar Funds.

Source: SEC Complaint, as reprinted in Hutchison, "The Looting of IOS," p. 140.

by president Jose Figures and managed by his son, Jose Marti Figueres. According to Ameringer, a loan to this firm, which produced mostly hemp and polypropylene coffee bags, was a most imprudent investment.

> Despite the fact that SAISC had lost over one-half million dollars in 1971, Figueres wanted to expand operations . . . by establishing a factory to produce low-cost prefabricated houses. Inconsistent with his reputation as a shrews businessman, Vesco made an unsecured loan of $2,150,000 to SAISC on August 2, 1972, barely a month after meeting Don Pepe and only after a perfunctory examination of the business.[2]

Furthermore, the loan to Figueres' company was made in blatant disregard of IIT regulations. Hutchison points out that, "IIT's letters patent expressly prohibit the lending of assets, 'except by purchase of government, corporate, or municipal bonds.'"[3]

On November 27, 1972, the Securities and Exchange Commission filed a civil fraud complaint against Vesco and 41 other defendents. This document, the culmination of years of investigation by the SEC, charged that Vesco and his associates diverted the IOS dollar funds for their personal gain at the expense of investors. The complaint traced the dollar funds, noting Vesco investments in Costa Rica, Panama, and the Bahamas. Two days later, Stanley Penn of

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[2]Ameringer, p. 270.

[3]Hutchison, "The Looting of IOS," p. 140.

the Wall Street Journal published an article explaining the SEC action in which he intimated tht Vesco was attempting to gain the favor of President Figueres.

> The Vesco group, the SEC asserts, got IIT to make the loan to San Cristobal contrary to the Fund's restrictions, as a part of their endeavors to relocate their operations in Costa Rica and obtain a haven there for their activities.[4]

In addition, Penn also revealed that Figueres' firm had received financing in 1968 from the Capital Growth Corporation, an offshore securities operation controlled by Clovis McAlpin. In return, McAlpin was accorded special treatment by the Costa Rican government.

> Following Capital Growth's $2 million investment, Mr. McAlpin became a resident of Costa Rica, obtained a diplomatic passport from Costa Rica, and in December, 1970 was named by the Costa Rican government as its minister counselor to the Belgian embassy.[5]

Also, the SEC complaint alleged that Inocente Alvarez, an advisor to Figueres, and Fernando Fournier, a prominent San Jose attorney, were responsible for facilitating Vesco's $60 million investment in Inter-American Capital S.A., a firm which had been used to channel IOS dollars to Vesco's parent company, International Controls.

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[4]Stanley Penn, "Company That Got $2,150,000 Loan Linked to Costa Rican President Figueres," Wall Street Journal, 29 November 1972, p. 17.

[5]Ibid.

Dismayed at the adverse publicity Costa Rica had received because of Figueres' involvement with offshore financiers, his opponents, both in the legislature and in the press, undertook a campaign to discredit Figueres by exposing the full extent of his complicity in their operations. Perhaps the most revealing discovery in this regard was a proposal to create an offshore financial district on Costa Rican territory. This plan is described below.

B. The Offshore Financial District

In 1968, Clovis McAlpin, an offshore financier of some repute, moved his mutual fund operation, Capital Growth Fund, from Belgium to Costa Rica, where he perceived the investment climate to be more favorable. As reported above, he offered to invest $2 million in the Sociedad Agricola y Industria San Cristobal, an offer which Figueres immediately accepted. In addition to the perquisites noted above, McAlpin also received considerable personal attention from Figueres, who was campaigning for the presidency at that time. Ameringer notes that Figueres respected McAlpin's financial acumen and solicited his advice:

> Don Pepe . . . asked McAlpin to suggest ways in which Costa Rica might attract additional investment. As a result, McAlpin consulted "a prestigious firm of experts in New York," which drafted a report recommending creation of an international financial district.[6]

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[6]Ameringer, p. 267.

Though no action was taken at the time, it is known that Figueres received a copy of this recommendation.

When the idea of an international financial district next surfaced in Costa Rica, it was proposed by Robert Vesco in 1972. Though Vesco claimed no knowledge of the McAlpin plan, it is obvious from the substance of Vesco's proposal that Costa Rica had long been under consideration by offshore financiers as a possible base of operations. Hutchison describes this proposal:

> Vesco's international free zone, according to an unsigned memorandum circulated among Liberacion party congressmen, was to consist of a financial district and a satelite resort area with a luxury housing development, hotels, recreational facilities, and "tourist development, including gaming." The zone was to be self-governed by a five-member council titularly headed by a governor appointed by the President of Costa Rica, but in reality controlled by a district director, a role Vesco reserved for himself.
>
> The council would be empowered to enact legislation, keep a registry of corporations and a maritime registry, issue bonds, collect taxes, assure business and banking secrecy, and create its own banking commission to supervise banks and trusts domiciled in the zone. Under the proposed charter, Costa Rican nationals would be excluded from working or residing in the zone except by permission of the council.[7]

On October 4, 1972, a bill which proposed creation of an international financial district was given first reading in the Costa Rican Legislative Assembly. The bill's sponsorship

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[7]Hutchison, Vesco, p. 309.

is unclear, for while President Figueres endorsed it emphatically, a number of his partisans in the legislature joined in a public condemnation of the proposal.

> Twenty-six PLN deputies and a group of economists and former government ministers published a statement objecting to the plan. "We do not desire, nor are we able to admit, investments of foreign capital directed toward international financial speculations . . . and much less if these efforts are accompanied by an effort to convert Costa Rica into a refuge for capital under a system of extraterritoriality."[8]

As a result of this opposition, the bill was never given a second reading and the idea of an autonomous financial district never resurfaced. However, the incident served to alienate the liberal wing of the PLN and to erode further the base of Figueres' influence within the legislature. The events which followed displayed the extent of Figueres political isolation as a result of his associations with offshore financiers.

C. Figueres and Vesco versus the SEC: The Politics of Isolation

In order to stem the tide of criticism which was mounting as a result of his involvement with the financial district and the unsecured loan to his business, Figueres appeared on Costa Rican television on December 4, 1972. In a passionate speech, he denied Penn's allegations, saying

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[8]Ameringer, p. 266.

that the Wall Street Journal "twisted the truth." In an attempt to appeal to the national pride of the Costa Ricans, he said that, "the citizens of Costa Rica aren't bought with money and there aren't sufficient billions in the world to buy them nor their national dignity."[9] He also intimated that the Journal, as the organ of the New York financial community, was using him as a scapegoat because it disapproved of Vesco's policy of diverting capital from the industrialized states to the less-developed Third World.

Whatever effect Figueres' speech might have had upon Costa Rican public opinion was mitigated by the revelation that a Vesco-controlled bank in the Bahamas had purchased $5 million in Costa Rican government bonds. The December 11 issue of the Wall Street Journal contained an article which stated that Costa Rican government securities had been sold to the Bahamas Commonwealth Bank. While the sale of the bonds themselves was not a particularly interesting item, the status of the purchasing bank was suspect.

> The SEC has alleged in court papers that the Bahamas Commonwealth Bank is a "conduit" used by the Vesco group for the diversion of assets of foreign-based mutual funds managed by IOS.[10]

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[9]"Costa Rican Head Says Wall Street Journal Twisted the Truth," Wall Street Journal, 6 December 1972, p. 19.

[10]Stanley Penn, "Bahamian Bank Linked to Vesco by SEC Has Bought $5 Million in Costa Rican Bonds," Wall Street Journal, 11 December 1972, p. 6.

In addition, the San Jose law firm of Facio, Fournier, and Canas earned $50,000 in legal fees from this transaction; at the time, Gonzalo Facio, a senior partner in the firm, was the Costa Rican foreign minister.

In the meantime, the process of establishing corporate offices in Costa Rica was begun by International Controls Corporation. Both Vesco's private plane and ICC-owned aircraft transported goods from Switzerland to San Jose, where no duty was paid. "The goods were brought into the country without clearing customs, which prompted a question in parliament as to why Vesco was permitted to dispense with the usual customs formalities."[11] Though this question was never answered officially, it was obvious that Vesco was being accorded special treatment by the executive branch; this was confirmed when Vesco applied for Costa Rican citizenship.

On December 22, after residing in Costa Rica less than seven months, Vesco applied for citizenship. Shortly thereafter, on January 7, 1973, a court ruled that Vesco did not meet the five-year residence requirement. However, several days later, a Costa Rican passport was issued to Vesco by the Institute of Tourism, granting him "pensionado" status. Ameringer observes:

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[11]Hutchison, Vesco, p. 310.

> Public opinion reacted against the action, not only because it seemed alien to the intent of the law, but also because it was performed by the executive power—granting citizenship was a judicial function—and the president was already under suspicion for his dealings with Vesco.[12]

Reacting to this blatant usurpation of the judicial power, the Legislative Assembly established a committee to investigate Vesco's personal and corporate dealings in Costa Rica. Several weeks later, on March 6, Vesco made an appearance on Costa Rican television, ostensibly for the purpose of defending his economic interests in the country and justifying his involvement with Figueres. He said, in part:

> Geographic employment of capital . . . runs at cross purposes with the institutional interests in a capitalistic society.
>
> I believe that the investment direction of the seventies should be back into (developing) countries in the form of sound economic investments that also carry a high degree of sociological benefit and contribute to the well-being of its people.
>
> For the SEC, this view is almost treated as a crime; it is also treason to the financial establishment and therefore must be stigmatized as "fraud."[13]

However persuasive Vesco might have been, he failed to deter the legislative committee from pursuing their investigation. On April 7, the Miami Herald reported that the committee had received the official SEC dossier on Vesco.

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[12]Ameringer, p. 273.

[13]Quoted in Hutchison, Vesco, p. 303.

Later, when it was discovered that Vesco's television appeal had been written by Figueres, his credibility was further reduced.

The final blow to Vesco's credibility was dealt on May 10. On that day, Vesco was indicted in New York on charges of having attempted to make an illegal contribution to the Nixon reelection campaign. It appears that this charge, linking Vesco with Nixon, had the greatest impact on Costa Rican public opinion. The following day, in the midst of a great public outcry against both Vesco and Figueres, Daniel Oduber, president of the legislative assembly and a high-ranking PLN official, resigned his post in order to oppose Figueres in the 1974 presidential election. This development is most significant in that it directly links Vesco to a rift in the National Liberation Party.

Less than a month later, on June 2, the New York Times published an article revealing that Vesco had made, "major cash contributions,"[14] to Bahamian, Costa Rican, and U.S. political candidates in an attempt to win concessions. In an interview with the Times, former Bahamian minister of tourism and communications Arthur A. Folkes said that:

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[14]Wallace Turner, "Bahamians Say Vesco Made Political Gifts That Recipients Now Find Embarrassing," New York Times, 2 June 1973, p. 14.

> it was "absolute nonsense" that Mr. Vesco came to the Bahamas "because he is interested in assisting developing countries" . . .
> . . . . . .
> It seems a vulgar attempt to take advantage of what he apparently believed to be the psychology of a persecuted, self-pitying Black Government.[15]

In Costa Rica, reports of Vesco affairs in the Bahamas were read with interest. Soto Pacheco, chairman of the legislative investigating committee, traveled to the Bahamas to conduct an independent inquiry, at the conclusion of which he admitted, "We experienced shame in the Bahamas."[16]

One week later, on June 9, U.S. ambassador Viron Vaky officially requested Vesco's extradition to the U.S. on both the SEC and Watergate-related charges. On June 22, a Costa Rican court denied the request. Two days later, the Supreme Court upheld the lower court decision, claiming that the 1922 extradition treaty between the U.S. and Costa Rica made no provision for the extradition of those charged with fraud.

Meanwhile, Vesco, perceiving the Costa Rican political climate to be worsening, journeyed to Paraguay, Argentina, and back to the Bahamas in an effort to find a more suitable location for his corporate headquarters.

The next year, 1974, began on an ominous note for both Vesco and Figueres. In the February election, Daniel Oduber,

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[15]Ibid.

[16]Quoted in Ameringer, p. 273.

campaigning on an anti-Vesco platform, became president and the PLN lost its majority in the legislature. Before leaving office, however, Figueres signed an executive order which prohibited the extradition of foreigners without substantial cause. This act, dubbed the "Vesco law" prompted a public outcry of unprecedented proportions. Alan Riding, in a New York Times article, said that the new law would make the extradition of Vesco nearly impossible. He also reported that two San Jose newspapers, La Republica and La Nacion, had formed a citizen's committee demanding Vesco's expulsion. Claiming that Vesco had been responsible for, "moral erosion and interference in local politics,"[17] the group appealed to Figueres to retract the order.

Figueres, however, was adamant in his support for Vesco and the order stood until countermanded by the Legislative Assembly in November, 1976. Shortly thereafter, fearing reprisals, Vesco left Costa Rica permanently, taking up residence in the Bahamas. By this time, Vesco had been sued in Costa Rica by both ICC and IOS shareholders who charged that Vesco had mismanaged their holdings. Trading of all International Controls stock was suspended and the company placed in receivership. Thus, Robert Vesco left Costa Rica stripped of his vast corporate holdings.

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[17]Alan Riding, "Key Costa Ricans Protesting Vesco," New York Times, 16 February 1975, p. 27.

D. The Senate Investigations

During his last two years in Costa Rica, Vesco lived in virtual seclusion and little is known of his activities during this period. Interestingly enough, evidence presented to the Permanent Subcommittee on Investigations of the Committee on Government Operations of the U.S. Senate suggests that Vesco may have been planning to overthrow the Oduber Government by force.

In the course of its year-long investigation of Vesco's activities in the United States, the committee discovered that Vesco had arranged for large quantities of sophisticated weapons and ammunition to be delivered to him in Costa Rica. Senator Henry Jackson, chairman of the subcommittee, alleged:

> . . . that Robert Vesco had in his possession in Costa Rica sophisticated weapons and night vision devices; that Robert Vesco, acting through third parties, planned to acquire some 2,000 Ingram M-10 machineguns; that Robert Vesco was interested in financing a machinegun factory to mass-produce these weapons with several Americans; that Robert Vesco, again through third parties, recently acquired a 54-foot aluminum yacht equipped with sophisticated electronic gear for exact purposes unknown but possibly connected with the transportation of weapons and other contraband.[18]

While the fact that Vesco assembled this arsenal does not in itself indicate that he was planning a coup, his

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[18]U.S. Congress, Senate, Committee on Government Operations, The Robert Vesco Investigation: Hearings Before the Permanent Subcommittee on Investigations of the Committee on Government Operations, 93d Cong., 2d sess., 1974, p. 104.

actions must be considered in light of a letter which president-elect Oduber wrote to Vesco in May, 1974. The letter (a copy of which was submitted to the subcommittee) said, in part:

> Before assuming my responsibilities as President of the Republic, and given the business relations you have had with mutual friends, it seems fitting to leave in your hands this letter with my ideas as to what your business and personal conduct should be during the period in which I will be carrying out my duties as President of the Republic . . .
>
> . . . . . .
>
> Now that a new government is beginning in which no one—I repeat, no one—among its members can be accused of being a shareholder in firms in which you are also one, the situation is different and the country will be able to see more objectively the problems caused by your arrival in Costa Rica.[19]

Clearly, the Oduber Government would brook no interference in its internal affairs. Whether or not Vesco would take steps to unseat Oduber is not known, but the type of weapons assembled by Vesco suggests that an offensive operation of some sort was planned. In the words of Senator Jackson, "To be concerned about one's personal safety is one thing; to amass weapons suitable for outfitting an armed camp is a much more serious and threatening matter."[20] In short, given the Oduber Government's hostility toward Vesco and Vesco's desire for complete

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[19]Ibid., p. 113.

[20]Ibid., p. 56.

autonomy in financial affairs, the suggestion that he would attempt to overthrow the government is not an unreasonable one.

E. Summary

From the case-study, certain observations about the relationships between transnational businesses and sovereign states can be made; perhaps the most important of these observations involves the points of access and resistance within the host state.

In the Costa Rican case, Robert Vesco appears to have determined that the executive branch, particularly the president, was the most accessible to overtures of transnational business. Figueres, on the other hand, believed that Vesco's investments would bolster Costa Rica's sagging economy and, in effect, staked his political future on the establishment of International Controls Corporation in Costa Rica.

As the case-study shows, both Vesco and Figueres misjudged the potential of the legislature, the judiciary, the PLN, and opinion leaders to resist a transnational business the effects of which were judged to be contrary to the interests of the country. Indeed, the concerted response of these four groups was a rejection of irresponsible transnational business, regardless of the economic costs.

In the case of the legislature, this response consisted of the rejection of the offshore financial district proposal and the formation of the investigative committee. The courts responded by denying Vesco's premature request for citizenship. On the extradition issue, it appears that only a procedural matter prevented the extradition request from being granted. The response of the opinion leaders was evidenced in the editorial posture of major newspapers, particularly La Nacion and La Republica and by the formation of the citizen's committee which demanded Vesco's expulsion from Costa Rica. Finally, the most significant point of resistance came from within Figueres' own political party when the PLN nominated Daniel Oduber for the presidency in 1974, dealing Figueres the most telling blow of his political career.

In the aftermath of Figueres' defeat in 1974, one sees the extent to which Vesco depended upon the support of the executive. Oduber, adroitly marshalling his political resources, openly challenged both Vesco and the offshore financial community. Vesco, realizing the importance of a solid alliance with the executive branch, was faced with the choice of either conforming to the Government's demands or unseating the government, an option which he apparently considered.

In sum, this case-study indicates the importance for both the transnational business and the host country of the mutual evaluation of political and economic resources as a prelude to consummating a relationship.

CHAPTER V

CONCLUSIONS

A. Implications of the Study

Having examined the transnational business-sovereign states relationship from the perspective of an individual case, it becomes necessary to suggest some broader implications of the study. Harking back to the questions posed in chapter I, the issues of the legitimacy and resources of transnational businesses and the resources of the host states must be addressed.

The question of the legitimacy of transnational actors is a perennially difficult one. Though it has been maintained that only public (intergovernmental) transnational actors are legitimate, this position ignores both the inevitability and the ubiquity of the private transnational business enterprise in the world system. However, when the enquiry is limited to certain categories of states and certain transnational businesses, the need to define precisely the relationship between them becomes more acute.

In the case of Costa Rica, and other states with limited economic resources, the need for foreign investment is crucial; without such investment, their very existence is threatened. This situation places the state in a precarious position

vis-a-vis the transnational business. Fearing that the transnational business will withdraw its operations if the political climate for investment becomes less favorable, such states are often reluctant to create the regulatory structures necessary to keep the transnationals out of the realm of politics.

As this study showed, this was not the case in Costa Rica. Although a transnational business was able to capture the executive, it was unable to do so in the case of the legislature, the judiciary, the political parties, or the media. As a result, the International Controls Corporation was unable to establish permanent operations in Costa Rica. However, the rejection of International Controls was not without costs; the loss of investment capital which ICC could have provided continues to be felt in the Costa Rican economy. On the other hand, the benefits which accrue from the maintenance of an independent political system are incalculable.

Unfortunately, most states in the less-developed Third World do not possess the political and legal resources which enabled Costa Rica to cope with the pressures imposed by transnational business. Indeed, the predominance of one-party systems, executive-dominated legislatures and impermanent constitutions throughout much of the Third World suggests that transnational businesses intent upon creating their own political environments in such countries would

have little trouble doing so. Quite simply, most Third World political systems provide too many points of access to transnational businesses.

In addition, the variation among transnational businesses bodes ill for the vulnerable host state. While there exists a class of transnational businesses which observe accepted standards of ethics when dealing with sovereign states, there also exists a category of transnational businesses with little regard for the political and legal structures of the Third World. In addition, a heretofore unrecognized series of actions by governments in the industrialized states has resulted in an increase in the number of firms of the latter type. By drafting regulations which restrict the activities of certain types of firms, the industrialized states have forced those firms which cannot comply to go offshore. Unscrupulous promoters like Bernard Cornfeld, Clovis McAlpin, and Robert Vesco, unwilling to submit to such regulation, simply transfer their operations to states where regulation of their activities has not been attempted. Thus, while it certainly is in the interest of the community of industrialized states to regulate the activities of business, in so doing these states have been responsible for the exportation of corporate irresponsibility to the Third World.

B. Regulation of Transnational Business

Having noted that some states have formulated policies which restrict the activities of transnational businesses, certain scholars have recognized the right of Third World states to follow suit. Among them are Keohane and Ooms.

> . . . How can governments construct the proper systems of incentives and constraints to achieve their purposes? Since the effects of direct investment on efficiency and equity will depend upon the circumstances of each case, we are generally sympathetic with the inclination of governments to experiment with regulation.[1]

More specifically, they propose two methods by which regulation of transnational business can be best accomplished: policy coordination and the alteration of bargaining power through regional arrangements.[2]

For purposes of regulating transnational businesses as a whole, such suggestions have obvious merit. However, regulation of offshore financial operations requires a broader approach. For example, many Third World states like Costa Rica have formulated elaborate policies designed to attract legitimate foreign investment. In such states, efforts to coordinate regulatory policy would undoubtedly conflict with established investment incentives. Similarly,

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[1]Robert O. Keohane and Van Doorn Ooms, "The Multinational Firm and International Regulation," International Organization, Winter 1975, pp. 208-209.

[2]Ibid., pp. 191-206.

while many Third World states, again like Costa Rica, have participated in regional economic arrangements designed to enhance their bargaining power, few states have found these arrangements advantageous. In the Costa Rican case, it is doubtful that the Central American Common Market, of which Costa Rica was a member from its inception, had any influence upon Costa Rica's bargaining power vis-a-vis International Controls. In short, only those regulatory proposals which consider the special situations of Third World states will be effective in checking the abuses of the offshore securities industry.

In his analysis of the behavior of offshore securities firms, particularly Vesco's, former U.S. Senator William Saxbe concluded, "Vesco flaunted the fact that he is exempt from prosecution because securities laws cannot be enforced internationally."[3] As such, effective regulation must begin with international cooperation.

> . . . international attention must be given to this problem and I ask that my colleagues give consideration to the formation of legislation to expand the operation of the Securities and Exchange Commission by setting up the ground rules for an international convention to deal with multinational stock and investment fraud.[4]

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[3]U.S. Congress, Senate, Senator Saxbe addressing the problem of multinational securities fraud, 93d Cong., 1st sess., 13 March 1973, Congressional Record, 102:7478.

[4]Ibid.

Although it is doubtful that securities fraud can ever be totally eliminated, the effects of such fraud on Third World political systems could be greatly reduced by the establishment of an international securities and exchange commission. Third World governments participating in such an organization could avail themselves of the sophisticated structures developed in the industrialized states to deal with securities fraud. Governments of developed states would also benefit in that their investors would be protected, resulting in the elimination of the "flight capital" phenomenon. Not incidentally, the onus of responsibility for the exportation of securities fraud to the Third World would also be removed. However, perhaps the most significant result of international cooperation on the financial securities issue would be the elimination of the offshore status of transnational business and the protection of otherwise vulnerable Third World governments.

C. Suggestions for Future Research

Making suggestions for future research in the area of offshore securities firm-sovereign state relationships is difficult in that so little has been attempted and so much remains to be done. Clearly, a primary objective is to identify individual offshore firms and the states in which they operate. The data from the resulting case-studies

would be useful in constructing a profile of a typical relationship of this type.

On a different level, detailed studies of individual states in which offshore firms have operated could be done in an effort to determine the precise effects of such firms on political participation, legislative output, and the development of political parties. The implications of the present study are that these three variables are most likely to be effected by the presence of highly visible transnational actors.

Finally, studies of offshore securities firms should be used in conjunction not only with studies of other transnational businesses, but also other types of transnational actors in an effort to contribute to the development of a systematic theory of transnational relations.

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