

# CODELCO-Anglo American Controversy: Let the Institutions do their Job

**The controversy of the last weeks between CODELCO and Anglo American has emphasized how important it is that our institutional framework operates adequately and normally, in order to guarantee a good business climate. This means that the Government has a clear function: to execute laws and get laws executed and not to become one of the disputing parties, since at the end of the day, if the Government of Chile neglects its arbitrator's role and becomes a player, all Chileans will actually lose.**

Much controversy has been generated by the operation through which the English company Anglo American Plc ("Anglo") sold to the Japanese company Mitsubishi Corporation ("Mitsubishi") 24.5% of its stake in Anglo American Sur S.A. ("AAS") in US\$5.39 billion, estimating 100% of AAS in US\$22,000 billion.

As we know, the operation took place in a particular context: the existence of a valid contract between CODELCO and Anglo, which stipulates the form and conditions under which CODELCO may exercise an option to purchase 49% share<sup>i</sup> of AAS. According to CODELCO, last January the state company had declared to Anglo that it was evaluating to exercise this call option; this possibility should take place once the financing negotiations between the Chilean mining company and another Japanese company, Mitsui & Co. (Mitsui), were concluded.

Although it is a very complex legal issue – entailing the parties to hire the services from important law offices to evaluate partnership, corporative, tax, civil, constitutional and even penal matters – it is after all a controversy between two companies. To forget this simple but crucial issue may have negative consequences for Chile from the most diverse perspectives: political, institutional, economic, etc.

### **The Legal Controversy**

There are two relevant contracts known by public opinion on this matter: the 1978 contract in which ENAMI (National Mining Company) sells to Exxon 86.58% of the shares of Disputada de las Condes, and the 2002 agreement (together with a transaction) by which, having Anglo bought Exxon's equity, the first one is complemented and construed. The problem arises precisely from the interpretation of certain clauses of the contracts, specifically concerning the call option right of ENAMI (today in the hands of CODELCO<sup>ii</sup>) for the total amount of shares liable to this call option<sup>iii</sup>, and the form and term in which this option can be exercised.

Anglo has stated that there is no impediment in the agreements to sell its share in AAS, and that the contracts have been put in the scenario of a potential sale, always safeguarding 24.5% of the rights for CODELCO. The fact that the contracts do not include a non-transfer clause and the free movement of goods principle are part of the arguments that would allow Anglo to sustain this stand.

On the other hand, CODELCO has declared that, based on the contracts' good faith execution principle, once Anglo knew of CODELCO's intention to exercise the option and the percentage of shares involved (49%), the former should have refrained from transferring the ownership during the time elapsed from CODELCO's notice of intent and the month in which the option must be settled.

Thus, the legal debate is focused on the items that the contract provides for or omits and that, as it was agreed by the parties, shall be resolved by the general courts of Santiago, Chile. Today, rather than a broad knowledge discussion on the issue's substance, what is being discussed in the courts is the appeal introduced by CODELCO for the reestablishment of preexisting rights before the Court of Appeals of Santiago— an action aiming to guarantee constitutional rights -, which was accepted for proceeding together with the requested injunction against further moves, with the purpose of "freezing" the said sale of Anglo American's share in AAS to Mitsubishi. While the presentation of Anglo's counter arguments to the Court of Appeals and the decision of the latter are still pending, the dispute remains open.

### **Reform of CODELCO's Corporate Governance (2009)**

We have to consider certain elements in order to evaluate the function of the Government in this matter. One of them is the recent

modification of CODELCO's corporate governance, carried out during the government of former President Michelle Bachelet (Law Nr 20,392<sup>iv</sup>). The purpose of this legal amendment was to improve the company's administration, maximize its economic value and make its production process more efficient, and at the same time, it was aimed at separating the company's ownership from its regulation, since both were mixed up in the State of Chile.

Three fundamental principles were at the base of this reform: excellence, State vision and transparency.<sup>v</sup> These basic principles transversely founded and limited the entire reform. Therefore, filters were considered to avoid the election of merely political positions, or otherwise, minimum high standard requirements were set so as to ensure the selected people's excellence; the appointments should keep in mind a long-run vision, beyond the majority in turn, as a faithful reflection of a company belonging to all Chileans. Likewise, the minority representation of the company "owners" plays the role of clarifying the agreements and measures adopted by the majority, thus facilitating its legal, economic and political control by the citizens. On the other hand, the Securities and Insurance Supervisor (SVS, in Spanish) also supervises the company, now permanently and not only subject to an eventual bonds issuance. Finally, we can highlight that the Board of Directors has the same authorities, powers and liabilities stipulated for that agency in Law Nr 18,046 concerning corporations, and also the same disabilities and incompatibilities, in such a way to rely on a symmetrical yardstick for measuring this kind of companies. This is the only way to ensure real excellence, independence and transparency to its administrating agency, thus allowing it to compete in serious terms in the global scenario.

Eliminating the interference of the Ministers of Mining and Finance in the company matters – and thereby that of the President– was precisely one of the main intentions of the reform. As a matter of fact, after the implementation of the changes, both ministers were no longer institutional members of the company's Board of Directors.<sup>vi</sup>

In view of this institutional framework, it corresponds now to the company's Board of Directors and main CEO to defend the interests of CODELCO, with all the due diligence.

### **The Government's Role**

In this context, it seems evident that we are dealing with differences in the contract's interpretation – and the various complementary

contractual documents - a controversy which is often present in the business world, except for the operation's amount and that CODELCO is one of the parties involved. The latter is curious: CODELCO appears in the world's news not for being a state-owned company – thus relying on a special protection from the Chilean State -, but for being a leading company in the global mining industry, and thus a commercial counterpart respected in all parts of the world. Therefore, it is not advisable for CODELCO to be “respected” in the world due to its dissuasive use of its State power.

It is expectable – although reprobable – that certain people coming from the political world use this incident to look for some profit based on nationalist and chauvinist slogans. In the last days we have seen requirements for legislative intervention of the contracts, nationalization and others along the same lines that, fortunately, were definitely eliminated from our institutional framework with the approval of the Constitution of 1980. Nevertheless, is a key issue for the Government not to confuse its role, thereby forgetting fundamental principles of the Constitutional State, like equality before the law and non-arbitrary discrimination in economic matters. The Government of Chile must behave as a neutral arbitrator before any controversy between companies; this case is not the exception, no matter what the legal nature of CODELCO is. We are dealing with two legal entities, and the Constitution and laws fully recognize their rights and, when it comes to compete in the market, their level playing field.

Because at the end of the day, if the Government of Chile neglects its arbitrator's role – making sure that laws are complied with - and becomes a player, all Chileans will really lose. Since we actually rely on a solid Constitutional State, international firms do not only feel safe to invest in our country – contributing to its economic and technological development, generating employment, developing different CSR actions and paying taxes -, but they are also confident that they will be able to interpret a contract in an openly disagreeing manner before CODELCO, taking the risk of going to the courts and not fearing – in principle – state reprisals of any kind whatsoever. Basically, there is trust in our independent legal system, and to erode that capital would be to go back many decades, towards an institutional State to which we do not want to return. It is precisely in these cases when we have to demonstrate our reputation and why we were incorporated to the OECD.

### **Conclusions**

The controversy between CODELCO and Anglo regarding the sale of the latter of part of its stake in AAS has emphasized how important it is that our institutional framework operates adequately and normally. This implies that the legal controversies are legitimate and must be taken before the corresponding judiciary or arbitration instances; that, as in any business area, there is a wide space for commercial cooperation and negotiation, which is positive, since taking disputes to court is very costly; that international investors compete in equal terms with national companies, and that they must not fear state reprisals when the national player is a state-owned company; and that the Government has a clear function: to execute laws and get laws executed and not to become one of the disputing parties. When doing so, our institutional framework loses and all Chileans lose as well.

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<sup>i</sup> This is a concept incorporated by deed on November 13<sup>th</sup>, 2002, at the notary of Mr. José Musalem Saffie, in Santiago, Chile.

<sup>ii</sup> This option was given to ENAMI or other company appointed by it, but which shall be exclusively owned by the State of Chile.

<sup>iii</sup> Between 24.9% and 49% of the existing shares according to the ownership distribution of Anglo American Sur (Disputada) as of the option's date of exercise.

<sup>iv</sup> With regard to this matter, see Libertad & Desarrollo, Public Issues Nr 1036, 952 and 931 and "A New Corporate Governance for CODELCO". Libertad & Desarrollo, Economic Report Series Nr 193, June 2008.

<sup>v</sup> The concept of "excellence" aimed at the fact that CODELCO wanted to rely on corporate governance with highly qualified people, who would carry out an efficient management with clear commercial approach, especially considering the demanding and competitive scenario in which it develops. The "State vision" implied to overcome the idea that the owner of CODELCO is the government in turn. It is, actually a *state-owned* company, and not a government-owned one, reflecting that there are company owners (all the Chileans), where the government in turn is only the controller for the time being or, in other words, the one holding the temporary majority. Finally, by "transparency" it is meant that CODELCO progresses in the compliance of the same transparency and information delivery standards demanded to publicly held corporations.

<sup>vi</sup> As a matter of fact, before the reform, the goals of the administration and the owners were not aligned. The CODELCO Board of Directors was made up of 7 members: the Ministers of Mining and Finance, three directors appointed by the President, a representative member of the Confederación de Trabajadores del Cobre (CTC, Confederation of Copper Workers), and a representative of the Asociación Nacional de Supervisores del Cobre (ANSCO, National Association of Copper Supervisors). This configuration, where most directors were appointed by the President or were part of the Government, made it more difficult to set long-run strategies, due to the corporate

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governance's short term, which strongly depended on political variables. For example, the challenge of the Ministry of Finance, as director of CODELCO, was to maximize the company's value; however, as the nation's Ministry of Finance, its objective was to obtain the highest possible contribution from the company in order to invest it in high social profitability programs. After the reform, the Corporation is headed by a Board of Directors composed of 9 members, appointed in conformity with the rules stipulated in the referred law Nr 20,392: three directors are directly appointed by the President, four directors are appointed from a list of five names selected by the Consejo de Alta Dirección Pública (Council of Senior Public Management), a director is chosen from a list of five names presented by the Federación de Trabajadores del Cobre (FTC, Federation of Copper Workers), and one director is chosen from a list of five names presented by the Federación de Supervisores del Cobre (FESUC, Federation of Copper Supervisors) together with ANSCO.