

# **Probe International submission to the Export Development Act Review**

**Submitted to Gowling, Strathy & Henderson**

## **Patronage Canada**

The Export Development Corporation Is Unnecessary, Costly, and Unaccountable. It Misleads the Canadian Public and Is an Environmental Wrecker. This Patronage Agency Should Be Shut Down.

By Patricia Adams, Executive Director, Probe International

December 21, 1998

---

### **CONTENTS**

1. Executive Summary
2. Probe International's History Investigating the Export Development Corporations
3. EDC Finances Economic Fiascoes and Environmental Disasters
4. EDC Sinks Third World Citizens in Debt
5. EDC Provides Life Support to Dictators
6. EDC Spawns Moral Hazard
7. EDC Provides a Perfect Habitat for Corruption
8. EDC Hides Its Activities from Canadians
9. EDC Misleads Canadian Taxpayers
10. EDC Costs Canadian Taxpayers Money
11. EDC Doles out Government Patronage -- It Should Be Shut Down
12. Endnotes

---

## **1. Executive Summary**

The Export Development Corporation (EDC) transfers the private risks of international business to the public sector. By socializing this risk, it spawns moral hazard allowing exports, investments, and projects to proceed that are otherwise economically unviable. It also interrupts important messages, conveyed by the market, that an open, transparent, accountable, and honest government that respects the rule of law is good for business. By doing so, it bankrolls or reinforces bad governments against their people and spawns crony capitalism.

Because of its exemption from the Access to Information Act, EDC's activities are sheltered from public view. The absence of public sector oversight and market discipline make EDC's activities a perfect breeding ground for corruption and for business activities that destroy the environment, sink Third World citizens in debt, and cost Canadian taxpayers money. Export credit is a government tool to win economically compromised sales for favoured exporters. Its sole raison d'etre is as a patronage dispensing agency that awards pork barrel contracts and supports unduly risky foreign investments for such firms.

With its preferential financing, tax, and regulatory position, EDC crowds out viable private sector businesses, such as the short-term credit insurance industry. There is no public policy reason for EDC to exist. Trade agreements are increasingly restricting the level of subsidies export credit agencies can deliver to their firms, and other Organisation for Economic Co-operation and Development (OECD) countries are privatizing their export credit agencies. Canada should follow suit. By doing so, it will protect the global environment, encourage a healthy Canadian and global economy, and allow democracy to flourish throughout the Third World.

## **2. Probe International's History Investigating the Export Development Corporation**

Probe International has been investigating the activities of the Export Development Corporation for the past decade. Based in Canada, we have worked with citizens groups in Third World countries, and OECD countries, to research the environmental, social, and financial damage caused by projects supported by EDC. Probe International has 20,000 supporters across Canada, many of whom regularly write letters of concern about EDC to their members of parliament. Patricia Adams, Probe International's Executive Director, and an economist, has written about the costly activities of EDC and other export credit agencies in *Odious Debts: Loose Lending, Corruption, and the Third World's Environmental Legacy* (Earthscan, 1991), and in *The Next City*, Spring 1997. Probe International has corresponded with Canadian government officials, including the various ministers who have been responsible for EDC, and with EDC officials, in an attempt to disclose the details of EDC's operations for the Canadian public. The following research and analysis is the result of Probe International's work investigating the EDC.

## **3. EDC Finances Economic Fiascoes and Environmental Disasters**

EDC refuses to release even the most basic details of its operations, including whether or

not it is supporting a particular project, "because it is our practice to respect clients' and potential clients' right to privacy in regards to their financial affairs." Hence, it is impossible to get a complete picture of the damages caused by EDC's activities. The following, obtained from trade journals, press reports, and correspondence with EDC, is the tip of the iceberg of economically unviable and environmentally damaging projects financed by EDC. These projects are among the world's most notorious environmental destroyers and infamous boondoggles.

### **Three Gorges Dam - China:**

In China, EDC is financing the sale of Monenco-AGRA's super computer (US\$12.5 million in 1994) and the sale of Canadian General Electric's turbines and generators (US\$153 million in 1997) for the Three Gorges dam. The super computer will help coordinate construction of the dam and the forced resettlement of 1.9 million people from their homes. The turbines and generators are intended to generate electricity. The Three Gorges dam is the world's single most environmentally damaging project under construction today. The dam will imperil endangered species along the Yangtze River, turn the river into a cesspool of human and industrial wastes, and submerge archeological sites dating back to 10,000 BC. Three Gorges is also recognized as an economic white elephant. Under optimistic conditions, the Three Gorges dam is estimated to cost US\$34 billion. But a Chinese banker told the Wall Street Journal that he expects the final cost to be US\$77 billion, making it the most expensive source of new power in China today. There are cheaper, cleaner, and more readily available ways to generate power and to reduce China's greenhouse gas emissions than by building the Three Gorges dam. (1) Chinese and foreign experts believe that the Yangtze's sediment-laden waters could destroy the dam's power turbines, cause flooding, and disrupt navigation. Because the dam is being built over fault lines, seismologists fear its weight will induce an earthquake. The dam, now under construction, is plagued with problems such as instability in the rock bed under the dam and popular resistance by the people who are slated to be moved in the next few years.

EDC was the first export credit agency to support the Three Gorges dam -- indeed the first international financier -- despite the better judgement of other institutions. The World Bank has warned that the project will not be economically viable. The U.S. Bureau of Reclamation, the world's foremost dam building agency, withdrew from the project after supporting it for 50 years, arguing that the dam is neither environmentally nor economically feasible. The U.S. Export-Import Bank (Ex-Im) concluded after an extensive review that it did not meet Ex-Im's environmental standards. Public debate and criticism of the dam is strictly forbidden in China; journalists who have attempted to publish critical views of eminent Chinese experts have been jailed, and documents criticizing the dam have been banned.

### **Gehe Yan Dam - China:**

The Canadian federal government quietly gave the green light for a \$130-million EDC loan for the Gehe Yan dam in China, a month after the Tiananmen Square massacre in June 1989. According to the Canadian Press, which quoted a government source, the government would normally have announced the deal with a press release. But the government had strongly denounced the bloody action by the People's Liberation Army and, apparently, did not want to attract public attention in Canada by supporting the regime. A group of seven companies headed by MIL Group Inc. and Asea Brown Boveri Canada won a contract to build turbines and other generating equipment for the dam.

### **Candu Reactors - China, South Korea, Romania, Argentina, and Turkey:**

EDC has been the source of life support for Candu nuclear exports over the years. It has financed Candu sales to South Korea, Argentina, and Romania. In 1974, EDC financed the Argentine government purchase of a Candu nuclear reactor from Atomic Energy of Canada Ltd., another Crown corporation that markets the Candu. The Cordoba plant continually breaks down, threatens the environment, and creates chaos for the economy. It has also resulted in millions of dollars in losses to Canadian taxpayers. Because the Candu could not sell on its own merits, the government enlisted the EDC. Meanwhile, in Romania, slave labour was reportedly used to build that Candu. In South Korea, the reactors are the subject of frequent protests. The Canadian government also tried, but failed, to sell Candus to Mexico. In 1982, Prime Minister Trudeau flew to Mexico City promising \$1.5 billion in EDC loans and another \$4 billion from the Canada Account, which EDC administers, if Mexico chose Candu reactors. Mexico's debt crisis hit soon after and spared Mexico this ill-conceived investment.

In 1997, the Liberal cabinet approved a \$1.5-billion EDC loan to enable Atomic Energy of Canada Ltd. to finance the sale of two Candu reactors to Turkey. In 1998, EDC announced it will back the sale of still more Candus to Korea and Romania. EDC also lent China \$1.5 billion for two reactors to China. EDC will finance these sales despite the fact that we can't run Candus safely and affordably in Canada and the fact that they are so defective and uneconomic that there is no longer a market for them here. Pressure tubes have ruptured and reactor feeder pipes have worn thin, a phenomenon known as premature aging. This increases the risk of a reactor meltdown, yet the cost of fixing these problems is greater than the initial cost of the plant. North America's largest utility, and the Candu's largest customer, Ontario Hydro, is known to have been bankrupted by this technology. Ontario Hydro has shut down one-third of its reactors, 20 years ahead of schedule. Finally, nuclear reactors produce highly radioactive waste by-products that will have to be managed for thousands of years to come. Wherever the old electric monopolies are being dismantled, cleaner and cheaper sources of power, such as combined cycle gas turbines, are the first choice of investors.

All of the foreign Candu sales have been approved by EDC without any formal public debate in Canada or in the recipient country, without environmental assessments, and without independent financial scrutiny. The courts are now considering whether or not the federal government violated its own environmental assessment laws in approving the recent Candu sale to China.

### **Kumtor Gold Mine - Kyrgyzstan:**

In 1995, EDC provided US\$50 million in senior debt to Kumtor Gold Company, a Kyrgyzstan joint stock company one-third indirectly owned by Cameco and two-thirds owned by the government of Kyrgyzstan, for a US\$452-million gold mine in that country. EDC also insured 90 percent of Cameco's subordinated loan and its equity contribution to the Kumtor Gold Company. On May 20, 1998, a truck carrying sodium cyanide to the mine crashed through a bridge, spilling nearly two tonnes of deadly cyanide into the Barskoon River. Company officials failed to notify local officials of the danger of drinking water from the river for five hours. Since then, it is reported, as many as 2,000 people were poisoned, 800 hospitalized, and four died as a result of the accident. Company officials deny responsibility, but Canadian Department of Health expert John Harrison, who went to the site of the accident, thinks if a person drank some of the water "within perhaps up to 24 hours after the exact spill, they would probably get a good size dose." Since then, it has

been reported that 70 litres of nitric acid leaked from a truck on its way to the mine and that the mine is dumping tailings on a nearby glacier. Local community leaders and members of parliament are up in arms, demanding that the mine be shut down until an independent investigation can be carried out, compensation is paid, and those responsible for the harm are held to account.

### **Omai Gold Mine - Guyana:**

In 1992, EDC issued US\$163 million in political risk insurance to Cambior for its Omai gold mine in Guyana. Of this, 34 percent was reinsured by the Multilateral Investment Guarantee Agency of the World Bank group.

Just before midnight on Saturday, August 19, 1995, the earthen dam holding back a waste pond at this gold mine in the Guyanese Amazon erupted, spewing 3.2 billion litres of cyanide and heavy metal-laced effluent into the Omai River. Forming a crimson plume, the effluent snaked its way down a narrow tributary leading to the Essequibo River, Guyana's main waterway. Via helicopter, boat, and runners, the Guyanese government tracked the Omai gold mine's plume and warned people by loudspeaker to stay out of the water. It hastily posted danger signs, warning people not to drink, swim, bathe, wash, or fish in the river and to keep their livestock away from the river's edge. The government then rushed drinking water to communities throughout the region. Within two days, the news of cyanide flowing down the river had devastated the country's fishing industry, with the origin of all fish now suspect. In the markets of Georgetown, Guyana's capital, catches could not be sold, and some Caribbean countries banned all seafood products from Guyana. Other industries, too, suffered in the wake of the spill. Farmers could not sell produce grown along the river, small mining and logging operations were put on hold and local abattoirs, which wash the meats with river water, had to shut down. Guyana's fledgling tourist industry, boasting river eco-tours on this northern tip of the Amazon rain forest, received cancellation after cancellation. Roger Moody of the London-based group Mine Watch, an authority on mining operations, reported that the cyanide plume killed the spectrum of life in the Omai River, from fish to microbes, and caused a ticking time bomb in the Essequibo River by leaching out heavy metals such as cadmium, copper, zinc, iron, and mercury. Within five days, the crimson plume stretched the full 115 miles from the mine to the river's mouth. Throughout the country, Guyanese citizens adopted cries reminiscent of the Yankee Go Home calls that rang throughout Latin America in previous decades: "Take Your Poison Back Home to Canada"; "Stop Killing Our People"; "Let Omai Pack up and Leave."

A Dam Review Committee, created to investigate the cause of the accident, found that the dam broke because of "inadequate application and execution of sound practice for design, construction, supervision and inspection that are well understood in current embankment dam and tailings dam technology." Later, the United Nations Development Programme stated that "baseline and continuous monitoring at Omai have largely been inadequate."

### **Guavio Dam - Colombia:**

West of Guyana in Colombia, EDC backed the Guavio hydroelectric complex in 1989. It has become synonymous in that country with white elephant. Delays due to collapsing tunnels and other technical problems, and stubborn landowners who refused to evacuate their homes to make way for the dam, doubled Guavio's cost to over \$2 billion. The cost overruns equalled the cost of building a subway system for the capital city of Bogota, half of the country's annual coffee exports, or half of the country's social spending. Colombians

suffered as a result, but not Canadian General Electric, which carried out the work.

**Lihir Gold Mine - Papua New Guinea:**

EDC guaranteed \$29.6 million of a syndicated loan from the Union Bank of Switzerland to investors in the Lihir gold mine project in Papua New Guinea -- a project that will dump 400 million tons of waste rock and toxic tailings into the ocean. EDC refused to provide further details of this guarantee.

**Mae Moh Power Project -Thailand:**

In 1979, EDC and the Bank of Montreal supported the sale of a Babcock & Wilcox steam generating unit for the Mae Moh lignite fired generating station in Thailand with a \$15.58-million loan. According to Watershed, a Bangkok-based journal, Mae Moh has become "one of the most serious public health disasters in Thailand's history of economic development." At least 42,000 village people near the plant suffer chronic respiratory diseases, breathing problems, and skin disorders; livestock regularly fall ill and die; large areas of orchards, vegetable gardens and rice crops wilt from acid rain; streams and waterways are blackened by the emissions as well as by the run-off from the coal mining operations. During the cold season from September to November every year, a combination of low temperatures, high air pressures, and the absence of strong winds leaves a dense shroud of toxic sulphur dioxide hanging over the Mae Moh valley. In April and May of 1996, six village people from Sob Paad village in the Mae Moh valley died of blood poisoning, suspected to be caused by sulphur dioxide emissions from the Mae Moh lignite burning plants. Mae Moh is one of the largest point-sources of poisonous sulphur gas in South East Asia.

**Panjapol Pulp Mill - Thailand:**

In 1989, EDC provided one of Thailand's largest pulp companies, which threatened to convert natural forests and farmland to eucalyptus plantations for pulp, with a US\$78-million loan to purchase equipment and services from Klockner Stadler Hurter. Thai peasants hate eucalyptus because it dries up natural springs and destroys fragile tropical soils.

Because Thai environmentalists have difficulty getting information about the project, we asked the EDC if an environmental assessment had been done to ensure that the project was environmentally and economically sound and that those affected would be properly compensated. EDC replied that it had not, even though those impacts could render the project uneconomic, making loan repayments difficult or impossible.

The Thai business press gave front page coverage to this pulp loan giveaway, calling it "the single largest loan and grant package, with the best terms ever awarded to a private Thai group." It went on to say, "Financial experts expressed amazement at the group's successful efforts to clinch the favourable package deal."

**Marcopper Mine - Philippines:**

In 1982, the EDC lent \$1.36 million for the Placer Dome Marcopper mine on the island of Marinduque in the Philippines. Between 1975 and 1991, Marcopper dumped more than 200 million metric tons of tailings from its Mount Tapian mine into the shallow and coral-rich waters of Calancan Bay. The 12,000 fishermen and their families who depend on the bay for their primary source of food and livelihood have been devastated by its demise. The rich diversity of life previously supported by the bay's coral reefs, including an

abundant fish population, has been dramatically reduced. Because of the loss of income caused by poor fish catches, some villagers can no longer afford to buy rice, while others have become ill after eating seafood caught in the bay.

A study conducted in 1997, confirmed the villagers' worse fears. A medical team from the University of the Philippines and the Philippine Department of Health found elevated mercury and lead levels among the children from Calancan Bay area. A doctor from the area has also reported a number of deaths potentially related to metal contamination.

Philippine President Fidel Ramos declared a "state of medical calamity for health reasons" for the Calancan Bay area. In his Proclamation No. 1172, he noted that soil samples collected, as well as air monitoring results, indicate lead levels higher than allowable limits.

That wasn't the end of problems for the people of Marinduque Island. In 1992, Marcopper began dumping its mine tailings into the mined-out Mount Tapian pit. On March 24, 1996, a tunnel beneath the pit failed and over a period of several weeks, more than 2 million cubic metres of tailings poured from the tunnel into the Makulapnit and Boac rivers.

Philippine President Ramos declared the region a state of calamity and the United Nations, which described the spill as an "environmental disaster," reported that the affected rivers suffered a "total loss of aquatic life and biological productivity." At least 20,000 people were affected by the spill. Hundreds of local villagers were evacuated from their homes while many others became stranded. Officials warned villagers not to drink water drawn from their wells for fear of contamination. Provincial officials predict the affected rivers will take 25 years to rehabilitate.

According to United Nations investigators, Marcopper failed to exercise good environmental management at the mine. A waste rock siltation pond operated by Marcopper was found by the UN to be poorly maintained and seeping toxins that exceed international water quality standards.

Local legal rights groups are organizing a lawsuit to seek payment for rehabilitation and compensation for all the people affected by the Marcopper mine.

### **Ok Tedi Copper Mine - Papua New Guinea:**

Located in the Western province of Papua New Guinea, the Ok Tedi mine is supported with \$88 million in export credits from EDC and is the third largest open-cut copper mine in the world. In 1984, a landslide destroyed the dam retaining the mine's toxic tailings, sending 80,000 tons of waste rock containing lead, cadmium, zinc, and copper into the Fly and Ok Tedi Rivers. The mine continued to operate despite its lack of tailings retention facility. Ok Tedi fish stocks have reportedly declined between 50 percent to 80 percent, nearly 70 kilometres of the Ok Tedi River became "almost biologically dead," and 130 kilometres of riverbank (including gardens, plantations, and forests) have reportedly been severely degraded, allegedly causing 30,000 downstream land owners to lose their ability to derive an income from fish and garden crops.

### **Carhuaquero Hydroelectric Project - Peru**

In 1980, EDC approved US\$10 million to support Shawinigan Engineering's work on this hydrodam. The dam was brought to a standstill in the mid-1980s, due to a lack of soft

loans and because of a lack of water. It was later revived, although the area suffers from a seasonal lack of water.

**Chamera Dam - India:**

In 1984, EDC and the Canadian International Development Agency co-financed \$650 million for the Chamera dam in India, winning all the foreign contracts for Canadian exporters, including SNC, Acres International, Marine Industries, and Canadian General Electric. Preliminary documents obtained through the Access to Information Act indicate that the dam is suffering from serious technical problems, including, failure of the concrete lining. Generating units have had to be shut down and repaired, and remedial work on spillway gates has become necessary.

**Guri II - Venezuela:**

In 1978, EDC lent Venezuela \$50 million to support the sale of Canadian General Electric hydroelectric generator sets for the Guri II power plant. Since then, thousands of people have lost their land to the dam reservoir and to transmission lines. Major protests have ensued. Much of the land cleared has been encroached on by settlers and gold-mining companies causing major sedimentation problems in the reservoir. Human rights groups criticized the "aura of secrecy" around the construction of these dams and noted that apparently no consideration was given to the environmental or social impact of the hydrodam complex.

**Indah Kiat - Indonesia:**

In 1996, EDC provided Cdn\$285 million in limited financing for the construction of the Indah Kiat Nine project in Indonesia, which has been responsible for massive destruction of primary rain forest.

**Soroako Nickel Project - Indonesia:**

In the 1970s, EDC lent up to \$60 million for INCO's massive open-pit nickel mine in Indonesia. The mine's dam caused the flooding of rice fields, coconut groves, and a local mosque, leading local people to launch a law suit. It also disrupted the migratory patterns of eels, an abundant and important protein source for local people.

**Food Irradiation - Algeria:**

EDC supported the sale of a food irradiator to Algeria. Irradiated food has not been proven safe for human consumption. Free radicals form during irradiation, creating carcinogens and mutagens. Irradiation kills vitamins, causes meat to smell like "wet dog," and disguises botulism.

**Yacyreta Dam - Argentina:**

In 1987, EDC agreed to lend US\$86.4 million to finance the sale of four Canadian General Electric turbines for the Yacyreta dam on the Parana River. Yacyreta was supposed to cost US\$3.7 billion. Today, this figure is expected to top \$10 billion. Yacyreta has been called the dam that financed the Falklands war. It was also called a "monument to corruption" by Argentine President Carlos Menem. Cost overruns, law suits from some of the 50,000 people who have had to move to make way for the dam, and shortages of money have meant that the dam will probably never operate as planned. It is alleged that the filling of the reservoir introduced stagnant, polluted water and contaminated ground water supplies used for drinking. Improperly cleared vegetation in the reservoir area also caused water quality problems. Crops, fish stocks, and human health have been adversely affected.

**Musi Pulp - Indonesia:**

In 1997, the Musi pulp and paper project was reportedly supported with a \$50-million EDC loan. Siti Hardiyanti Rukmana, the daughter of former Indonesian president Suharto, is believed to be one of the owners of the venture. The Musi Pulp project gets its supply of wood from a 193,500 hectare tropical timber estate, part of its primary tropical forest, in South Sumatra. The respected Indonesian environmental organization, the Indonesian Forum of Environment (Walhi), said the venture will cause "massive social problems" by taking away local villagers' livelihoods because the company "seized the people's forests and farmland without any prior consultation." In 1997, Indonesian Minister of Forestry Djamiludin accused the company of contributing to the infamous forest fires that raged across the country that year.

**Pangué Dam on the Bio-Bio River - Chile:**

EDC announced in 1994 that it would lend US\$20.5 million to finance the export of Canadian generators and cables from Alcatel and Canadian General Electric for the Pangué hydroelectric dam on the Bio-Bio River in Chile. The Pangué dam, the first of six on the Bio-Bio River, flooded lands of the Pehuenche native people and appropriated their forests. It threatens unique fish species, and disrupts water flows to downstream farmers. It is built in the second most seismically active area of the world, threatening to cause reservoir induced seismicity, landslides, and avalanches. So rich with sensational gorges and towering waterfalls, the Bio-Bio River, many have argued, is worthy of world heritage site status.

**4. EDC Sinks Third World Citizens in Debt**

xxx

Until the 1960s, private commercial banks and other financiers serviced their exporting clients and imposed on them the discipline of the market. The Pearson Commission, struck by the World Bank in the late 1960s to investigate Third World poverty and led by Canada's Lester Pearson, analysed the newly created export credit agencies and observed that once they started guaranteeing commercial trade, prudent lending and guarantees by the private sector gave way to a free-for-all. The private banks are becoming "less concerned about the borrowing country's credit worthiness because of the facility of export credit insurance," the Pearson Commission warned. Imprudent use of export credits "involves very real dangers."

The Pearson Commission also found that export credits were an expensive form of external finance. Though the interest rates offered the borrower were favourable, the exported product would usually be marked up, by as much as 100 percent.

To its dismay, the Pearson Commission also discovered that export credits often financed projects whose only "feasibility study available is one prepared by the equipment supplier," and that borrowing countries pushing reckless development schemes often favoured export credit agencies because they enforced less "rigorous tests of economic desirability."

More than one project rejected for financing by the World Bank Group on economic grounds has been promptly financed by an export credit. This is the most unfortunate aspect of export credit finance: it provides a temporarily painless way of financing projects conceived by over-optimistic civil servants, by politicians more concerned with immediate

political advantage than with potential future economic problems, and by unscrupulous salesman for the manufacturers of capital equipment in developed countries.

All this, according to the Pearson Commission, created both an excessive use of short-term export credits to finance long-term investments and a serious balance of payments problem for developing countries: "Since the mid-1950s, [this] has been a major reason for the need to reschedule the debts of a number of countries, notably Argentina, Brazil, Chile, Ghana, Indonesia, and Turkey."

"This rescheduling will be more difficult in the future if export credits are imprudently used," predicted the Pearson Commission in 1969.

Imprudently used they were: Export credit programs continued at full throttle throughout the 1970s. Then the debt crisis hit in 1982. While the debt crisis of the 1980s frightened commercial banks away, export credits became an even more important source of external financing to the Third World and to Western exporters. By the late 1980s, according to estimates by the National Foreign Trade Council, an American export industry association, one-third of the \$30 billion a year in capital goods traded worldwide was financed through tied aid and export financing packages.

Over the past decade, annual new commitments of officially supported export credits have increased over fourfold, from about \$26 billion in 1988 to \$105 billion in 1996. In 1990, 15 percent of the Third World's debt was owed to export credit agencies. By 1996, 24 percent of the total indebtedness of all developing countries was owed to export credit agencies, accounting for 56 percent of their official debt.

That debt has been so unsustainable that Canada has had to forgive many EDC loans to Third World nations. According to correspondence from Finance Minister Paul Martin (December 9, 1998), since 1991, Canada has forgiven over \$2 billion worth of debt owed to various Canadian agencies by Benin, Cameroon, Democratic Republic of Congo (formerly Zaire), Republic of Congo (Brazzaville), Egypt, Guyana, Honduras, Ivory Coast, Madagascar, Poland, Senegal, and Tanzania. As much as \$600 million of that may have been debts that those countries owed to EDC. Precise figures are unavailable because Mr. Martin refuses to release numbers "in order to respect the agencies' [EDC and others] needs for commercial confidentiality." EDC has released these numbers for just a few years.

We predict that new unsustainable debts will be created and that the export credit agencies (ECAs), including EDC, will be required to forgive them in future. According to the World Bank, about half of all new ECA commitments in recent years has supported project finance, "mainly for large infrastructure projects in power generation, telecommunications, and transport." This makes ECAs the single largest public financiers of large-scale infrastructure projects in the developing world, exceeding by far the total annual infrastructure investments of multilateral development banks and bilateral development aid agencies.

## **5. EDC Provides Life Support to Dictators**

By providing state financing for projects that the private sector considers too risky, EDC

helps blunt the incentive of recipient governments to reform. If the money is available to the Chinese government to pay for a Candu nuclear reactor, without any conditions attached, why should the government of China, enforce the rule of law, introduce transparent and fair regulations for the financial sector, and respect the rights of its citizens to scrutinize the wisdom of a Candu system before buying one? Export credit, says *The Economist*, "slows down economic reform."(2)

By allowing Canadian corporations to ignore the financial risks of dealing with dictators or less odious governments that are otherwise unpredictable, unstable, and unaccountable, EDC helps sponsor bad governments and crony capitalism. When EDC stepped in to insure Cambior against the risk that its Omai gold mine assets might be expropriated, that it might not be able to transfer its funds out of Guyana, and that it might not be able to enjoy its assets due to war and insurrection in Guyana, it interrupted an important message that the private sector would have otherwise sent to governments that don't respect the rule of law or the rights of their citizens: Clean up your act, prove to us that your government is legitimate and has the confidence of the people, show us that the courts work fairly, govern your nation democratically, and then we'll invest. Or as Cambior's manager of investor relations Robert LaVallière put it, "If you have \$10 in your pocket and you can invest in Canada or Colombia, then where do you invest? Canada!"(3)

## **6. EDC Spawns Moral Hazard**

By transferring the risk of international business dealings from the private sector to the Canadian taxpayers -- by socializing the risk -- the EDC creates a moral hazard among exporters, Canadian companies making foreign investments, and the banks whose loans are guaranteed by EDC. Cambior's manager of investor relations, Robert LaVallière, put it succinctly when he said his company would not have invested in the Omai gold mine without the US\$163-million political risk insurance package from EDC. "We have shareholders, we want to be safe." Speaking about the Candu sale to China, a commercial banker, quoted in the *Globe and Mail*, said that no commercial bank would lend against a nuclear power plant.

Moral hazard is created when an investor, lender, or exporter can take a financial risk with little fear of a loss. That weakens the integrity of financial contracts and the scrutiny that contracting parties would otherwise apply to each other. It also results in excessive risk taking because a third party -- the Canadian taxpayer in the case of EDC -- bears the risk.

One of the foremost magazines on megaproject financing, *Project Finance*, described recently how export credit agencies use tax dollars to convince the private sector to take risks they otherwise wouldn't. In its annual review of export credit agencies this year, *Project Finance* noted that in the wake of the Asian contagion and the Russian meltdown, private project sponsors were returning to the protective embrace of export credit agencies. These sponsors had grown impatient with the export credit agencies, even questioned their relevance. "Many claimed that the agencies were too bureaucratic, too unresponsive and needed to evolve." Instead, projects were consummated with bonds and loans with a minimal amount of guarantees or support. "In hindsight, bankers and sponsors realise that they went to [sic] far," said *Project Finance*, adding, "the export credit agencies are back in fashion." (4)

## **7. EDC Provides a Perfect Habitat for Corruption**

Ten days after EDC financing for the Candu sale to Argentina was put in place in 1974, Atomic Energy of Canada, which markets the Candu, put \$2.4 million into a Swiss bank account for an "agent" to clinch the sale, leading to bribery investigations by Canada's Auditor General, a parliamentary inquiry, and a public furor. In response to such questionable activities, the Canada government decided to make a virtue of a vice. Revenue Canada pronounced that Canadians could legally bribe foreign officials and even made bribes tax deductible, provided the briber received a receipt. Then Trade minister Jean Chrétien explained: "Commercial practices in other countries sometimes are different from ours. I am not about to condemn the morals of anybody. It would be very presumptuous for Canadians to tell other people how to conduct their morals." Chrétien urged Canadians not to put their "head in the sand" and pass up overseas sales by being rigidly moralistic.

Now, according to a recent internal World Bank report, more than 20 percent of World Bank loans to Suharto-led Indonesia were "diverted" to bureaucrats and politicians. Much of the corruption, said the report, occurs in a culture that "blatantly expects civil servants to supplement their incomes by such means." Of funds intended to compensate citizens whose land was expropriated for dams and forestry projects, government officials and their relatives pocketed an estimated 50 percent to 80 percent.

For years the World Bank insisted that it had tight control over its monies, that none of it was lining the pockets of politicians and their families. That, the world now knows, is false. World Bank loans were public assets turned into private assets, though the Indonesian public at large remained liable to pay those debts back.

EDC's Candu sale to Argentina was associated with bribery and corruption, it has co-financed many of the same projects with the World Bank (such as the Yacyreta and Pangué dams) and extended credit to the governments of the world's most notorious kleptomaniacs -- former president Suharto of Indonesia, former president Mobutu Sese Seko of Zaire, to name just two. Corruption is regarded as such a major problem and an economically debilitating phenomenon that multilateral efforts are underway to curtail it. Corruption is not an inherent part of Third World culture. Rather, it is the result of the lack of public sector oversight and market discipline that is typical of EDC's transactions. As EDC has operated in a dark, unscrutinised, and unchecked environment, a forensic audit should be done of its operations over the years, to assure taxpayers that its transactions have been honest.

## **8. EDC Hides Its Activities from Canadians**

EDC's exemption from the Access to Information Act gives EDC the power to shelter its activities and its financial dealings from public scrutiny. This exemption prohibits competitors in the insurance industry, for example, from proving unfair pricing practices. It blindfolds the Canadian public who are concerned about EDC's activities. For example, EDC will not tell us if it is considering supporting a particular exporter or overseas investment before the commitment is made. In contrast, the World Bank provides such information. Nor will EDC tell us if it has supported a particular project in the past. The

standard response we receive from EDC's Public Affairs Advisor is, "Unfortunately I cannot help you because it is our practice to respect clients' and potential clients' right to privacy in regards to their financial affairs."

Similarly, EDC will not disclose information about the status and state of its outstanding loans. In 1990, I wrote to then president of EDC, Mr. R. L. Richardson, requesting details of the Paris Club rescheduling of EDC's loan to Argentina for the Candu reactor. EDC responded, saying that the "details regarding principal and interest payments for the loan" and "rescheduling terms for Argentina are confidential." In the same year, I wrote to the U.S. Export-Import Bank, requesting similar details for Ex-Im's loan to the Philippines for the Bataan nuclear power station. Ex-Im responded promptly with details of its original loan and with a thorough accounting of the rescheduling agreements, plus a repayment schedule.

EDC's access to public resources without public accountability is unacceptable. EDC should be subject to the Access to Information Act. The act would protect legitimate business claims for commercial confidentiality while protecting the public's right to know what EDC is doing on its account. Inexplicably, the private sector seems to have an attitude of entitlement -- that they are somehow entitled to public resources from EDC without the concomitant responsibility to report to EDC's shareholders and taxpayers. I believe that, if the private sector does not like the disclosure requirements of a public agency, they should rely on private sector resources instead.

Finally, many of EDC's sovereign loans have been forgiven as a result of Paris Club agreements. While the Minister of Finance will say which countries' loans have been forgiven, he will not reveal their value, in order to respect EDC's needs for commercial confidentiality. We can see no such need. These forgiven loans were state-to-state transactions. Taxpayers have a right to know how many of their government's loans to other governments have been forgiven in order to evaluate the risks taken on their behalf, and the management skills of public agencies operating in their name.

As the former Auditor General, Kenneth Dye, stated in his 1989 Annual Report to Parliament, "Without good information, Parliament cannot legislate. Without good information, governments cannot govern. Without good information, Members of Parliament cannot hold governments to account. These things have always been true."

## **9. EDC Misleads Canadian Taxpayers**

### ***On its environmental record:***

On its environmental record, EDC grossly distorts reality and shamelessly misleads the Canadian public and Canadian Parliamentarians. In a January 1996 letter to a member of Parliament, former EDC President Paul Labbé claimed that the EDC was an environmentally responsible export credit agency. **(5)** EDC's 1997 Annual Report repeats the claim: "EDC has long taken environmental concerns into account in its analysis of risk, since transactions that are not environmentally sound may, in addition to their damaging effects, not be viable and thus may be poor credit risks." The evidence that these statements must be false, is overwhelming.

Probe International has been monitoring the activities of international financiers for the past two decades. The details we have managed to secure about EDC's activities only scratch the surface. Nevertheless, we can unequivocally say that EDC has supported the majority of damaging projects brought to public attention in the past 20 years. As such, it rivals the World Bank as an environmental destroyer. According to our information, EDC is far and away the most environmentally reckless export credit agency in the world. We think another statement, by EDC public affairs advisor Rod Giles quoted in an Inter Press Service article, better indicates the kind of care EDC takes with the environmental effects of its projects: "We did not ask Monenco AGRA, a Canadian company, for environmental assessments when we gave it a \$12-million loan to supply equipment for the Three Gorges dam in China, nor did we ask for such an assessment when we insured a \$1-billion sale of a Candu atomic reactor to Romania."

The EDC has also tenaciously lobbied against having to comply with Canada's environmental assessment laws, which would force EDC to conduct public environmental assessments for such projects as the Omai gold mine in Guyana and the Three Gorges dam in China. It is now attempting to draft an Evergreen Document -- a voluntary environmental review procedure that it would follow. Environmental review procedures, especially ones enforced by proponents voluntarily, are corruptible to political interests, are unreliable, and are therefore unacceptable.

In his 1996 letter, Mr. Labbé also claimed that EDC ensures that the high environmental standards embedded in Canadian technology and products are made available in other countries. Yet with the Three Gorges dam, an investigation by the Complaints Committee of the Association of Professional Engineers of Ontario found that the standards used by the Canadian engineers in their feasibility study for the dam differed from those that would be used in Canada. Furthermore, those engineering companies -- including Hydro-Québec, BC Hydro, SNC-Lavalin and Acres International -- failed to complete an environmental assessment for the dam and instead, relied on a thoroughly discredited Chinese assessment to declare the project feasible.

Mr. Labbé also grossly misrepresented Guyana's Commission of Inquiry into Cambior's massive cyanide spill at its Omai gold mine, claiming falsely that the Commission's report "does not indicate the company was responsible for the spill." In fact, the Commission stated that:

[T]he tailings pond was built as a receptacle for the storing of large quantities of a noxious substance, to wit, water with a high concentration of cyanide, and that if it were to escape, it could foreseeably cause harm to the environment, and in particular the Essequibo river, as well as result in financial loss to the residents and all other users of the river. Therefore, the company had a legal obligation to ensure that the substance did not escape: and it is no excuse that they employed competent engineers to execute the work. Therefore, in the Commission's view they would be liable for all the foreseeable loss and damage that was a direct result of the effluent entering the Essequibo River.

Furthermore, the Dam Review Team, in its final report on the causes of the tailings dam failure said, "We are at a loss to explain why the design and construction of these critical elements of the dam, whose importance to its safety were evidently recognized and understood, were executed so inadequately." They concluded, "in retrospect, it is clear that the Omai tailings dam as designed and constructed was bound to fail."**(6)**

### ***Claiming it makes Canadian exporters and investors competitive***

EDC's claim of making Canadian exporters competitive is also economic make believe. Canadian exporters that win contracts with EDC backing haven't won them because they've produced a better product for less money than their competitors: Rather, the Canadian government has subsidized them more than other governments have subsidized competitors. The effect of this on a nation's economy is unhealthy, as documented by a French study that tidily expressed what everyone in the business knows, but few admit: "Export-credit subsidization wastes France's scarce public resources in promotion of the wrong industries exporting the wrong products to the wrong markets."

### ***Claiming it operates on a commercial basis***

EDC's claim of operating on a commercial basis is also grossly misleading. Rather, it operates on the good faith and credit of the Canadian taxpayer: The loans, guarantees, and insurance packages it offers are subsidized. Some of the advantages the EDC enjoys over the private financial services sector include: EDC does not pay taxes; it borrows money at the preferred rates of the Canadian government; it is not subject to supervisory and regulatory requirements; and it does not face demands to earn a competitive rate of return for shareholders.

A report by the U.S. Commercial Service explains how EDC undercuts both the Ex-Im Bank and the commercial banking sector with its subsidized lending and insurance rates.

Essentially [EDC] acts like a commercial bank in commercial markets, providing generous credit terms to exporters and their buyers, and enforcing looser credit standards for the buyers than Eximbank would require. EDC is also more generous in accepting foreign content than Eximbank, bending its own rule of at least 50 percent Canadian content in cases where an important product or market is being targeted for development. EDC will also finance the entire amount of the loan up to 85 percent of the value of the export (the OECD limit), covering both Canadian and foreign content.

Moreover, EDC's cost of funds (its borrowing cost) is often lower than that of the commercial banks with which it competes. This enables it to be very aggressive in its pricing of credits. It can borrow at the Canadian government rate -- the Canadian Interest Reference Rate (CIRR) -- and if it is lending in U.S. dollars, it can price its loan at Eximbank's low rate, as mentioned above. That rate is currently 6.3 percent fixed for five years, which is even better than the floating LIBOR rate plus a spread, adjustable upwards after six months.

Exim's credit terms and standards are tougher than EDC's, its U.S. content rule is 51 percent or greater, and it only finances the U.S. content portion of the item being exported. While its cost of funds and its lending rates are low, so are EDC's, and EDC, unlike Eximbank, operates in the developed world where it competes directly with the commercial banks that are lending to U.S. companies in that market at often higher rates.

(7)

## **10. EDC Costs Canadian Taxpayers Money**

In protecting the private sector from the necessity of making prudent decisions, and in pushing these exports and overseas investments for political purposes, export credit agencies and their political masters have cost their own taxpayers. In 1990, the U.S. Export-Import Bank went into technical insolvency when it was forced to establish a US\$4.8-billion reserve to cover the third of its loan portfolio deemed delinquent. Britain's Export Credits Guarantee Department (ECGD) was also forced to set aside reserves against its delinquent debts. So, too, did the EDC, after our Auditor General accused it of misleading taxpayers with financial statements that didn't conform to generally accepted accounting principles.

EDC and the other export credit agencies have their own way of pretending that their bad loans aren't bad: They wish away the problem by rescheduling delinquent debts. Under rescheduling, if a debtor falls behind on interest, the creditor converts the interest to principal. If a debtor falls behind on principal, the government may adjust repayment dates or provide a repayment holiday. Little wonder that Canada's former auditor general, Kenneth Dye, called rescheduling "a shield to hide from public scrutiny losses the government has suffered or is likely to suffer on its sovereign loans. Paperwork disguises reality." Or that Eugene Rotberg, a former World Bank treasurer, sees a "financial charade" in loan rescheduling: "If someone owes you money and you say 'You don't have to pay it for ten years,' then ten years go by, and you don't collect, and another ten years -- well you may not wish to call that forgiveness for bookkeeping or political purposes, but you're not getting paid....Now I'm not going to talk about how many angels can dance on the head of a pin, but that is de facto forgiveness." EDC rescheduled the loan to Argentina for the Candu reactor sale, but denied losing any money on the deal.

EDC argues that it does not cost taxpayers money, claiming it operates on a financially self-sustaining basis. But the government does bail EDC out of its bad loans: The government has instructed EDC to forgive the sovereign debts of more than a dozen countries to date. To keep EDC's books unscathed as a result of forgiving these debts and writing them off, the government of Canada makes payments to EDC to compensate for amounts that otherwise would have been due from debtor countries. Thanks to this bailout, to a rapid growth in gross loans receivable, and to the reinstatement of impaired loans as performing loans, the EDC has managed to reduce its impaired loans as a percentage of its gross loans receivable from 37 percent in 1993 to 14 percent in 1997. EDC's rapid growth in loans receivable is, in part, due to the \$1.5-billion loan to China for the Candu sale. Unusually, the government of Canada, rather than the Chinese government, has accepted responsibility for this loan in the case of default.

By borrowing its funds on the good faith and credit of Canadian taxpayers, EDC weakens Canada's credit rating and increases the government's borrowing costs. By its own admission, EDC seeks out higher risk markets than the private sector can tolerate.

Earlier in the year, EDC issued a press release to reassure Canadian companies doing business in Southeast Asia that it would be there for them. "Despite recent declines in investor confidence in Southeast Asia due to the current financial crisis, EDC remains open for business. In fact, EDC is increasing its business activity in the region and is well positioned to help Canadian exporters maintain their long-standing presence in many key markets." **(8)** Ian Gillespie, EDC President and CEO, went on to explain that "While there is no question that the risk of doing business in Asia has increased, thus posing significant selling and financing challenges for exporters, EDC is there to help shoulder the risks and

convert challenges into opportunities. We are in there for the long haul." When it became apparent that claims paid out under risk management programs in the first half of 1998 had grown 35 percent, EDC remained undaunted, explaining that this increase "is clear evidence of EDC's value to Canadian companies competing internationally." **(9)** Rather than acting cautiously on behalf of taxpayers, EDC intends to march boldly into Asia next year, despite signs that those economies are not prudently managed.

## **11. EDC Doles out Government Patronage -- It Should Be Shut Down**

Canada is a trading nation -- about 40 percent of our GDP comes from exports -- and we have a vital interest in facilitating international commerce. NAFTA and other measures to reduce government interference in trade will help to open up our economy and those of our trading partners to mutual advantage. But EDC, and the politically inspired Team Canada trade missions, for which EDC is the steroid, undo trade liberalization efforts and bleed the national economy.

For whose benefit? The big ticket items for EDC and these trade missions tend to be economic basket cases, such as nuclear power plants and megadam technology that have burned takers back home. Their boosters -- Atomic Energy of Canada and wings of Hydro-Québec, Ontario Hydro and B.C. Hydro, and the many private sector companies that feed at these Crown-owned troughs -- would be bankrupt without government largesse from the likes of EDC, and at the first whiff of true trade liberalization. Gerald Rowe, assistant treasurer of General Electric Canada, understood the importance of EDC well. He implored the Legislative Committee that was considering the amendments to the Export Development Act in 1993 to accept the proposed amendments because his company and other manufacturers "certainly would not survive without [EDC]." If EDC's resources were not increased, he argued, "they're going to reach their ceiling. That's not good. That will cut us off at the knees and we'll be out of business."

Rather than promote viable trade, EDC, in reality, is a patronage machine touting government-propped trade. Its web of influence should be curtailed by privatizing the services that the private sector can provide. The short-term export credit insurance services of EDC are no longer needed. The insurance industry in Canada can provide those services and should. Similarly, EDC should never have been in domestic credit insurance services and should withdraw. The big infrastructure contracts which could not attract private credit insurance were never viable. There is no public policy reason that these pork barrel contracts should proceed.

"Governments love to think," says *The Economist*, "usually mistakenly, that their economies will be better off if they help things along than if they leave well alone." The dean of the Yale School of Management, Mr. Garten, concurred, lamenting the effect of export credit agencies arguing that "In the best of worlds, governments ought to get out of this business altogether. But the marketplace is corrupted by the presence of government."

The signs that governments are beginning to withdraw are hopeful, despite what *The Economist* calls, "the temptation to meddle" by these "thoroughly modern mercantilists." OECD rules now limit tied aid and eliminate beggar-my-neighbour subsidies on export credit guarantees of two years or more. At the same time, export credit agencies around the world are beginning to hive off those sections of their agencies that can be provided by the

private sector. This is good news. EDC should follow suit. It would be good news for the Canadian economy.

It would be good news for the soul of the nation, too. To dispense largesse to favoured firms, or to politically important constituents, and to make subsidy-dependent parts of our economy seem viable, the government cynically bends rules out of shape and abandons principle and honour. To secure a Candu reactor sale in China, the Prime Minister tried to exempt EDC from environmental scrutiny by stealthily issuing an order-in-council that changed federal regulations (the courts will decide if this change was legitimate). When no other foreign government would touch China's Three Gorges dam, the government reversed its policy and stepped up to finance the dam. When the cyanide spill occurred at Cambior's Omai gold mine in Guyana, Canada's High Commissioner lobbied behind the scenes to get the Guyanese government to reopen the mine, without too many questions being asked about the wisdom of using cyanide.

By turning politicians and civil servants into salesmen, and businessmen into politicians, we corrupt our governing structures and undermine our economy. A process to dismantle the EDC machinery should be put in place and carried out in an orderly fashion.

---

## 12. Endnotes

1. Patricia Adams and Grainne Ryder, "China's Great Leap backward," *International Journal*, Toronto, Fall 1998.
2. "In OPICKle," *The Economist*, September 21, 1996.
3. Patricia Adams, "Patronage Canada," *The Next City*, Spring 1997.
4. "Taking the credit," *Project Finance*, November 1998, p. 29.
5. Letter from Mr. Paul Labbé to Ms. Beryl Gaffney, M.P., January 26, 1996.
6. Dam Review Team, "Final Report on Technical Causation Omai Tailings Dam Failure, to the Guyana Geology and Mines Commission," January, 1996, p. 33.
7. "Canada: The EDC: Bank Look-Alike," *International Market Insight Reports*, August 1998.
8. "Export Development Corporation continues to support exports to Asia," EDC Press Release No. 5, February 12, 1998.
9. "Customer demand drives EDC's mid-year business results to new levels," EDC Press Release, August 13, 1998.

SEE: [Statement to the House of Commons Standing Committee on Foreign Affairs and International Trade](#), November 16, 1999