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"Building Prosperity in Latin America: Investor Confidence in the Rule of Law"
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Chairman Salmon, Ranking Member Sires, and members of the Subcommittee on the Western Hemisphere, I am honored to have the opportunity to appear before you today to share my views about the rule of law in Latin America as it affects foreign investment. I commend the Committee for holding this important hearing.

I first traveled to Central America in 1985 as a young law firm associate. I had just been named Chair of the American Bar Association's Latin American Law Committee largely, I am convinced, because Latin America was going through the "lost decade" and no one else wanted the job. I was then asked to spearhead the ABA's efforts to improve the rule of law in Central America.

What I learned on that first trip has stayed with me forever. On the first day of my visit, my meeting with the US Ambassador to Guatemala was cut short when the Ambassador's secretary slipped him a note. The top labor leader in the country had just been given two hours to leave the country -- or else -- by unidentified gunmen, had no place to hide, and needed American help to flee the country. Apparently that was not unusual during labor negotiations in those days. On the next leg of the trip, in Panama, the administration of General Noriega looked askance at an American organization's efforts to improve the country's judiciary.

But nothing prepared me for what I saw in El Salvador. Never mind that in the midst of a bloody civil war my meetings at the Salvadoran Supreme Court were constantly interrupted by the staccato of gunfire nearby. When the Chief Justice of the Supreme Court -- who would be assassinated by a car bomb two years later -- showed me the library, I noticed that there were no law books beyond 1968. "Where are the statutes and cases for the last 20 years?" I asked. "We have only a couple of books since 1968", he shrugged. "We just don't have the money." That's when I decided that, if we wanted to help Central America escape its cycle of violence and poverty by encouraging commercial development, one of our first projects would be drafting a commercial arbitration code. In this part of Latin America, no sane businessman would trust his investment to the local judiciary.

I mention this incident to illustrate that the challenges to the rule of law are not new. They are long-standing, will take a long time to fix, and -- while we can help -- will only be overcome with domestic support and buy-in from local governments, lawyers, private enterprise and civil society. And until addressed, these challenges will continue to hinder all commercial activity, be it foreign or domestic.

To be sure, there are some bright spots in the Latin America rule of law firmament. According to the *World Justice Project's Rule of Law Index* (WJP) for 2014, which ranks 99 countries based on indicators such as constraints on governmental powers, absence of corruption, open government, regulatory enforcement, and civil and criminal justice, countries such as Uruguay and Chile place high, sometimes higher than the United States in several criteria. But overall the region falls to the bottom third in most of the factors used by the WJP. So today the vast majority of foreign investors going into Latin America still prefer arbitration, as opposed to the local courts, as a means to resolve their disputes.

But as I learned in thirty years of representing investors in Latin America, arbitration is not a panacea. The problem is broader. Not everyone can arbitrate, and even when you can at some point in the arbitration you may need to resort to the local courts. Plus local investors, especially small businesses, are not always familiar with arbitration. More importantly, a decision to invest is not merely based on the availability of arbitration. It is based on an investor's perception of whether the legal system is transparent, stable and free from bias and corruption, whether property rights are enforced, and whether fundamental personal rights are respected. As the WJP points out:

> Imagine an investor seeking to commit resources abroad. She would probably think twice before investing in a country where corruption is rampant, property rights are ill-defined, and ineffective means to settle disputes undermine legitimate business and drive away both domestic and foreign investment.

On all of these scores, Latin America certainly fares better than it did three decades ago, but it still has a way to go.

According to *Transparency International's Corruption Perception Index*, which ranks the perceived levels of public sector corruption in 177 countries and territories around the world, over two-thirds of the nations in the Americas scored less than 50, indicating a serious corruption problem even after including Canada which scored 81 and the U.S. with a score of 73. Venezuela was 160th out of 177. When asked by respondents whether a high ranking government official exposed for taking government money was likely to be prosecuted or punished, less than 30% of Latin Americans answer yes, dead last among all regions of the world.

In other indicators Latin America does not fare much better. Central America and Venezuela rank among the most dangerous countries in the world, and the population's perception of safety -- when asked if they feel safe or very safe when walking around their neighborhood at night -- is less than 40%, again the lowest of any region. No wonder: the conviction rates in Latin America are abysmal. In Panama, only 12% of burglars are captured prosecuted and punished. And 12% is the highest in Latin America: in Venezuela the number is 1%. As for murder cases, Honduras has seen a 250% increase in homicides in the last few years, but the impunity rate is over 90%. Even in Mexico, according to one study from last year 80% of homicides go unpunished without conviction or even trial.

I could go on, but you get the picture. In other traditional indicators of the rule of law, such as ensuring compliance with regulations, and the effectiveness of judicial oversight, there is still much room for improvement in Latin America, despite the undeniable advances we have seen in places such as Brazil, Mexico and Colombia.

Both in private practice and in government, I have witnessed how weaknesses in the rule of law can impact investment, in addition to wreaking unspeakable human tragedy. El Salvador has had the lowest rate of foreign investment in Central America for several years, and when we asked business -- both local and foreign -- why, the reason given almost always was insecurity. Crime affected all levels of Salvadoran commercial life, to the point that paydays were random because if the gangs knew when employees received their salaries they could plan when to assault the buses taking the workers home. As a result, in El Salvador some workers actually do not know if they will be paid today, this week, or next. Imagine trying to motivate your workforce under those conditions. That's why when we looked for ways to stimulate the Salvadoran economy as part of the Partnership for Growth (PFG) -- our cooperation agreement with the Government of El Salvador that I was fortunate to help negotiate -- the first item we looked to improve was the rule of law. Today much of the emphasis of the PFG in El Salvador is on strengthening justice sector institutions, improving criminal procedures and strengthening the civil service, including the courts.

The PFG was just one of the ways that the Obama Administration tried to help willing Latin American governments improve the rule of law during my time in Washington. Other parts of the U.S. government also worked to do the same. One of the principal requirements for Millennium Challenge Corporation grants, for example, is that countries commit to minimum rule of law standards. USAID has also supported legal reforms programs throughout the hemisphere for many years, including most recently in Mexico, Colombia and Central America.

At the end of the 1980's, as the Central American conflicts subsided, our funding at the ABA was cut just as we finished putting together draft labor and commercial arbitration laws for the region. But our efforts were not for naught. Recently, my old colleagues at the ABA, now called the Rule of Law Initiative ("ROLI"), have held several workshops in Mexico in the new "accusatorial" style justice system, modeled in part after the American system, which will be implemented throughout Mexico by 2016. They have also hosted workshops on criminal investigation and crime scene processing in Central America. I am proud of the work of the ABA for the last three decades, and hope that this time the funding will continue. It may not be flashy, headline-grabbing work, but it remains essential if we are to support our Latin American partners as they seek to improve the rule of law.

But the U.S.'s efforts to help Latin American countries improve the rule of law should not be confined to technical assistance workshops. The new Model BIT that was finalized in 2011 imposes high level environmental and labor standards on all parties, and requires that the host country generally accord foreign investors the same treatment received by locals. It also includes procedures for investor-State arbitration, a key request from our business community. Washington should continue to press our Latin American neighbors that today are not party to a regional or bilateral trade agreement with the United States -- such as NAFTA, CAFTA-DR and various FTAS and BITs -- to negotiate and sign on to a BIT with the U.S. We should not be deterred in these efforts by Ecuador's and Bolivia's disappointing decisions to terminate our bilateral investment treaties. And when the Trans Pacific Partnership Agreement is finalized, the U.S. should move quickly to bring other like-minded Latin American nations into this trade pact.

At the end of the day, however, the rule of law in Latin America can only be advanced by the Latin Americans themselves. To do so, in addition to dealing with the deficiencies already mentioned, they will have to devote more resources to their judiciary, to their law enforcement capabilities and to providing more economic opportunities for their youth. This will require funding, but -- as I recently argued in the Council of the Americas' *Americas Quarterly* -- today many Latin American nations, especially in the Caribbean and Central America, face unsustainable debt levels and cannot devote more to improving the rule of law. Poor tax administration hampers efforts to finance public investment. While at the State Department, we began a pilot project called "Domestic Finance for Development", or "DF4D", to improve public revenue administration in three Latin American countries. The premise of the project was that the elites and the new middle classes will not pay taxes, and informality will persist, unless taxpayers are convinced that their funds will not be siphoned off to offshore bank accounts and will instead be used, transparently, for agreed public purposes such as improving the rule of law. Whether through DF4D or another mechanism, many Latin American governments will need to allocate more resources to their judicial and law enforcement agencies.

Blessed with a legal system that is admired throughout the hemisphere, the United States can help Latin America improve its rule of law system, not by grafting our legal traditions on to other countries, but by partnering with nations that seek our support to improve their judicial and law enforcement institutions. Doing so will mean not only fairer, more open and more stable neighbors, but also countries that are more attractive to both domestic and foreign investment.

I welcome this Committee's attention to these issues and look forward to your comments and questions.

Thank you.