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A political storm threatens to put the lights out in Guatemala

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LIGHTNING is not supposed to strike twice, but this seems to have happened to Railroad Development Corporation (RDC), the U.S. specialist in railway privatisation. No sooner have RDC and its partners recovered from the shock of being forced out of Estonia as a result of the railway being taken back under state control, than the privatised railway in Guatemala is being forced to close. Although the circumstances are different, in both cases, a change in government, which led to an abrupt change in policy, is the primary cause of putting an end to private rail operation.

In both countries, railway privatisation was initiated by the government. In Estonia, part of the national railway was privatised as a going concern, but in Guatemala rail operations had ceased, requiring a huge effort to get trains running again initially on the eastern part of the network. RDC and its partners bid in good faith for both concessions, and in Guatemala RDC was the only bidder. So it was hardly a case of privatisation being forced on unwilling governments.

RDC was awarded a 50-year concession in 1998 in exchange for maintaining the railway and paying the government 11.25% of revenue. The new concessionaire, Guatemala Railways (FVG), reopened the 322km 914mm-gauge line between Guatemala City and the Caribbean port of Puerto Barrios in 1999, three years after operations had ceased. By 2004, RDC had invested US$15 million in the railway and annual freight traffic had built up to 150,000 tonnes. The next objective was to reopen the railway to the Pacific coast which has greater traffic potential than the eastern section.

“We were on the glide path to self-sufficiency because we had been increasing the quality of the traffic we carry and we had negotiated leases for the use of the right-of-way,” says Mr. Henry Posner III, chairman of RDC. Posner says this was achieved despite FEGUA, the former state railway that owns the infrastructure, failing to meet its own contractual responsibilities. That was until the Guatemalan government declared that the rolling stock element of the concession was against the interests of the state. This was clearly a device to force RDC out of Guatemala, especially as the locomotives and wagons are very old.

“FEGUA is the landlord of the railway,” says Posner. “They are there to make sure we don’t steal anything, but they stole it. We appealed, but they changed the law arguing that the previous government had done a bad deal, so they should take it back. There are two ways to make money: create wealth or steal it.”

The declaration has had a devastating effect on the railway, which already had to contend with squatters on the tracks, and criminals trying to steal the infrastructure. A private utility company has erected electricity transmission lines on the railway, sugar barons have built roads on railway land, and FVG has found it impossible to evict squatters and traders from railway property. Traffic has plummeted forcing FVG to announce that train services will cease on October 1.

Posner believes the government wants to give the railway to its cronies. “Unfortunately, the railway is worth more dead than alive,” he says. “The government is acting on behalf of the Guatemalan private sector to use the right-of-way for other purposes.”

Fortunately for RDC, Guatemala is a member of the Central American Free Trade Agreement (CAFTA), which covers Central America, the United States and the Dominican Republic. CAFTA provides an impartial forum outside Guatemalan law in which to obtain compensation. RDC has filed a claim with the International Centre for the Settlement of Investment Disputes seeking compensation from the Guatemalan government of at least US$65 million. The process could take up to two years, which effectively will put an end to Guatemala’s rail revival.

This is certainly not the outcome hoped for by Posner, who is a railwayman through and through. “Our experience in Guatemala has not shaken our faith in capitalism, but it does question our faith in the rule of law,” he says. “Estonia should have put us off Europe, but we are still looking at opportunities there. Peru is our best operation. We have good relations with the government and strong partners — it is a textbook example of how well it can be done.”

Private companies depend for their success on a fair and just legal system. This means that contracts entered into with one government must be honoured by subsequent governments. If a government changes its policy and wishes to terminate a contract, then there should be fair compensation. Whether or not RDC wins its case against the Guatemalan government, there will be few actual winners. Certainly, the chances of reviving the railway in Guatemala for a second time will be virtually non-existent, and it will make investors more wary, which will be a great shame. **IRJ**