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HANDLING INDICATOR

TO : DEPARTMENT OF STATE

INFO : AmConsuls - PORTO ALEGRE, CURITIBA

FROM : AmEmbassy - RIO DE JANEIRO DATE: April 8, 1966

SUBJECT : Recent Developments on IT&T's Problems in Parana and Rio Grande do Sul.

REF : Embtel 2019  
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1. There is enclosed a memorandum covering several recent conversations with GOB, Parana State and IT&T officials. Also enclosed is a copy of an excellent report prepared by Consul McLain, giving additional details on historical and recent developments. The information is being forwarded as background for the Department in the event IT&T officials from New York wish to discuss their problems with officers of the Department.

2. As the Department will note there are three separate problems any one of which could cause us problems at any time: a) The Rio Grande do Sul Case. Should the State Supreme Court rule that IT&T is to receive Cr\$5.7 billion as final settlement for its properties, which IT&T would in all likelihood refuse as inadequate, we could be confronted, as a minimum, with adverse publicity which would provide additional ammunition to those Brazilians opposed to foreign investment and influence in Brazil; b) The City of Curitiba. Should CTN fail to meet the CONTEL criteria, as outlined in the enclosed memorandum, for financing its expansion program in Curitiba the company may be faced with "expropriation" or purchase proceedings. Should this occur we would be faced with a disagreeable problem since local officials of IT&T have indicated to the reporting officer that the company would only consider the sale of all of its properties in a package deal and this only on an immediate cash in full basis; c) The Parana Long-Distance Problem. Should CTN go ahead with its plan to install additional carrier equipment

- Enclosure: (1)Memorandum of Conversation with GOB, Parana State and IT&T officials.  
 (2)McLain Report.  
 (3)Parana State Telecommunications Law

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in opposition to TELEPAR's contention that the CTN concession has expired, the least we can expect is a legal hassle with likely undesirable publicity.

3. While there are some minor discrepancies between the information contained in the Curitiba memorandum and the Embassy memorandum, the basic fact that IT&T appears to be heading toward real problems in continuing its operations in Paraná is borne out by both memoranda. The President of TELEPAR has made it clear that his ultimate goal is to have TELEPAR control all the telecommunications in the state of Paraná. It would also appear that the Governor of Paraná and the President of CONTEL are to say the least disenchanted with IT&T, which as a consequence can expect little sympathy from them in CTN's struggle to survive and expand.

4. The Embassy will keep the Department informed of any further developments.

For the Chargé d'Affaires a.i:

*Ray H. Crane*

Ray H. Crane

Second Secretary of Embassy

DRAFTING OFFICER:  
R. H. Crane

MEMORANDUM OF CONVERSATION

Participants: Ray H. Crane - TCO  
Sr. Raiz, Paraná Secretary of Public Works  
Sr. Guimaraes - President of TELEPAR  
Sr. Quandt de Oliveira - President of CONTEL  
Mr. M. Wells, of IT&T

Subject: IT&T, Paraná, and Rio Grande do Sul  
Telephone Problems

On February 23 Minister Nei Braga, former Governor of Paraná telephoned the Ambassador's Office to request an appointment on the following day for the Paraná Secretary of Public Works and the President of TELEPAR (Paraná Telecommunications Company). Minister Braga was informed that the Ambassador's schedule would make it difficult for him to make any further appointments prior to his departure for Washington but that someone in the Embassy would receive the Paraná delegation. At the Ambassador's reception that evening the matter was discussed with Minister Braga and it was decided that since the Paraná officials were interested in discussing the telephone problem of Paraná that I should receive them.

The following day I received a telephone call from Mike Wells of IT&T who said he had just received a phone call from Curitiba reporting that the Curitiba Press carried an article stating Ambassador Gordon was going to receive Paraná officials to discuss a loan for the expansion of the State's telephone system. Mr. Wells said he had some information which would be of interest to us and asked whether I could arrange an appointment with Ambassador Gordon prior to his meeting with the Paraná group. When I told Mr. Wells that I would be receiving the Paraná officials, he asked whether he could come and see me immediately. I agreed to receive him.

Mr. Wells stated that TELEPAR had issued tenders for a micro-wave communications system for the Northern and Central part of Paraná. He stated, further, that the cost of the micro-wave system as envisaged by TELEPAR would cost the State about Cr\$13 billion broken down as follows: approximately Cr\$5 billion for imported equipment, and Cr\$8 billion for the construction of communications centers, administration buildings, etc. He added that CTN had offered to build a micro-wave network which would be fully financed by CTN. The cost of the CTN project would amount to

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only Cr\$4 billion. Mr. Wells commented, however, that one of the conditions of his Company's proposal was that TELEPAR would not also try to build a competitive communications system. ^

Mr. Wells stated there was a local problem which he feared could cause unfavorable publicity. This local matter concerns TELEPAR's contention that a State Law overrides the Federal Telecommunications Code and grants TELEPAR a monopoly on the long distance communications system and at the same time terminates CTN's concession. CTN's position is that the Federal Telecommunications Code permits State or municipal entities to construct and operate telecommunications system but does not terminate existing concessions.

On the afternoon of February 24 Sr. Raiz, Paraná Secretary of Public Works and Sr. Junot Guimaraes, President of TELEPAR called on me at the Embassy. They stated they were seeking an AID loan of Cr\$3 billion to provide assistance in their proposed micro-wave communications system. They stated that bids had been let for the equipment required for the system and proposals had been received from several European companies. One of the conditions of the tender was that the imported equipment would be financed by the supplier, with a two-year grace period and the remainder to be spread over a five-year period. They believed TELEPAR would have no problem in meeting payments for the equipment after the two-year grace period. With regard to the Cr\$8 billion required for local construction, the State has about Cr\$5 billion available but needs an additional Cr\$3 billion before it can go ahead with its project. I advised the Paraná officials that while I could not speak officially for AID, it would seem to me their request for a loan for all local cost financing might be difficult. I also suggested that perhaps a more appropriate source for financing for a local cost project might be the BNDE. However, I had no way of knowing what priority might be given to their project by the Ministry of Planning and/or the BNDE.

I commented that I had heard that CTN was interested in expanding their existing communications system in the Northern part of Paraná through adding carrier equipment to existing telephone lines and also by setting up a micro-wave communications system. I suggested it might be more useful if the State Government were to use its limited funds to expand the communications system in the Southern part of the State where virtually nothing exists at the present and permit CTN to go ahead with its plans to expand in the Northern part of the State. Sr. Guimaraes replied that this was impossible since the CTN concession expired April 15, 1965 and the State Government had no intention of

permitting the company to install new equipment. Sr. Guimaraes further commented that he expects a serious conflict to arise between the State Government and CTN because he has issued, or plans to issue shortly, instructions which will prohibit CTN from installing the additional carrier equipment on its existing long distance telephone lines.

I pointed out to Sr. Guimaraes and Sr. Raiz that it seemed to me in view of the urgent need of communications throughout the State of Paraná it would be in the best interest of the State to find some way in which the CTN and TELEPAR could work together. I asked if this were not possible. Sr. Guimaraes replied emphatically that so far as he is concerned it will not be possible for CTN to continue to operate long distance communications systems in the State of Paraná. I then asked Sr. Guimaraes "if this is the case then what is the future for CTN in Paraná and how could a conflict which would result in adverse publicity be avoided?" After a moment's reflection, Sr. Guimaraes replied that perhaps the answer would be to reconsider the State of Paraná's offer to purchase the entire CTN holdings in the State of Paraná.

On Monday, February 28 Mr. Wells telephoned to say he had received a report from Curitiba to the effect that the Paraná officials upon their return to Curitiba had told the Press that the State was seeking an AID loan to purchase CTN. Mr. Wells asked whether there was any foundation to this report. I informed Mr. Wells of the mention of the subject but also informed him that at no time during my conversation with the Paraná officials was the question of an AID loan for the purchase of CTN properties discussed.

Later on the same day Forest Farmer telephoned to say he was concerned about reports that the US Government, either through AID or the IDB, was considering financing telecommunications projects in Brazil. He said he was aware of a letter from the IDB to Brazilian government officials indicating that the Bank was interested in financing telephone expansion projects. He commented that he felt the United States Government was making a serious error and could not justify using public funds whether it be for telephones or the satellite communications system when private financing - (for private read IT&T) - is being offered to the Brazilian Government.

On March 4, Secretary of Public Works Raiz telephoned to request an appointment to discuss possible AID financing for Paraná's telephone system. An appointment was made for 4:30 p.m. with Economic Counsellor Elwood and a representative from AID/ENRO was invited to attend the meeting. Sr. Raiz did not show up for the appointment, but telephoned at 5:30 p.m. to say he was returning to Paraná that evening and would be unable to come to the Embassy. He then said the purpose of his

intended visit was to ask whether AID would be prepared to make a loan to the State of Paraná to be used to purchase all of the CTN properties in the State. I informed Raiz that, while I could not speak officially for AID, I saw no possibility of a loan being made for the purpose he described. Raiz responded that he had been informed the United States had provided the funds for the purchase of the CTB and AMFORP and wondered why the same could not be done for the State of Paraná. I made it clear to Raiz that the United States Government had provided no funds for either of the foregoing deals nor would we be inclined to do so for future deals of this kind.

On March 4 Sr. Quandt de Oliveira, President of the National Telecommunications Council (CONTEL) asked me if I would come to his office to discuss a matter which he thought would be of interest to the Embassy. During the course of our conversation, Sr. Quandt de Oliveira stated he was concerned about the attitude of IT&T officials, both local and from the New York office. He said he was particularly concerned about the failure to reach an official settlement of the Rio Grande do Sul expropriation case. Sr. Quandt de Oliveira said the Government of Brazil is anxious to settle the matter so the State can move ahead with the expansion of the telephone system in Porto Alegre and other areas of the State. He said that in December 1965, he met with Mr. Harkins of the New York office of IT&T and local IT&T officers to discuss specific terms on which the case could be settled. At that time he proposed the case should be settled along the lines of the interim agreement reached in 1964. According to Quandt de Oliveira, the IT&T officials said they could, under no circumstances, accept payment on those terms because it did not represent the present value of the properties nor did it compensate for the loss on the investment during the period they had not had the use of the company's facilities. They also said that in any case, IT&T was not bound by the interim agreement since that agreement was reached between the Governments of Brazil and the United States and not by the company. Quandt de Oliveira said he informed the IT&T officials that he felt settlement should be based on the interim agreement but he would be prepared to consider a reasonable counter-proposal from IT&T. As of this date, Quandt de Oliveira has heard no further word from IT&T on the Rio Grande do Sul case.

In discussing the problems of IT&T in the State of Paraná, Quandt de Oliveira said he would, of course, comply with Brazilian Law, in dealing with IT&T but as a personal matter, he could not be very sympathetic with IT&T's problems owing to their attitude in the Rio Grande do Sul case, the unacceptable proposal they had made for the city of Curitiba, and the attitude they had assumed with respect to TELEPAR. In commenting on the city of Curitiba, Quandt de Oliveira said that CTN -- a subsidiary of IT&T --, had presented an expansion plan for the city but the plan had been disapproved by CONTEL. He

said the plan provided that each new telephone subscriber would pay approximately one million cruzeiros for a telephone but would receive nothing in return except telephone service for which they would pay the same as other subscribers. He said he saw no reason why private individuals should finance the expanded telephone system and receive nothing in return, while at the same time IT&T would invest nothing and expect, under the terms of its concession, to receive a 12% return on the subscriber's money. In this connection, he said that CONTEL has adopted a firm policy with regard to telephone expansion by private or public companies. The policy is that, preferably expansion projects should be self-financed. If this is not possible and the operating company seeks financing from its subscribers, then the subscriber should receive either bonds or stock shares in the company in an amount equal to what he invests for his telephone. If neither of the foregoing plans are possible, then the Government will have no choice but to expropriate the companies and assume the responsibility of expanding the telephone systems. Sr. Quandt de Oliveira hastened to explain that when he used the word "expropriate" he meant that the companies should be given just compensation for their properties.

In discussing the long distance line problem mentioned above, Sr. Quandt Oliveira said he was not in a position to state whether or not TELEPAR was legally correct in claiming that the Paraná State Law (a copy of the Law is attached) did in fact terminate IT&T's concession. He indicated this would probably be a matter which would have to be settled in the Brazilian Courts. He commented that he sympathizes with TELPAR's position that if it is to develop a state-wide communications system it must have the Central and Northern part of the State under its control since this is the most lucrative part of the State's system and the profits could be used to construct new lines and expand existing lines in the Southern and Western part of the State. He also commented that TELEPAR had presented a communications plan for the State of Paraná which has been approved by CONTEL and which has already had radio frequencies assigned to it. CTN has not yet submitted a formal micro-wave project but according to Quandt de Oliveira he has seen a preliminary plan of their project which he said he would not be able to approve since it does not correspond with the national telecommunication plan. He also commented that according to his information, IT&T's offer to build a micro-wave communications system in Northern Paraná came only after TELEPAR had issued tenders for the system and had practically signed the final papers with European suppliers. He added that it seemed to him there was a real question as to whether or not IT&T acted in good faith in making its proposal or whether it was merely an effort to obstruct TELEPAR's plans and force them to accept the IT&T proposal.

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SUBJECT: CTN Negotiations on Curitiba and State Interurban Service at Impasse.

REF: Consulate OMs dated September 16, and November 16, 1965  
Embtel 57, March 11, 1966.

1. Relations of the CTN (ITT owned and operated telephone company) with the City of Curitiba and with the state of Parana appear to be worsening. A CTN proposal to add 30,000 telephones to its Curitiba franchise probably will come to naught due to the inability of the CTN and a special city negotiating committee to agree. A CTN proposal to install an interurban state-wide microwave telephone system has been unofficially but firmly rejected by Governor Paulo Pimentel. Implicit in these developments is the determination of state officials to install and operate their own long distance telephone service and (perhaps) a growing tendency to make the CTN's position in Curitiba uncomfortable enough to pave the way for a cut-rate state takeover of the city telephone service.

2. The CTN positions vis à vis the city of Curitiba and the state of Parana are complex. Although these positions are interrelated, for the sake of clarity, they are best considered separately.

The CTN in Curitiba

3. As indicated in the reference OMs, by last November the city of Curitiba and the CTN seemed near an admittedly complicated subscriber financing agreement whereby the city and the CTN would jointly add 30,000 telephone lines to Curitiba's present 10,000 line system. By last December the special committee representing the city had removed what was apparently the last obstacle to an expansion agreement by accepting the CTN's Cr\$ 8 billion evaluation of its Curitiba holdings as a basis for rate structuring. Recently, however, the special committee has fallen under the control of (retired) General Junõt Rebelo Giumarães who, as head of TELEPAR, the Parana telecommunications company, has always doggedly opposed any expansion by the CTN that would not vest title to new equipment in TELEPAR. (Gen. Junõt, whose mild appearance and air of reasonableness is quite

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deceiving, also is Governor Pimentel's newly appointed Secretary of Public Security.) While Gen. Junot has told us that agreement with the CTN on expansion in Curitiba is close, in reality he is imposing conditions and making statements elsewhere that indicate either a complete ignorance of the CTN's position, or a determination to make the CTN's position in Curitiba untenable. He has asked that the CTN give up its exclusive concession in Curitiba which runs to 1980, rejected as too high the CTN's proposal to operate the new telephones installed for TELEPAR for a 6 percent (of rates) fee, and has insisted that any operating agreement made between the city and CTN be limited to five years instead of until the termination of the CTN Curitiba concession in 1980. Gen. Junot has reportedly said that if the CTN will not accept his conditions, he (TELEPAR) would cancel the CTN Curitiba concession and build and operate his own city telephone company independent of CTN facilities. (This, of course, is completely unrealistic, but it does indicate the depth of Gen. Junot's feelings on the subject.) <sup>1</sup>

4. The Consulate has no information indicating that CONTEL has rejected the subscriber financing scheme or that CTN was unwilling to issue bonds to the subscribers as indicated in the reference telegram. While cancellation has been mentioned here, the term "expropriation" has yet to be heard.

5. Last year the CTN (as it is entitled to do under terms of its concession) requested CONTEL permission to increase rates to reflect a 12 percent return on the net worth of its Curitiba operation evaluated then at Cr\$ 5 billion. CONTEL conceded only one half the requested increase, at least partly because of pressure from Curitiba and Parana officials. Presently before CONTEL is a CTN request for another increase based on a net worth figure of Cr\$ 8 billion. We understand that Curitiba Mayor Ivo Arzua has requested that CONTEL refuse the rate increase until CTN

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- (1.) In spite of his opposition to CTN (and, thus, ITT) Gen. Junot plans to install ITT Standard equipment in Curitiba since "the company prices are limited by price control agreements."

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accepts the city's conditions regarding the expansion of service (see above and reference OMs). On March 14, the CTN, after a monetary correction required by CONTEL (for income tax purposes) amended its pending rate increase request to base it on a net worth figure of Cr\$ 10.342 billion.<sup>2</sup> This latest CTN request will almost certainly increase the difficulty of a city/CTN agreement for expanded service.

6. Robert Grubhoffer, director of the CTN here, has long felt and still feels that even if agreement can be reached for expansion of service in Curitiba along lines reported in the reference OMs, the difficulties of a CTN operation of TELEPAR telephones and lines will create a politically and administratively impossible situation. He opposed the ITT decision to negotiate on this basis and sees the sale of the CTN to a Brazilian entity as the only means of expanding service in Curitiba under existing circumstances.

7. In 1964, when negotiations for a state purchase of all CTN properties collapsed,<sup>3</sup> then-Governor Ney Braga shelved an unratified agreement extending the CTN's state interurban franchise from 1965 to 1986 and the Parana Legislative Assembly passed a bill assigning this franchise to TELEPAR. (The CTN is, by terms of its expired interurban franchises, allowed to continue to operate its existing interurban facilities.)

8. Since then TELEPAR, headed by the ubiquitous Gen. Junot, has installed a few interurban lines, gathered capital, and prepared ambitious plans for the installation of a Cr\$ 10 billion (the CTN thinks it will cost Cr\$ 14 billion) 360 channel microwave interurban network. According to Gen. Junot, TELEPAR has arranged the financing for this project and expects it to pay for itself completely in a maximum of three years after installation.

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- (2) The CTN adjusted its declared statewide capital investment figure from Cr\$ 750 million to Cr\$ 16.125 billion and its statewide net worth evaluation from Cr\$ 15 to Cr\$ 22 billion.
  - (3) The state would not accept ITT terms for payment in 5 instead of 14 years, for a Bank of Brazil guarantee instead of one from the state bank, and for delivery of control of the company only upon receipt of the final payment.

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9. That this optimistic estimate of the profit potential of interurban service may be reasonably accurate is suggested by a recent ITT proposal to the State Government to install (using a FINAME loan) a Cr\$ 12 billion 120 channel interurban network. This has been rejected in favor of TELEPAR unofficially but firmly by Governor Pimentel. Pimentel reflects the general sentiment here that ITT's proposal, after years of inaction, comes too late, is inspired by selfish motives, and was forthcoming only after it became evident that TELEPAR was a real threat to the CTN's operations.

10. A serious problem has been created by the CTN's recent addition of five new lines to its interurban service between Curitiba and Cambará and its apparent determination to increase service on existing facilities elsewhere. As the CTN interprets its legal position, it can improve its existing facilities even though it has lost its franchise to initiate new interurban service. (It may be that the CTN will claim it has not lost its franchise.) Although Grubhoffer says that Gen. Junot told him he did not object to improvement of the CTN's existing interurban service, the general has indicated absolutely the contrary to the Consulate. According to Gen. Junot, the CTN's installation of the new lines is a flagrant defiance of state and federal laws and regulations that cannot and will not be tolerated. (He claims an ITT attorney told him "the ITT does not recognize the state law granting the interurban franchise to TELEPAR." Gen. Junot has said that an American company might be able to get away with this in Central America but that "this is Brazil which will defend its sovereignty.") In spite of Gen. Junot's pious declaration that he wishes at all costs to avoid a newspaper "polemic" he seems utterly determined to check any type of CTN interurban expansion by any means. We have the impression that he would welcome a public uproar, exploit the national sovereignty issue to the hilt, and is unimpressed by the CTN's opinion that the public will support the CTN against TELEPAR because of the new service offered.

11. COMMENT: We understand that Governor Pimentel has no present interest in renewing negotiations for a state purchase of CTN's Parana properties unless some sort of soft loan from sources outside the state can be arranged. He has apparently decided to back TELEPAR's interurban telephone service plan with all state money available for telecommunications and attempt to resolve the Curitiba expansion problem

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in another way. Thus, politically, financially and emotionally Pimentel is committed to a TELEPAR owned and operated interurban service and the CTN can expect determined opposition to any plans it may have to expand its interurban activities in any way. The CTN's belated attempts to increase interurban service here will be almost universally regarded as either tokenism or effrontery and will only further damage the company's badly tarnished local reputation.

12. The telephone situation in Curitiba may not be beyond recovery. Much depends on Pimentel's relations with Gen. Junot of whom he, Pimentel, has jocularly complained "I always have to hold him by the coattails to keep him from going too far." Gen. Junot, by virtue of his technical knowledge of telecommunications has made himself indispensable to both the city and the state in any negotiations with the CTN. Nevertheless, Pimentel will definitely make the final decisions. He has told us he is willing to risk public disapproval if a reasonable deal can be made with the CTN to expand service in the capital. It is difficult to imagine Pimentel expropriating the CTN or even threatening to do so. He might, of course, view with complacency a similar move by either federal or municipal authorities, particularly if the situation in Curitiba remains deadlocked or if he is badly handled (read threatened or pressured by negotiators).

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