# FTAA's Transition Period:

# An Unexpected Source of Disparity?

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## *Introduction*

One of the most sensitive issues confronting Latin American and Caribbean (LAC) countries in the creation of the Free Trade Area of the Americas (FTAA) is how the agreement will affect the economic disparities of the Western Hemisphere. Many authors and policy makers argue that FTAA represents an opportunity for the LAC development aspirations. The most referred regional objectives in the FTAA are, to improve the attractiveness for foreign investment; stimulate the transfer of technology; accelerate the process of industrial specialization, and above all, to get free access to the United States market. The present chapter analyses the possibilities of satisfaction of the last objective taking as indicators the emerging characteristics of the FTAA transition period. Its purpose is to introduce the FTAA debate in the context of the heterogeneous and ambiguous process called "trade liberalization", and to point out its implications for less-developed LAC countries. The first section provides a conceptual discussion on the liberalization policy, including an overview of the contributions made to assert FTAA consequences for the small economies. The second section places the tariff barrier liberalization in a broader context, which calls for a comparative analysis with the other components of the

hemispheric project. Based on the finding that several non-tariff barriers used by the United States are likely to remain in force at least during the FTAA transition period, the third section draws on the significations of an uneven liberalization process for LAC countries. In its ensemble, this chapter seeks to substantiate the idea that the complexities of the disciplines involved could serve as a source of unequal distribution of trade benefits within the Western Hemisphere.

## *The current view of the FTAA liberalization process*

The FTAA negotiations have produced an impressive amount of literature linking the project to national, industrial, and social issues. The most influential models seeking to identify the benefits of free trade for less developed countries, usually match one or another of the following conclusions: Free trade will have positive effects for big, medium, and small economies; and FTAA will cause dissimilar consequences depending on each country's degree of preparation. The first conclusion substantiates the classic small-country assumption, i.e. free trade reduces the costs of transaction, stimulates the consumer's acquisitive capacity, increases the opportunities for scale industries, and generates new employments. Therefore, the FTAA is equally advantageous for all countries despite their economic size. This approach is shared by Hufbauer and Schott (1994), who compare FTAA and non-FTAA scenarios, and predict (in the former case) a general 1.5 percent increment in GDP annual rate (273 billion dollars; 525 dollars per capita). Similar conclusions are supported by Salazar and Segura (1994) regarding the

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impact of the continental agreement on Costa Rica, and by Hinojosa, Lewis and Robinson (1996) for the United States, Argentina, Brazil, Chile, and Mexico.

The structuralism usually criticizes this argument for its dependence upon simplistic assumptions such as, full employment, non-restricted mobility of factors across the sectors, and perfect competition. Singer (1995) explains that several variables could reduce free trade benefits or even cause harmful effects on less developed economies: substantial disparities in infrastructure; difficulties in accessing special services and export markets; scarce capital markets, and minor organizational capacities. Within this paradigm, Escaith and Pérez (1999) develop a mixed forecasting depending on the level of preparation. The variables considered in this study (macroeconomic and microeconomic eligibility; structural preparation in terms of export diversification, human resources and infrastructure, and public policy adequacy in macroeconomics, trade and productive transformation), indicate that the degree of preparation of the small countries doesn't differ from the capacity of the big or medium countries, although the first ones show higher commercial and macroeconomic vulnerability.

Even though these conclusions result from careful research, seemingly they fall short to define free trade as zero protection level, i.e. non-restrictive circulation of merchandises within the Western Hemisphere. By suggesting this connotation, they overlook both, the ambiguity that characterizes any liberalization process, and the implications of the power bargaining in the definition of FTAA risks and opportunities. As practiced today, full free trade does not constitute a workable scenario. Freer trade involves not only a complex tariff negotiation product by product, but also several disciplines, which entail specific approaches to their liberalization. Concretely, the first

ten years of the FTAA are likely to represent an intricate and non-linear process of liberalization, filled with complicate calendars, administrative stress, and heterodox consequences on the associated economies. For the assessment of the latter scenario, I distinguish two components in the liberalization process: the dismantling of tariff barriers, and the less conclusive eradication of non-tariff obstacles to trade. The set of such instruments normally includes standard barriers (tariffs, quantitative restrictions, and quotas); customs technicalities; strict rules of origin; contingent barriers (safeguards, antidumping and compensatory duties); complicate environmental, health or labor regulations; corporate and government protection of national industry; and the barriers to services and labor mobility. Most of them are subject to negotiation within the FTAA; however, as the next pages will show, they do not follow the same path, and represent different challenges across the Hemisphere.

## *Tariff liberalization and starting points*

The starting points in tariff protection in the United States and Latin America are notably dissimilar. The U.S. trade-weighted taxes are one of the lowest of the world: 2.0 percent in 1998 (3.27% in 1992), although it usually applies higher rates to products like concentrated orange juice (30%), rubber footwear (20%), suitcases (17%), and woman's wallets (14%) (Hufbauer and Elliot, 1994). Among the 125 LAC products exported to the United States, only 18.4 percent are always subject to tariffs; 30.4 percent are fully exempt, 18.4 percent benefit of the preferential treatment accorded to the Caribbean, Central American and Andean countries, and the remaining 32.8 percent enjoy from one or another preferential program (SELA, 1998). As an outcome, the percentage subject to

tariff represents an even smaller part of the average duty rate of all imports from the region: 1.1 percent in 1998 (ECLAC, 1999).[2]

Tariff dismantling in Latin American builds a different case. The liberalization within the region and with third countries, spine of the economic restructuring in the late 1980', began in the form of trade unilateral liberalization. In 1985, the tariff average corresponding to South America and Central America was 58.5 percent, with 80 percent covering of non-tariff barriers. The average diminishes to 28.7 percent in 1988, and to 12.2 percent in 1999, higher in some countries like Brazil, Argentina, and Peru (ECLAC, 2001a: 113).[3]

[2] The average duty rate expresses the share of total duties collected over the amount of the imports subject to taxation. For Central American exports, the average is substantially high, 16.2%, due to a large extent to the taxes applied to textiles (ECLAC, 1999).

[3] The tariff decrease is not a uniform process during the period. After the Mexican financial crisis, in May of 1995, Costa Rica increased its duties from 5 to 13 percent for non-refined products, and from 20 to 28 percent for finite products. Guatemala registered in the same period a marked tariff uncertainty with political background. Honduras and Nicaragua, finally, declared once again their inability of putting into practice the common external tariff decided by the Central American Tariff Council.

**Table 1**

**Total Tariff Revenues in Less Developed FTAA Countries (As percentage of GDP)**

| | 1990 | 1991 | 1992 | 1993 | 1994 | 1995 | 1996 | 1997 | 1998 | 1999 |
|---|---|---|---|---|---|---|---|---|---|---|
| **Latin America** | | | | | | | | | | |
| Argentina | 12.4 | 14.2 | 16.5 | 17.9 | 17.7 | 17.3 | 16.0 | 17.3 | 17.6 | 17.6 |
| Bolivia | 8.2 | 8.7 | 10.7 | 11.4 | 12.4 | 12.4 | 12.3 | 14.5 | 16.3 | 18.1 |
| Brazil | 10.2 | 10.0 | 9.4 | 10.6 | 13.2 | 12.6 | 11.8 | 12.6 | 14.5 | 15.0 |
| Chile | 14.5 | 16.7 | 17.3 | 18.0 | 17.5 | 17.0 | 18.2 | 17.6 | 17.8 | 16.9 |
| Colombia | 9.3 | 10.7 | 11.2 | 11.6 | 11.8 | 11.4 | 11.5 | 12.2 | 10.5 | 10.8 |
| Costa Rica | 14.0 | 11.4 | 12.0 | 12.1 | 11.7 | 12.5 | 12.7 | 12.6 | 12.8 | 12.5 |
| Dominican Republic | 10.5 | 11.8 | 13.8 | 14.8 | 14.0 | 13.8 | 13.1 | 14.7 | 15.0 | 14.4 |
| Ecuador | 7.6 | 7.6 | 7.2 | 7.4 | 7.7 | 8.0 | 7.2 | 9.3 | 9.9 | 9.8 |
| El Salvador | 9.1 | 9.5 | 9.6 | 10.3 | 10.9 | 12.0 | 11.3 | 11.1 | 10.3 | 10.5 |
| Guatemala | 6.8 | 7.3 | 8.2 | 7.8 | 6.7 | 8.0 | 8.8 | 9.4 | 9.6 | 10.0 |
| Haiti | 8.7 | 9.5 | 6.1 | 5.5 | 2.6 | 6.4 | 7.5 | 9.2 | 8.9 | 9.1 |
| Honduras | 14.1 | 14.5 | 15.4 | 14.8 | 14.3 | 15.7 | 14.4 | 14.1 | 17.0 | 17.7 |
| Mexico | 11.5 | 12.0 | 12.4 | 11.4 | 11.3 | 9.2 | 9.0 | 9.8 | 10.5 | 11.2 |
| Nicaragua | 13.5 | 17.7 | 19.2 | 18.7 | 19.3 | 20.6 | 20.7 | 23.0 | 24.1 | 23.0 |
| Panama | 11.7 | 12.5 | 12.5 | 12.1 | 11.8 | 12.5 | 12.1 | 12.5 | 12.1 | 12.6 |
| Paraguay | 9.5 | 9.4 | 9.3 | 9.4 | 10.7 | 12.2 | 11.5 | 11.8 | 11.6 | 10.8 |
| Peru | 7.7 | 8.9 | 10.0 | 10.1 | 11.2 | 11.6 | 12.1 | 12.1 | 12.1 | 11.4 |
| Uruguay | 14.4 | 14.3 | 14.9 | 14.7 | 13.1 | 14.6 | 14.9 | 15.8 | 16.1 | 15.4 |
| Venezuela | 3.7 | 4.4 | 5.5 | 7.2 | 8.7 | 8.2 | 7.9 | 9.8 | 10.3 | 10.3 |
| Latin America (average) | 10.39 | 11.11 | 10.85 | 11.88 | 11.93 | 12.42 | 12.26 | 13.13 | 13.48 | 13.53 |
| **Other Western Hemisphere Countries** | | | | | | | | | | |
| Antigua & Barbuda | 17.3 | 17.0 | 17.1 | 17.1 | 17.5 | 17.8 | 18.5 | 17.9 | 17.5 | - |
| Aruba | 16.6 | 18.2 | 18.5 | 19.4 | 18.5 | 18.2 | 17.9 | 16.9 | 17.4 | - |

| | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| Bahamas | 14.2 | 14.3 | 15.3 | 14.7 | 16.5 | 16.7 | 16.5 | 16.7 | 16.5 | - |
| Barbados | 25.3 | 26.9 | 26.0 | 27.9 | 27.0 | 27.8 | 27.7 | 30.7 | 30.0 | - |
| Belize | 21.5 | 21.8 | 20.8 | 20.9 | 20.6 | 20.6 | 19.4 | 19.8 | 19.3 | - |
| Dominica | 24.7 | 24.3 | 24.5 | 23.2 | 22.0 | 23.3 | 23.5 | 23.4 | 23.8 | - |
| Grenada | 21.9 | 21.5 | 21.9 | 23.1 | 21.8 | 22.6 | 22.7 | 21.9 | 22.2 | - |
| Guyana | 28.8 | 25.7 | 35.9 | 35.7 | 29.8 | 31.4 | 32.3 | 29.6 | 28.6 | - |
| Jamaica | 23.8 | 22.9 | 22.7 | 25.4 | 24.9 | 26.1 | 24.8 | 24.5 | 26.3 | - |
| Netherlands Antilles | 6.5 | 6.8 | 7.0 | 7.6 | 7.8 | 7.6 | 8.6 | 10.1 | 10.3 | - |
| St. Kitts & Nevis | 19.9 | 19.3 | 19.5 | 21.2 | 21.1 | 21.3 | 21.5 | 22.2 | 22.7 | - |
| St. Lucia | 22.3 | 23.0 | 23.3 | 23.0 | 22.2 | 21.8 | 21.4 | 21.6 | 22.0 | - |
| St. Vincent & G. | 25.3 | 24.1 | 22.5 | 22.8 | 23.9 | 23.2 | 24.3 | 24.3 | 24.6 | - |
| Trinidad & Tobago | 24.6 | 27.5 | 24.6 | 25.7 | 17.6 | 17.5 | 17.7 | 18.4 | 21.2 | - |
| Non LA (average) | 19.83 | 20.95 | 21.40 | 21.98 | 20.80 | 21.13 | 21.20 | 21.28 | 21.60 | |

Source: Escaith and Inoue (2001).

The central issue of this difference with the U.S. tariff structures is that the LAC economies are often fiscally dependent upon tax revenues. As Table 1 shows, tariff income represented in 1999 more than 13 percent of Latin American and the Caribbean GDP. Historical data of its share in total GDP demonstrates that it has become an element of growing importance: Between 1990 and 1999, it raised in Latin America from 10.39 percent to 13.53 percent, and in the Caribbean from 19.83 to 21.6 percent. In addition, among the 16 countries highly dependent on these revenues, except Dominican Republic, all show trade deficit. Venezuela, together with four Caribbean countries (Netherlands Antilles, St. Kitts & Nevis, St. Lucia, St. Vincent & Grenadines) register moderate deficits, while the rest of the economies are exposed to a large deficit: Antigua &

Barbuda, Bahamas, Belize, Colombia, Dominica, Grenada, Haiti, Honduras, Jamaica, and Nicaragua (Escaith and Inoue, 2001).[4]

It is true that the estimates of the tariff importance for Latin American and the Caribbean presented above cover only a part of the tariff liberalization issue. Another important aspect is the relation between the optimun degree of tariff protection, and the effect of the indiscriminate liberalization proposed by the FTAA. A further topic is the heretogeneity of tariff structures, with products like capital goods, which enter LAC markets with zero or low rate taxes. Nevertheless, it is unambiguous that the tariff dismantling will demand to Latin America and the Caribbean economies a comparative higher effort. It is probable that the stress would be enhanced by the adoption of mechanisms of acceleration similar to the NAFTA's Article 302.3. The U.S. position in this matter has advocated "for rapid reduction of most duties" in the Western Hemisphere, as well as for the elimination of "high proportion of (each country') tariffs

USTR, 2001). If that is the case, FTAA risks to reduce the LAC revenues on external trade without giving them enough time to adjust the efficiency of their fiscal reforms, mainly to substitute direct taxations by indirect ones. Another risk to consider on the part of the small countries (or of precarious industrial integration) would be the fracture of national productive chains, reducing the possibilities of industrial specialization, referred as their principal goal. Under these circumstances, tariff liberalization would represent not only a costly non-reciprocal trade concession, but also a minor contribution to the achievement of LAC objectives within the FTAA. At this point,

[4] The main consideration of deficit is that it reduces national savings, and this decline has a negative effect on the overall economy because it leads to a drop in investment or net exports or a combination of both.

it appears that the satisfaction of the LAC negotiating positions depends on the outcome of the other FTAA components.

## *The issue of no-tariff barriers*

### Antidumping measures

The attention accorded to the antidumping rules in FTAA negotiations reflects the growing importance of this instrument for the international trade. As Bhagwati (1988) noted, the global decrease in tariff duties during the last years is causally linked to the proliferation of antidumping cases. While the world tariff average was 50 percent in 1958, and went downward to only 5 percent in 1988, unfair trade investigations, on the other hand, were implemented in the 1980' in a proportion of twice as much in comparison to the precedent decade. In the Western Hemisphere from 1987 to 2000 were conducted 484 antidumping investigations. United States initiated 147 cases, in particular against Canada, Mexico, Brazil, Argentina and Venezuela, and was responded with other 182 investigations, 73 percent filled by Mexico and Canada. Here it is worth noting that the shift from one to another type of barriers is not the fact of all countries. Although Mexico, Argentina and Brazil have rejoined United States and Canada as leading users of antidumping measures (93% of total FTAA cases), 20 Latin American and Caribbean Countries have never carried out any investigation under trade remedy laws; 17 have yet to be the target of any investigation, and eight LAC countries have used them in seven or less occasions. (See Table 2). This situation leaves NAFTA members, together with Argentine and Brazil, as the sole *connoisseurs* of an important protectionist device. Even if most LAC countries have actualized their trade remedy legislations, the lack of experience, including administration inefficiency, accentuates the vulnerability of the

small economies in front to a trade barrier which has harmful effects whether is justified or not.

Only in 1990, U.S. investigations represented in tariff equivalence, 25 percent of LAC textile, ferrous metals, steel, color television and milky products exports; 30 percent of rice, and 40 percent of sugar and gear (Erzan and Yeats, 1992: 59 and s.). In general, the costs for the targeted countries are higher than the current tariff levels. According to Prusa (1999), when the duties are applied the impact ranges from 50 to 70 percent, and when are turned down the costs fluctuate between 15 and 20 percent.[5] The last figures express perhaps the most pervasive effect of the antidumping measures: the growing uncertainty for LAC exporters. In some cases, taking advantage of the relative ease with which U.S. firms can pursuit unfair trade strategies, they have propitiated favorable arrangements to their interests by filling several petition against the same product: Once the country's legal system is saturated (by the large number of investigations), the foreign company sees itself forced to negotiate with the domestic firm voluntary exports restraints (Finger, 1993: 5). These negotiations constitute a specific treat to the less powerful firms, as 20 to 25 percent of U.S. antidumping petitions filled from 1980 to 1994, resulted in voluntary restraints (Prusa, 1997: 235).[6]

[5] Antidumping investigations have also costly effects on the initiating country. Extensive research carried out by the U.S. Commission of International Trade showed in 1992 that the eventual antidumping and compensatory duty suppression in this country could have increased its trade in 1.6 billion dollars. Morkre and Kelley (1994) support the same conclusion in their analysis of the U.S. antidumping cases during 1980-1988. Dutz (1998) finds Canadian antidumping investigations as diminishing import competition (because of the increase in prices).

[6] U.S. negotiators advocate for preserving the voluntary export restraints in the FTAA "in compliance with the WTO regulations"; that is to say, without significant modifications to the present rules (USTR, 2001).

**Table 2**

**Antidumping Investigations in the Western Hemisphere (1987-200)**

| Country | Initiating | Affected |
|---|---|---|
| Antigua & Barbuda | 0 | 0 |
| Argentina | 61 | 22 |
| Aruba | 0 | 0 |
| Bahamas | 0 | 0 |
| Barbados | 0 | 0 |
| Belize | 0 | 0 |
| Bolivia | 0 | 1 |
| Brazil | 40 | 104 |
| Canada | 84 | 48 |
| Chile | 5 | 16 |
| Colombia | 11 | 11 |
| Costa Rica | 6 | 2 |
| Dominica | 0 | 0 |
| Dominican Republic | 0 | 0 |
| Ecuador | 1 | 4 |
| El Salvador | 0 | 0 |
| Grenada | 0 | 0 |
| Guatemala | 1 | 1 |
| Guyana | 0 | 0 |
| Haiti | 0 | 0 |
| Honduras | 0 | 1 |
| Jamaica | 0 | 0 |
| Mexico | 103 | 54 |
| Netherlands Antilles | 0 | 0 |
| Nicaragua | 2 | 1 |
| Panama | 1 | 0 |
| Paraguay | 0 | 2 |
| Peru | 11 | 2 |
| St. Kitts & Nevis | 0 | 0 |
| St. Lucia | 0 | 0 |
| St. Vincent & G. | 0 | 0 |
| Trinidad & Tobago | 4 | 3 |
| United States | 147 | 182 |
| Uruguay | 0 | 3 |
| Venezuela | 7 | 28 |

*Source*: Tavares *et al*. (2001).

Many authors and LAC policy makers have recommended the change, the amendment or the replacement of trade remedies by other mechanisms. Seemingly, these initiatives will not have significant repercussions. The substitution of antidumping by competition rules in the European Union, and between Australia and New Zealand, began after the tariff liberalization was completed. Under this consideration, the start of the substitution process in the Americas would have to wait until the year 2015. However, this

precondition could prove to be not enough for two reasons. First, the setting in practice of alternative instruments needs supranational institutions (Horlick and Shea, 1997: 276), not mentioned in the Action Plans, or in the draft of the Treaty presented at the Quebec Summit in 2001. Second, United States is "vigorously opposed" to any change or amendment to the antidumping legislation. To make it clear, this country has stated that one of its main goals in the hemispheric negotiations is to preserve the existing rules in the matter. It argues that antidumping and competition rules, "address distinctly different problems", and consequently they are not interchangeable (USTR, 2001). Thus, antidumping regulations can be regarded as another source of administrative stress, as well as a threat to the LAC aspirations in having a free access to the U.S. market.

## Section 301

Another important barrier for the Western Hemisphere is the U.S. Section 301, a form of antidumping reverse, which promotes the opening of foreign markets by means of the threat of retaliation. According to the Trade Act of 1974, the Section 301 authorizes the U.S. Trade Representative to negotiate with other governments the elimination or the reduction of the obstacles to U.S. exports. It applies when a foreign country performs unfair trade practices at the domestic level (or violate or are not consistent with the U.S. trade rights), or is discriminatory to U.S. products by allowing anticompetitive activities. It also applies when the country block trade and investment opportunities for U.S. firms or shows limited compromise in respecting intellectual property rights, trade unions' activities or labor rights. If the nation is found accountable, retaliation measures can adopt the form of suspension or elimination of trade concessions, the application of new duties, or other kind of restrictions (Husted, 1995).

In the 1980', United States processed around 350 cases under the Section 301. Among them, 88 were implemented against LAC countries, often resulting in voluntary export restraints or in higher trade tariffs (ITR, 1994). In this category figures the 1985 reprisal against the Brazilian import license system, which lead to 100 percent tariff increase in Brazil's paper, pharmaceutical and electronic exports (Abreu, 1995: 396). During the 1990', the U.S. sanctions against the Argentinean patent law in pharmaceuticals lead in turn to the annulment of 50 percent of the benefits perceived by this country as part of the Generalized System of Preferences. The costs of this measure were estimated in about 600 million dollars loss in export earnings. Mexico, on the other hand, was the object of 301 actions in three specific areas: the jitomate exports (it did not prosper as a consequence of the non demonstration of the zero year argument); the exports of millet brooms, conflict that generated mutual trade reprisals, and the Mexican policies regarding the imports of high-fructose corn syrup.

The Special 301, an enforcement of the Section 301, allows the identification of those countries that violate or give limited protection to intellectual property rights. This normative registers four levels of concern, which constitute successive steps towards a 301 action. The "Other Observations List" reflects the first and the lowest level of concern. It did not include any LAC country in 1999 (Bolivia demanded unsuccessfully to be incorporated in this status in order to avoid the pressures that characterize the Watch List). The "Watch List" indicates higher concerns for not enforcing against piracy or denying the application of the WTO agreement on trade-related aspects of intellectual property rights (TRIPS). Ten LAC countries were placed under this heading, mainly because they failed to achieve TRIPS compliance. The "Priority Watch List" represents an

even higher level of concern, which implies a constant pressure for assuring the changes recommended by the U.S. authorities. This category includes four countries due to inadequate patent protection in pharmaceuticals. Finally, the "Priority Foreign Country" identifies the nation that must be investigated under Section 301. The last country placed in this category was Paraguay, revoked in 1999 after it committed to strengthen intellectual property rights at its borders, especially with Argentina and Brazil. (See Table 3).

**Table 3**

**Special 301 Review Affecting Latin America**

| | Country | Justification |
|---|---|---|
| Priority Watch List | Argentina | Inadequate patent protection for pharmaceuticals. |
| | Dominican Rep. | Inadequate enforcement against piracy and counterfeiting in pharmaceuticals. Failed to achieve TRIPS compliance. |
| | Guatemala | Neglect the enforcement of intellectual property laws. Failed to achieve TRIPS compliance. |
| | Peru | Neglect the enforcement of intellectual property laws in pharmaceuticals. |
| Watch List | Bolivia | Failed to achieve TRIPS compliance. |
| | Brazil | Failed to achieve TRIPS compliance. |
| | Chile | Failed to achieve TRIPS compliance. |
| | Colombia | Inadequate enforcement against pirate cable television. Failed to achieve TRIPS compliance. |
| | Costa Rica | Inadequate enforcement of copyright law. |
| | Ecuador | Failed to achieve TRIPS compliance. |
| | Jamaica | Did not passed the bilateral agreement on intellectual |

| | | |
|---|---|---|
| | | property with U.S. |
| | Mexico | Partial implementation of the new anti-piracy initiative. |
| | Uruguay | Failed to achieve TRIPS compliance. |
| | Venezuela | Neglect enforcement against piracy in video, satellite signals, among others. |

*Source*: ECLAC, 1999: 17-19.

These lists have given rise to a tense atmosphere in the inter-American relations. Together with the Section 301, and the Super 301 (which mandates the U.S. Trade Representative to identify the most important unfair practices), they constitute in all terms a compelling, and an unacceptable device. However, none of them is likely to be eradicated during the FTAA transition period, given that trade agreements do not pose limits to their use.[7] During the negotiation of the U.S.-Canada Free Trade Agreement (CUFTA), Canada tried in several occasions (and using different approaches) to protect itself from this normative (Winham, 1988: 38; Hart, 1990). Yet, from the entry in force of the agreement until now this country has been the object of three 301 actions regarding the fishing industry, the Canadian conditions of beer import, and the export of wooden beams of coniferous (Husted, 1995: 272 and s.). As mentioned above, Mexico was also the target of 301 actions inside the NAFTA. The immovability of the Section 301 and its developments do not only entail a prolonged instrument of retaliation. Empirical evidence suggests a broader effect that clearly contradicts the FTAA intentions of promoting welfare: 301 actions can stimulate trade deviation in favor of U.S. firms.[8]

[7] For a multi approach review of the Section 301, see Bhagwati and Patrick (1990).

[8] A study carried out by McMillan (1990) on the 301 action undertaken against South Korea in 1985 stresses this consequence: It caused mainly trade deviation in favor of North American firms.

## Rules of origin

In an integration process guided by managerial interests like the FTAA, the adoption of strict rules of origin, i.e. high level of minimum content, or excessive technical complications, is likely to lead to anticompetitive practices (Krueguer, 1993; Ju and Krishna, 1996). NAFTA's automobile and textile rules of origin illustrate the U.S. preferences in content requisites. At the demand of its car makers, the minimum content rose from the CUFTA's 50 percent, to 60 and 62.5 percent of regional content for cars and their components. In the other sensitive industry, textile and apparel, the rule was reinforced to its maximum: from the weave now on. Two reasons, one relying on the rule's classical function, and the other with more subtler objectives, explains this attitude: to avoid the risk of commercial triangulation, and –most important for the LAC perspectives—to hinder the presence of non-hemispheric firms whose inputs come in significant part from outside the area. The protectionist rationale based in technical complexities is difficult to estimate. Although it is relatively easy to identify the rule of a product, its purpose is covered by a logic that often escapes to the direct observation (Palmeter, 1995: 193, 197). The Specific Tariff Shift, for example, the principal method used in establishing the origin of a merchandise, stimulates the multiplication of specific rules, which in turn make possible the adoption of the most influential managerial choices, generally interested in minimizing the firms exposition to open competition. One solution is the simplification of the normative by adopting a uniform methodology. However, as United States "does not advocate using a uniform tariff shift" (USTR, 2001),

it seems that the hemispheric agreement will not avoid the atomization of the originary regime.

A different concern represents the non-accumulation issue. If the FTAA constitutes a single agreement, as stated by the Summits of the Americas, then all products elaborated (in a percentage to be negotiated) in any Western Hemisphere country should qualify as originary, and therefore benefit from the hemispheric preference. This kind of accumulation (i.e. the inputs and the final products fabricated in the region are considered originary) has been until now a common feature for all free trade and integration agreements in Europe, and Latin America. In spite of this, United States has recently addressed the topic in different terms: this country "reserves its position to the issue of permitting 'accumulation' of production across FTAA countries in qualifying for origin" (USTR, 2001). Although this statement might represent a negotiating pressure, it is worth noting that a non-accumulation scenario would involve a drastic modification of the FTAA project. Due to the limited geographic covering of the non-accumulative rules, instead of composing a single agreement, the FTAA would be *de facto* divided in more than 30 different agreements (one for each LAC country with United States). This would oppose the integrated and sophisticated U.S. industries, to the superficial productive chains of every country of the continent.

**Table 4**

**Latin American Exports to the United States (Percentage of total item exported)**

| Item | Mexico | Mercosur[1] | Andean zone[2] | Central America[3] |
|---|---|---|---|---|
| Machinery & Equipment | 91.4 | 20.7 | 20.1 | 44.6 |

| | | | | |
|---|---|---|---|---|
| Textiles | 79.2 | 11.6 | 19.5 | 34.4 |
| Apparel | 96.7 | 17.0 | 56.6 | 71.8 |
| Other manufactured | 87.1 | 21.0 | 32.5 | 37.8 |

*Source*: ECLAC, 2001b (Tables 4.1 to 4.4).

[1] Argentina, Brazil, Paraguay, and Uruguay. [2] Bolivia, Colombia, Ecuador, Peru, and Venezuela. [3] Costa Rica, El Salvador, Guatemala, Honduras, and Nicaragua.

In their ensemble, the FTAA rules of origin represent a key issue for LAC exporters. Except for oil, metal or agricultural products, the rest of LAC exports are extremely sensitive to the U.S. originary regime: machinery and equipment, textile and apparel, and other manufactured goods are sold to the United States in a proportion of 17.6 percent of the total exports from Mercosur, 32.2 percent from the Andean zone, and 41.1 percent from Central America. (See Table 4). Under these conditions, the definition of the rules of origin becomes a fundamental FTAA component able to stimulate or, conversely, to avoid the creation of better conditions for the more developed industries in detriment of the manufactures lacking enough regional transformation. It might also represent a step towards non-competitive distortions (by increasing the costs of inputs that can be bought from outside the region to smaller price), and to a lower attractiveness for extra regional investment, important in sectors like the automobile industry, where Europe and Asia provide 32.4 percent of total foreign direct investment.

## Other non-tariff barriers

According to an ECLAC report, the U.S. obstacles to LAC exports cover an even wider set of non-tariff barriers. Between 1998 and 1999, 15 countervailing duties (normally included as part of the contingent barriers) were applied against different products of

Argentina, Brazil, Chile, Mexico, Peru, and Venezuela. Tariff-Rate Quotas, in turn, were applied to the sugar exports of 23 LAC countries, and to the textile and apparel imports from Central America. During the same period, the phitosanitary and environmental standards sanctioned the Mexican avocado and tuna, the Brazilian fruits and vegetables, the Guatemalan raspberries, and the Venezuelan gasoline. Two controversial barriers, the embargo to the LAC shrimp exports, and the subsidies to the domestic agricultural industry, actually promote unfair competition with the similar industries from most LAC countries (ECLAC, 1999). Like the precedent and at least partially, these barriers might remain in place after 2005, as the United States shows no interest in making important concessions. The last document available of the Office of the Trade Representative addresses the technical barriers liberalization in diffused, but significant terms: "the country is taking a range of options into consideration in determining the best means of achieving the goal of eliminating and preventing unnecessary technical barriers" (USTR, 2001). Obviously, this concern does not embrace the 'necessary' technical obstacles, which U.S. considers as the instruments for "fulfilling legitimate objectives".

## *Towards a fair transition period*

Central to an assessment of the costs and benefits of the transition period is the question of how Latin America and the Caribbean will manage to combine successfully all components of the FTAA process. The sections of this chapter have shown that the tariff liberalization represents a unilateral LAC trade concession, while several non-tariff obstacles used by the U.S. are probably to remain in place. Under these circumstances, the FTAA brings in the risk of generating asymmetrical liberalization tasks with negative impacts on the less developed countries in the Hemisphere. Ironically, the most ill treated

goal seems to be the free access to the U.S. market, the principal rationale of the hemispheric agreements on the part of the LAC countries. Nevertheless, the dialogue on free trade in the FTAA does not necessarily need to be framed in terms of eliminating non-tariff barriers. A possible institutional approach to dealing more efficiently with the fair market access issues, consist of a set of provisions facilitating higher levels of preparation to new forms of trade competition. Adopting a general rule limiting the application of non-tariff barriers, and negotiating the lengthiest possible calendars for standard liberalization, will also help paving the way for a more balanced transition period, including a less biased allocation of the protection costs.

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