

September 2001

# FREE TRADE AREA OF THE AMERICAS

## Negotiators Move Toward Agreement That Will Have Benefits, Costs to U.S. Economy





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**Abbreviations**

CACM	Central American Common Market
CARICOM	Caribbean Community
ECLAC	United Nations Economic Commission for Latin America and the Caribbean
EU	European Union
FDI	foreign direct investment
FTAA	Free Trade Area of the Americas
IDB	Inter-American Development Bank
IPR	intellectual property rights
Mercosur	Common Market of the South
NAFTA	North American Free Trade Agreement
OAS	Organization of American States
SPS	sanitary and phytosanitary measures
TNC	Trade Negotiations Committee
TRIMS	Agreement on Trade-Related Investment Measures
TRIPS	Trade-Related Aspects of Intellectual Property
USTR	U.S. Trade Representative
WIPO	World Intellectual Property Organization
WTO	World Trade Organization



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United States General Accounting Office  
Washington, D.C. 20548

September 7, 2001

The Honorable Charles Grassley  
Ranking Minority Member  
Committee on Finance  
United States Senate

Dear Senator Grassley:

This report responds to your request that we review the negotiations toward a Free Trade Area of the Americas (FTAA) agreement. Specifically, it addresses (1) the progress made to date and the issues that remain on topics relating to negotiating greater market opening among FTAA countries, (2) the progress made and the issues that remain in developing other rules and institutional provisions for an eventual FTAA agreement, (3) the significant crosscutting themes affecting the FTAA negotiations and how have they been addressed to date, and (4) the potential effects of a completed FTAA on U.S. trade and investment with other Western Hemisphere countries.

As agreed, unless you publicly announce its contents earlier, we plan no further distribution of this report until 15 days after its issue date. At that time, we will send copies of this report to the U.S. Trade Representative, the Secretary of State, the Secretary of Agriculture, the Secretary of Commerce, and interested congressional committees. Copies will be made available to others upon request.

If you or your staff have any questions about this report, please contact me on (202) 512-4128. Other GAO contacts and staff acknowledgments are listed in appendix II.

Sincerely yours,

Loren Yager  
Director,  
International Affairs and Trade

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# Executive Summary

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## Purpose

The Free Trade Area of the Americas (FTAA) agreement would eliminate tariffs and create common trade and investment rules among the 34 democratic nations of the Western Hemisphere.<sup>1</sup> When completed, the FTAA agreement will cover about 800 million people, more than \$11 trillion in production, and \$3.4 trillion in world trade. Because of its scope, negotiations toward such an agreement are among the most significant of ongoing regional trade negotiations for the United States, and the Bush administration has made establishing the Free Trade Area of the Americas one of its top trade priorities. We reported in March 2001<sup>2</sup> that the April 2001 Trade Ministerial in Buenos Aires, Argentina, and the Summit of the Americas in Quebec City, Canada, offered an opportunity to inject political will and set an ambitious pace for the current, more difficult phase of the negotiations, when hard bargaining is expected to begin. In May 2001, we testified before the Subcommittee on Trade, House Committee on Ways and Means, that negotiators had succeeded in attaining these goals but that fundamental challenges remain.<sup>3</sup> Among these challenges are bridging differences on a number of complex and controversial topics.

Because of the significance of the Free Trade Area of the Americas initiative, you asked us to report on the current status of negotiations on specific topics and the agreement's potential effect on the United States. In this report, we address (1) the progress made to date and the issues that remain on topics relating to negotiating greater market opening among FTAA countries, (2) the progress made and the issues that remain in developing other rules and institutional provisions for an eventual FTAA agreement, (3) the significant crosscutting themes affecting the FTAA negotiations and how have they been addressed to date, and (4) the potential effects of a completed FTAA on U.S. trade and investment with other Western Hemisphere countries. Our observations are based on our past and ongoing work on the Free Trade Area of the Americas process.

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<sup>1</sup>The 34 countries participating in FTAA negotiations are Antigua and Barbuda, Argentina, the Bahamas, Barbados, Belize, Bolivia, Brazil, Canada, Colombia, Chile, Costa Rica, Dominica, the Dominican Republic, Ecuador, El Salvador, Grenada, Guatemala, Guyana, Haiti, Honduras, Jamaica, Mexico, Nicaragua, Panama, Paraguay, Peru, St. Kitts and Nevis, St. Lucia, St. Vincent and the Grenadines, Suriname, Trinidad and Tobago, the United States, Uruguay, and Venezuela.

<sup>2</sup>See *Free Trade Area of the Americas: Negotiations at Key Juncture on Eve of April Meetings* (GAO-01-552, Mar. 30, 2001).

<sup>3</sup>See *Free Trade Area of the Americas: April 2001 Meetings Set Stage for Hard Bargaining to Begin* (GAO-01-706T, May 8, 2001).

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## Background

Building on a decade of expanding trade and investment ties in the region, the leaders of 34 countries in the Western Hemisphere pledged in December 1994 to form a Free Trade Area of the Americas no later than 2005. At the first Summit of the Americas in December 1994, hemispheric leaders agreed that free trade and increased economic integration of production and consumption are key factors in raising standards of living, improving working conditions, and protecting the environment. The leaders resolved to form an FTAA that would progressively eliminate barriers to trade and investment. The FTAA would involve a diverse set of countries, from some of the wealthiest (the United States and Canada) to some of the poorest (Haiti) and from some of the largest (Brazil) to some of the smallest in the world (St. Kitts and Nevis).

In 1998, the 34 participating countries formally launched negotiations toward the FTAA at the San José Ministerial (Costa Rica) and the Santiago Summit (Chile). The countries agreed on the guiding principles for the negotiations and the mandates for nine negotiating groups: (1) market access; (2) agriculture; (3) services; (4) investment; (5) government procurement; (6) intellectual property rights (IPR); (7) subsidies, antidumping, and countervailing duties, which are measures to counter imports that are sold at below cost or that involve financial benefits from governments; (8) dispute settlement; and (9) competition (antitrust) policy. The countries also formed special committees to address the crosscutting themes of smaller economies, electronic commerce (e-commerce), and the participation of civil society. The completed FTAA agreement will include the following: trade rules, which each negotiating group is currently negotiating; market-opening schedules to be negotiated by five groups; and a general text to cover overarching and institutional issues.

In April 2001, heads of state and government agreed to conclude the FTAA negotiations no later than January 2005 and to seek implementation of the agreement no later than December 2005. The negotiating groups have produced a draft text containing trade rules, among other accomplishments. These drafts compile and consolidate proposals received from FTAA participants. Because these proposals diverge in many ways, hard bargaining will be required to produce consensus on the final FTAA agreement. During the current negotiating phase (May 2001-Oct. 2002), FTAA participants will agree on how to conduct the market-opening negotiations by April 1, 2002, begin these negotiations no later than May 15, 2002, and produce a new version of their text by August 2002. Since the FTAA ground rules call for a “package deal,” and since nothing is final until

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everything has been agreed upon, much can happen between now and the scheduled conclusion of the negotiations.

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## Results in Brief

The five FTAA negotiating groups pursuing liberalization of trade and investment—market access, agriculture, investment, services, and government procurement—have submitted initial proposals and agreed on a date to begin market access negotiations, but the groups face short-term and long-term issues. In the short-term, these groups must resolve a number of practical issues in order to begin negotiations on market access schedules no later than May 15, 2002, and to narrow differences and prepare revised trade rule chapters by August 2002. For example, how countries should identify which service sectors to include in the terms of the agreement must first be resolved before negotiations to liberalize services can begin. Over the long term, these market-opening groups face fundamental questions about how much and how fast to liberalize. For example, some FTAA countries want FTAA agriculture provisions to liberalize trade by reducing or eliminating domestic supports, which are payments provided to farmers that raise or guarantee prices or income. However, the United States wants these measures to be addressed at a multilateral, not regional, level. For tariffs, the questions will be if there are to be product exclusions and how fast to phase-in the elimination of tariffs on covered products, a particularly sensitive topic for certain sectors such as agriculture and apparel that are vulnerable to import competition.

Narrowing outstanding differences may be difficult for the four other negotiating groups, which have made initial proposals on rules governing intellectual property; subsidies, antidumping, and countervailing duties; competition policy; and dispute settlement. Some groups face fundamental differences. For example, proposals for antidumping vary widely, ranging from maintaining the current World Trade Organization (WTO) rules as preferred by the United States, to eliminating antidumping measures once free trade is achieved. Other negotiating groups have reached agreement on basic principles but disagree on key details. For example, there appears to be wide agreement about the key steps in the FTAA dispute settlement process, but differences remain regarding how to handle compliance and whether to allow appeals.

Two of the three crosscutting themes—smaller economies and civil society—have proven controversial. Because the FTAA's smaller economies are concerned over their capacity to implement such a vast agreement and its potential economic effects on their countries, they have been seeking assurances of technical assistance and other special treatment. The FTAA ministers have agreed to address these concerns but not how they will do so. The second controversial theme concerns civil society. The FTAA process has been viewed as not sufficiently open to the public, and past efforts to include nongovernmental interests, such as business, labor, the environment, and academia, have been widely seen as ineffective. Some steps have been taken to address these concerns, and other steps are being considered. For example, in July 2001 the draft FTAA text was made publicly available.<sup>4</sup>

As a comprehensive agreement, the FTAA could have wide-ranging effects on U.S. trade and investment with other Western Hemisphere countries. The elimination of tariff and nontariff barriers would improve U.S. market access; put U.S. exporters on an equal footing with competitors in FTAA markets; and expand trade, particularly in highly protected sectors such as agriculture. As the world's largest exporter of services; largest source of direct investment; and a major creator of software, pharmaceuticals, and other knowledge-based industries; the United States could benefit substantially from commitments from other FTAA countries to liberalize services and strengthen protection of investment and IPR. On the other hand, certain protected U.S. sectors, including textiles, apparel, and agricultural goods such as sugar and citrus, may face increased import competition and declining production if barriers were lowered.

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## GAO's Analysis

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### Negotiators Are Set to Begin Market-opening Negotiations

Five FTAA negotiating groups are market-opening groups established to develop schedules for reducing tariff, nontariff, and other barriers to trade and to draft chapters outlining associated trade rules. To date, each of the five has submitted a draft text on their respective rules, but they have yet to begin negotiations on liberalization schedules. In reaching consensus and

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<sup>4</sup>The draft FTAA text can be accessed on the FTAA Internet site at [www.ftaa-alca.org/Alca\\_e.asp](http://www.ftaa-alca.org/Alca_e.asp).

beginning negotiations on schedules, each group faces complex and often controversial issues.

- **Market access**—The largest of the negotiating groups, market access, includes the elimination of industrial tariffs and nontariff barriers and related topics. The bulk of the FTAA's market-opening opportunities will be determined through tariff schedule negotiations. The most difficult task in these negotiations will be dealing with sensitive sectors that are vulnerable to competition from imports. Before negotiators can begin tariff schedule negotiations, they must reach agreement on several issues, such as the starting point or base tariff rate used to apply scheduled reductions. This is important because starting from a higher point will have the effect of delaying the liberalization of trade. They also must reach agreement on a number of other complex issues, including the rules that determine whether a product is eligible for FTAA preferences, the types of customs procedures the FTAA should contain, and the design of a “safeguard” mechanism that allows increased protection for industries when imports surge.
- **Agriculture**—Both the United States and other FTAA countries view expanding access to agricultural markets as one of their top trade priorities, but they disagree on three major issues. First, FTAA countries must decide whether they wish to address domestic support payments to farmers such as market-price support programs, loan deficiency payments, and commodity loan programs. The United States, which currently uses domestic support payments but competes in world commodity markets with the European Union (EU), believes that domestic supports can only be addressed at a global level and not in a regional trade agreement. Second, once tariff negotiations begin in May 2002, FTAA countries must decide how to treat import sensitive agricultural products. Often, a sensitive product from one country (such as orange juice in the United States) is a competitive product for another country (Brazil). Third, while FTAA countries have agreed to eliminate export subsidies in the region, they have not agreed on how to deal with subsidized products from countries outside of the region or whether to create rules to discipline their own export subsidies to other regions.
- **Services**—As the world's largest exporter of services such as telecommunications, the United States could benefit greatly from negotiations within the FTAA on the liberalization of services trade. Negotiators on services have made progress developing a draft chapter

on services but several issues remain to be resolved. They need to make decisions concerning whether the coverage of the chapter should include when a company provides services through a commercial presence in another country, which is also considered an investment issue. Also, negotiators must develop the structure for producing the individual country schedules of market access commitments. For example, negotiators must decide whether the approach for liberalization will be a top-down or "negative" list approach, which assumes that all sectors are covered by the agreement unless specifically excluded, or a bottom-up or "positive" list approach, which covers only those sectors specifically included in a country's schedule. The United States supports the negative list approach, arguing that it would lead to more ambitious liberalization.

- **Investment**—The United States has a keen interest in the FTAA negotiations on investment, not only because it is one of the largest foreign investors in Latin America, but because it has investment agreements in force with only 10 of the 33 other FTAA participants. The investment negotiators have reached broad agreement on the overall thrust of the chapter and the nature of many of its provisions, but they diverge on the coverage of the FTAA's investment rules. The United States is seeking a comprehensive agreement that covers all forms of investment as well as an agreement that addresses certain labor and environmental issues associated with investment. Some other countries are opposed to taking such a broad approach. The U.S. proposals on labor and environment to the investment group initiated larger debates over the inclusion of language on labor rights and environmental standards in the FTAA. Investment is also at the center of a debate over the proper balance between corporate rights and the public interest.
- **Government procurement**—Valued at approximately \$250 billion, the Western Hemisphere's government procurement market offers potentially great market-opening opportunities. Only four of the FTAA countries—the United States, Canada, Mexico, and Costa Rica—are party to an international government procurement agreement that sets out predictable procedural rules enabling foreign suppliers to compete on an equal footing with domestic suppliers. Negotiators on government procurement are challenged by the fact that many countries have little experience with procurement disciplines. The government procurement group will have to reach consensus on whether the FTAA's rules on government purchases should require the use of specific procedures for announcing and awarding bids or simply contain broad

principles. The group must also agree on the government entities that will be covered by such disciplines.

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## Other Negotiating Groups Develop Rules and Institutional Provisions

In addition to the five market-opening groups, FTAA countries are developing rules on IPR; subsidies, antidumping, and countervailing duties; dispute settlement; and competition policy. Each of these four negotiating groups has developed a draft of their respective chapters. The drafts, as with the five market-opening groups, are heavily bracketed, with brackets denoting text that is still in dispute. Currently, the groups vary in the extent of their divergence. Negotiators in the IPR and subsidies and antidumping groups differ on important principles. On the other hand, negotiators in dispute settlement and competition policy have reached broad agreement but differ over details. Some of the more significant differences in each group follow:

- **Intellectual property rights**—Because the United States maintains a decisive competitive advantage in high-technology, knowledge-based industries that are dependent on IPR, this is one of the most important topics for U.S. negotiators. FTAA countries have somewhat divergent interests in this area. Developed countries want to bolster enforcement of existing rules and cover new technologies, such as the Internet and biotechnology. Developing countries, despite wider recognition of the importance of IPR to fuel innovation and investment, are reluctant to go beyond existing trade and IPR treaties and face the need to build enforcement capacity. Certain issues within the negotiations, such as compulsory licensing and the patenting of plants, animals, and biological processes, may also prove controversial.
- **Subsidies, antidumping, and countervailing duties**—An area that is likely to be contentious throughout the course of the negotiations is the use of antidumping and countervailing duties. Many countries in the Western Hemisphere employ these trade remedies to counter subsidized or unfairly traded imports. The United States has been an active proponent of their use. However, some countries believe that these measures are inappropriately protectionist. FTAA countries proposed widely varying draft text on this issue. The United States, in a controversial move, proposed that countries be able to maintain their current antidumping and countervailing duty laws as permitted under the WTO. However, other countries proposed to limit these measures or eliminate the use of trade remedies altogether once free trade is achieved.

- **Dispute settlement**—Effective provisions for settling disputes will help ensure that the FTAA's commitments are met. Crafting these provisions will require members to balance a desire for a strong regional enforcement mechanism against national concerns about sovereignty. While negotiators agree on much of the broad framework of the dispute settlement process, they disagree over details such as how to handle compliance, whether to allow appeals, and the extent to which the process should be open to outside parties. FTAA negotiators also must determine the relationship between the FTAA's dispute settlement process and other international agreements.
- **Competition policy**—Competition policy is a new area for most countries in the Western Hemisphere, as only 12 of the 34 participating countries currently have competition policy laws. While the 34 participants have agreed that members of the FTAA should implement measures that proscribe anticompetitive business conduct such as monopolistic behavior, they differ over the level of detail necessary to promote the effective development of competition policy laws and agencies at the national or subregional level. The participants also have not agreed on the type of dispute settlement mechanism that should be used to settle disputes over implementation of the competition policy chapter.

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### Ministers Take Steps to Address Crosscutting Themes

FTAA participants have taken steps to incorporate into FTAA negotiations three crosscutting themes: smaller economies, electronic commerce, and civil society. These "non-negotiating" groups do not produce text for the FTAA agreement. They serve as a forum for discussion and a source of information on issues that reflect challenges arising from the diversity of FTAA participants, the need to respond to emerging technologies, and the support and concern that the trade negotiations attract from a range of societal interests.

- **Smaller economies**—Although there is no agreed definition of what constitutes a smaller economy, by various measures, up to 25 of the 34 FTAA countries could be considered to have smaller economies. FTAA ministers have agreed that the FTAA should take into account differences in size and development. However, negotiators have not reached agreement on what form any special treatment will take or which countries will qualify for it. The United States would like to address these issues on a case-by-case basis, while other participants feel this may exclude them from receiving certain special considerations

that they might receive under a more categorical approach. In addition, FTAA countries are seeking technical assistance to help them participate in the negotiations and implement the obligations of the eventual agreement.

- **Electronic commerce**—E-commerce involves the use of information technology and telecommunications networks to produce and sell products. Because fostering a supportive environment and maintaining a liberal trading regime for e-commerce are goals of FTAA nations, they have created a forum to share information. E-commerce issues also arise in several areas of the FTAA negotiations, such as the exchange of goods and services and the protection of intellectual property. The FTAA could result in commitments that provide a more open and predictable environment for this promising technology.
- **Civil society**—The FTAA's comprehensive scope has attracted interest from a number of civil society groups representing nongovernmental interests, such as business, labor, the environment, and academia. Recognizing the importance of these groups, the ministers created a mechanism for receiving the views of civil society through a formal submission process. However, civil society representatives complained that the FTAA process was not open enough to allow meaningful input, and that the input they had provided had not been adequately considered. In Buenos Aires, FTAA ministers began to address these complaints by (1) agreeing to publicly release the draft negotiating text, (2) directing that the civil society submissions be transmitted to the appropriate negotiating groups, and (3) mandating the exploration of other ways to focus and sustain communications with civil society. The draft FTAA agreement is now available on the Internet in all four official languages of FTAA negotiations (English, French, Portuguese, and Spanish).

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### FTAA Would Expand Market Access and Other Rights for the United States in the Western Hemisphere, but Some Industries May Be Adversely Affected

Although the scope of the FTAA has yet to be determined, a comprehensive agreement could have wide-ranging effects on U.S. trade and investment with other Western Hemisphere countries. Currently, this trade and investment is substantial and growing.

- Elimination of tariff and nontariff barriers would provide greater market access for U.S. exporters. Although FTAA countries have significantly reduced tariff barriers over the past decade, average tariff rates still

remain over 10 percent for many countries. Agricultural tariffs tend to be even higher for most FTAA countries.

- FTAA tariff elimination also could fix problems faced by U.S. exporters whose competitors receive more favorable treatment through preferential trade agreements. For example, Canadian forest products, wheat, vegetable oils, and potatoes receive duty-free access into the Chilean market through the Canada-Chile Free Trade Agreement, while U.S. products generally face a 8-percent duty. The EU is also negotiating free trade agreements with Chile and Mercosur (comprised of Argentina, Brazil, Paraguay, and Uruguay) to gain duty-free access to those markets, which the United States presently does not enjoy.
- Since the U.S. market is already relatively open for FTAA countries, many U.S. imports will face little change. Eighty-seven percent of U.S. merchandise imports from these countries entered the United States duty-free in 2000, and trade-weighted average U.S. tariffs on imports from FTAA countries were less than 1 percent.
- Some U.S. products remain protected through high tariffs, tariff-rate quotas, quotas, and other measures. Removal of these barriers for some products, such as textiles and apparel, sugar, peanuts, and citrus, would likely increase competition, lower prices, and reduce production, potentially displacing some U.S. firms and workers.
- Liberalization of trade in services would benefit highly competitive U.S. service providers in such sectors as finance and telecommunications. In the WTO, FTAA countries have generally made very limited commitments to open their service markets. Although some countries have begun to unilaterally liberalize their markets and privatize some industries, these changes are not bound by a trade agreement with the United States. The U.S. market for services is already relatively open, although some sectors, such as maritime services, are restricted.
- Investment is increasingly interconnected with trade as companies set up processing plants in multiple countries to supply goods and services for their worldwide operations. The United States is the world's largest source of long-term investment and, in 1999, had accumulated investment valued at \$265 billion in FTAA countries. However, the United States has in force investment treaties protecting investor rights with only 10 of these countries. Brazil, the second largest recipient of U.S. foreign direct investment after Canada, does not have a bilateral

treaty with the United States. An FTAA investment chapter would guarantee specific rights to foreign investors and would require all participants to give foreign investors these specific rights.

- As a world leader in the creation and production of original works and intellectual content in fields ranging from motion pictures and software to pharmaceuticals and plant varieties, the United States would generally benefit from improvements in the protection of IPR through the FTAA. Establishment of FTAA principles on intellectual property could also increase exports of U.S. products embodying intellectual content.
- Finally, government procurement is an area in which the United States has no multilateral or bilateral commitments with FTAA countries outside of the North American Free Trade Agreement, which applies to Mexico and Canada. As many FTAA countries' government operations make up important shares of their economic activity, improved access to procurement markets elsewhere in the hemisphere would provide new opportunities for U.S. exporters of goods and services.

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## Agency Comments

We obtained oral comments on a draft of this report from the Assistant USTR for the Americas. USTR generally agreed with the information in the report and provided technical comments that we incorporated as appropriate.

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# Introduction

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In December 1994, the heads of state and government of the 34 democratic countries in the Western Hemisphere agreed at the first Summit of the Americas in Miami, Florida, to conclude negotiations to create a Free Trade Area of the Americas (FTAA) no later than 2005.<sup>1</sup> These negotiations are an extension of the economic reform and integration that has occurred in much of the hemisphere over the past decade, fueling increased trade and investment within and outside of the region. Since then, the FTAA trade ministers have established a framework for the FTAA negotiations and negotiators have begun drafting the text of the agreement.

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## The FTAA Is Part of a Larger Process of Economic Liberalization and Integration

The FTAA negotiations were initiated within the context of ongoing unilateral liberalization in many countries. Following a serious debt crisis, sluggish economic growth, and spiraling inflation in the 1980s, most Latin American economies shifted their economic strategies from protected, state-assisted industrialization to externally oriented, export-driven development. These strategies included lowering trade barriers and taking steps to attract foreign investment. As a result, economic growth doubled, rising from 1.7 percent on average in the 1980s to 3.4 percent in the 1990s; inflation decreased significantly; and trade expanded rapidly.

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<sup>1</sup>The 34 countries participating in FTAA negotiations are: Antigua and Barbuda, Argentina, the Bahamas, Barbados, Belize, Bolivia, Brazil, Canada, Colombia, Chile, Costa Rica, Dominica, the Dominican Republic, Ecuador, El Salvador, Grenada, Guatemala, Guyana, Haiti, Honduras, Jamaica, Mexico, Nicaragua, Panama, Paraguay, Peru, St. Kitts and Nevis, St. Lucia, St. Vincent and the Grenadines, Suriname, Trinidad and Tobago, the United States, Uruguay, and Venezuela.

All but 1 of the 34 nations participating in FTAA negotiations are members of the World Trade Organization (WTO), which sets trade rules on a global basis through a process of multilateral negotiations among its members. As part of their economic liberalization programs of the past decade, countries in the Western Hemisphere have also pursued economic integration through numerous free trade and customs union agreements.<sup>2</sup> The largest trading bloc outside of the North American Free Trade Agreement (NAFTA) is Mercosur, which comprises Brazil, Argentina, Paraguay, and Uruguay. Other regional blocs include the Caribbean Community and Common Market (CARICOM),<sup>3</sup> the Andean Community,<sup>4</sup> and the Central American Common Market (CACM).<sup>5</sup> Countries in the region, particularly Mexico and Chile, have concluded numerous bilateral free trade and investment agreements with others in the region. These subregional agreements provide greater access for industrial goods and have sometimes covered agriculture, services, and investment.<sup>6</sup> Countries in the Western Hemisphere also are making agreements with those outside of the hemisphere. Mexico recently concluded a free trade agreement with the European Union (EU), and Chile and Mercosur are negotiating their own bilateral free trade agreements with the EU.

Trade among Latin American countries and between Latin America and the rest of the world expanded rapidly during the 1990s. Overall trade by the region grew by 10.8 percent annually on average, outpacing world trade growth (6.6 percent) over the same period. However, intra-regional trade between members of the same trade blocs grew faster than extra-regional

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<sup>2</sup>Free trade agreements generally eliminate tariff duties and other barriers on substantially all trade between the member countries and may include other provisions covering subjects such as investment and government procurement. Customs union agreements go beyond free trade agreements by eliminating duties between partners and by setting common external tariffs that are applied to countries not party to the agreement.

<sup>3</sup>The CARICOM's members are Antigua and Barbuda, the Bahamas, Barbados, Belize, Dominica, Grenada, Guyana, Haiti, Jamaica, St. Kitts and Nevis, St. Lucia, St. Vincent and the Grenadines, and Trinidad and Tobago.

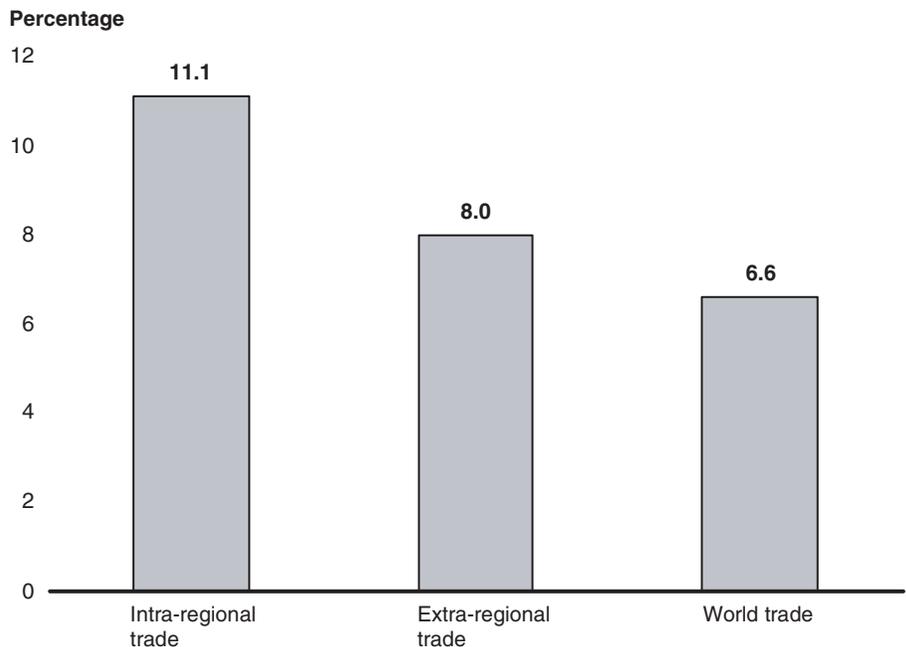
<sup>4</sup>The Andean Community's members are Bolivia, Colombia, Ecuador, Peru, and Venezuela.

<sup>5</sup>The CACM's members are Costa Rica, El Salvador, Guatemala, Honduras, and Nicaragua.

<sup>6</sup>Some subregional agreements exclude provisions on agriculture altogether. Although the U.S.-Canada Free Trade Agreement, Mercosur, and CARICOM agreements all include agriculture provisions, they also exclude sensitive products such as sugar, dairy, poultry, and eggs. The services area is relatively new for trade agreements. Investment has been covered in free trade agreements and through bilateral stand-alone agreements.

trade. This was particularly true for Mercosur and the Andean Community, where intra-regional trade grew twice as fast as extra-regional trade. Trade within Latin America as a whole also grew faster than trade between Latin America and the rest of the world (see fig. 1).

**Figure 1: Growth of Extra-regional, Intra-regional, and World Trade, 1990-99**



Source: Inter-American Development Bank.

Although the 1990s was a decade of continued reform and expanded trade, new challenges arose. For example, Mexico and Brazil both faced serious financial crises in 1995 and 1998, respectively—Hurricane Mitch devastated parts of Central America in 1998, and the Andean region has struggled with political instability and effects of the drug trade. Also, Argentina has been mired in recession and has recently faced its own financial crisis. Despite reforms, many countries still face high unemployment rates and wide disparities between the wealthy and the poor. These economic and social obstacles create challenges for continued reform, economic development, and liberalization.

The prospects for the FTAA agreement, which evolved out of the reform process, will be affected by how well countries resolve these challenges. At the same time, a successfully concluded FTAA agreement may help secure the liberalization that has already taken place and extend it to new areas. Beyond these economic benefits, the FTAA is widely regarded as a centerpiece of efforts to forge closer and more productive ties among Western Hemisphere nations, increase political stability, and strengthen democracy. While the FTAA should provide benefits, it may also adversely affect certain sectors. In addition, some labor and environmental groups are concerned that potential FTAA provisions may reduce the ability of countries to set and enforce high standards for health, safety, and the environment. As in the case with other international trade agreements, the FTAA has also drawn the attention of organizations and individuals apprehensive about increased globalization of international economic activity.

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## Negotiators Have Succeeded in Laying the Groundwork for the FTAA

Some progress has been made in the FTAA process, including building a technical foundation for FTAA negotiations. At the March 1998 San José Ministerial, ministers agreed on guiding principles for the FTAA. An organizational structure and objectives for negotiations were established, and overall and interim deadlines were set. Since then, draft chapters reflecting proposals on the topics under negotiation have been prepared. Milestones for progress in the current negotiating phase have been set, but challenges remain, including bridging differences on key topics.

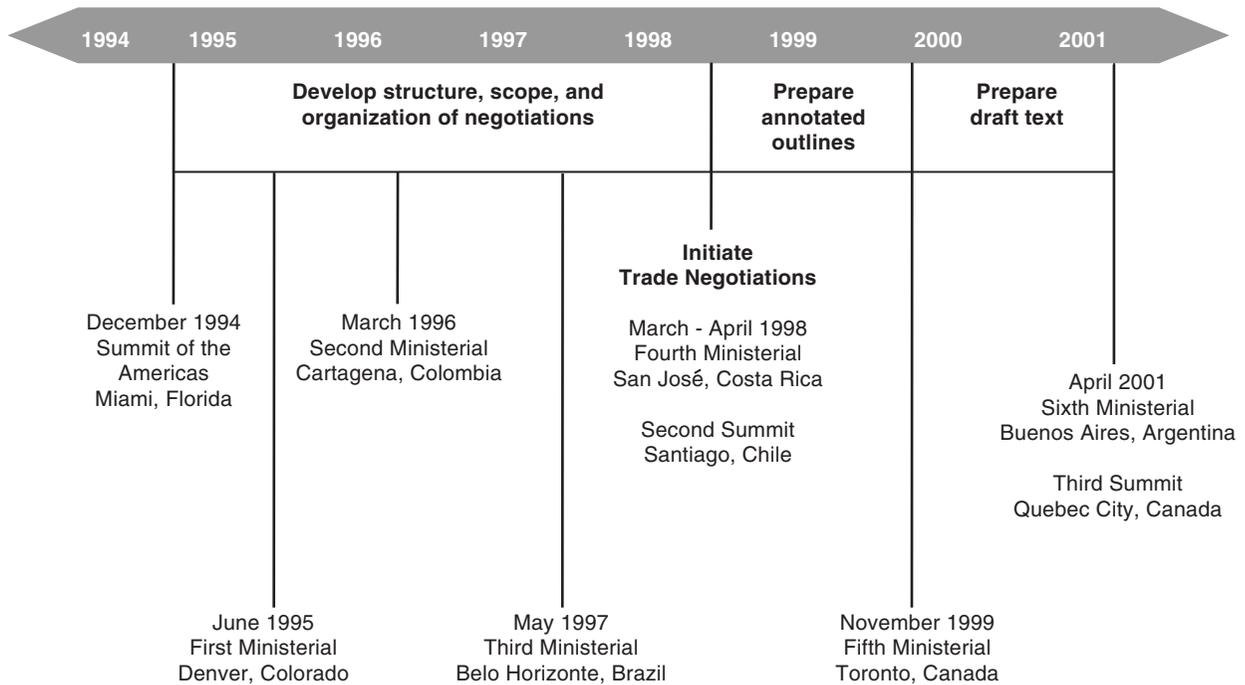
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## FTAA Progress to Date

Since beginning the process in 1994, the 34 participating countries have succeeded in building a technical foundation for the negotiations. As shown in figure 2, from December 1994 to March 1998, participants developed guiding principles for FTAA negotiations. For example, they agreed that all decisions in the FTAA negotiating process would be made by consensus and that the FTAA would be a single undertaking, meaning that the agreement would be completed and implemented as a whole rather than in parts. They also agreed that the FTAA agreement would (1) be consistent with the rules and disciplines—or practices—of the WTO; (2) improve WTO rules and disciplines whenever possible and appropriate; and (3) coexist with other subregional agreements, such as Mercosur and NAFTA, to the extent that the rights and obligations of those agreements go beyond or are not covered by the FTAA. They also reached consensus on the overall structure, scope, and objectives of the negotiations. The

participating countries then formally initiated the negotiations in 1998 at the San José Ministerial and the Santiago Summit of the Americas.

Figure 2: FTAA Negotiations, 1994-2001

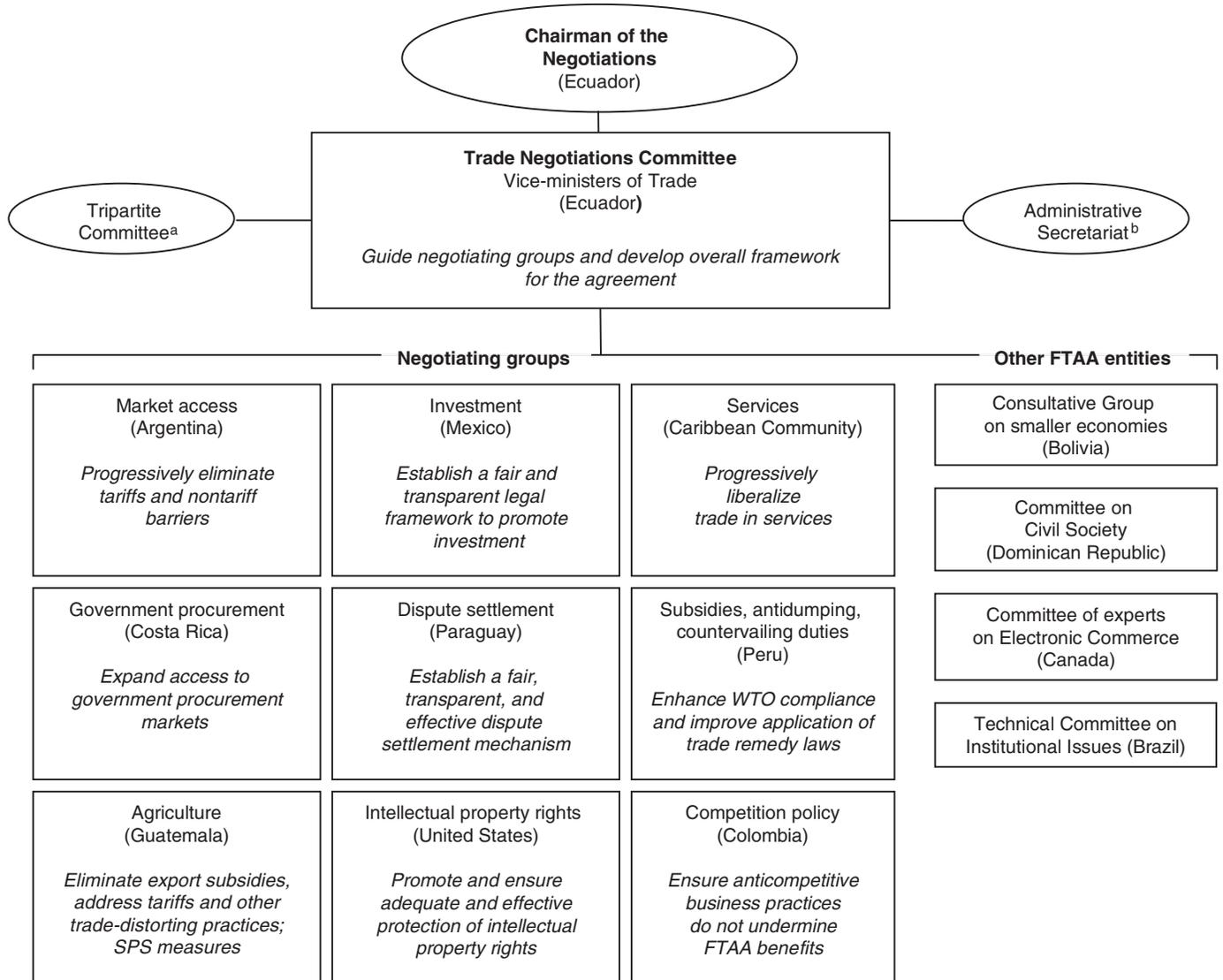


Source: GAO.

## FTAA Organizational Structure

The FTAA negotiations are organized into nine negotiating groups and four special committees and overseen by the vice-ministerial level Trade Negotiations Committee (TNC) (see fig. 3). The ministers set out the workplans for the negotiating process and select new chairs for the negotiating groups and committees in 18-month cycles. The chairmanship of the negotiations changes at the start of each 18-month negotiating cycle, with Ecuador serving as chair for the current cycle of negotiations. Brazil and the United States are set to co-chair the final cycle from November 2002 to December 2004.

Figure 3: Organization of the FTAA Negotiations



Legend:

SPS = Sanitary and phytosanitary measures. These measures are taken to protect human, animal, or plant life or health.

Note 1: Current chairs of the various FTAA entities are in parentheses. The general objectives of each negotiating group and the Trade Negotiations Committee appear in italics.

Note 2: The venue for the actual negotiations, currently in Panama City, was initially located in Miami and will rotate to Mexico City in March 2003.

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<sup>a</sup>The Tripartite Committee, which provides technical support to the negotiations, is comprised of the Organization of American States, the Inter-American Development Bank, and the United Nations Economic Commission for Latin America and the Caribbean.

<sup>b</sup>The Administrative Secretariat supports the FTAA ministers, the Trade Negotiations Committee, negotiating groups, and other FTAA entities.

Source: GAO analysis of FTAA data.

In preparation for the Buenos Aires Ministerial in April 2001, the negotiating groups produced a first draft text on their specific issues. The draft text is heavily bracketed,<sup>7</sup> indicating that agreement on specific language has not been reached. Nevertheless, the draft text will form the basis for future negotiations, which are expected to narrow differences on the range of proposals currently under consideration.

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## Milestones Set for Current Phase of FTAA Negotiations

At the April 2001 Buenos Aires Ministerial and Quebec City Summit, FTAA countries set out objectives and interim deadlines to promote the progress of the negotiations during the current 18-month negotiating cycle (May 2001 to Oct. 2002), which will culminate at the next trade ministerial to be held in Ecuador (see fig. 4). Ministers also set specific goals and timetables for the current cycle:

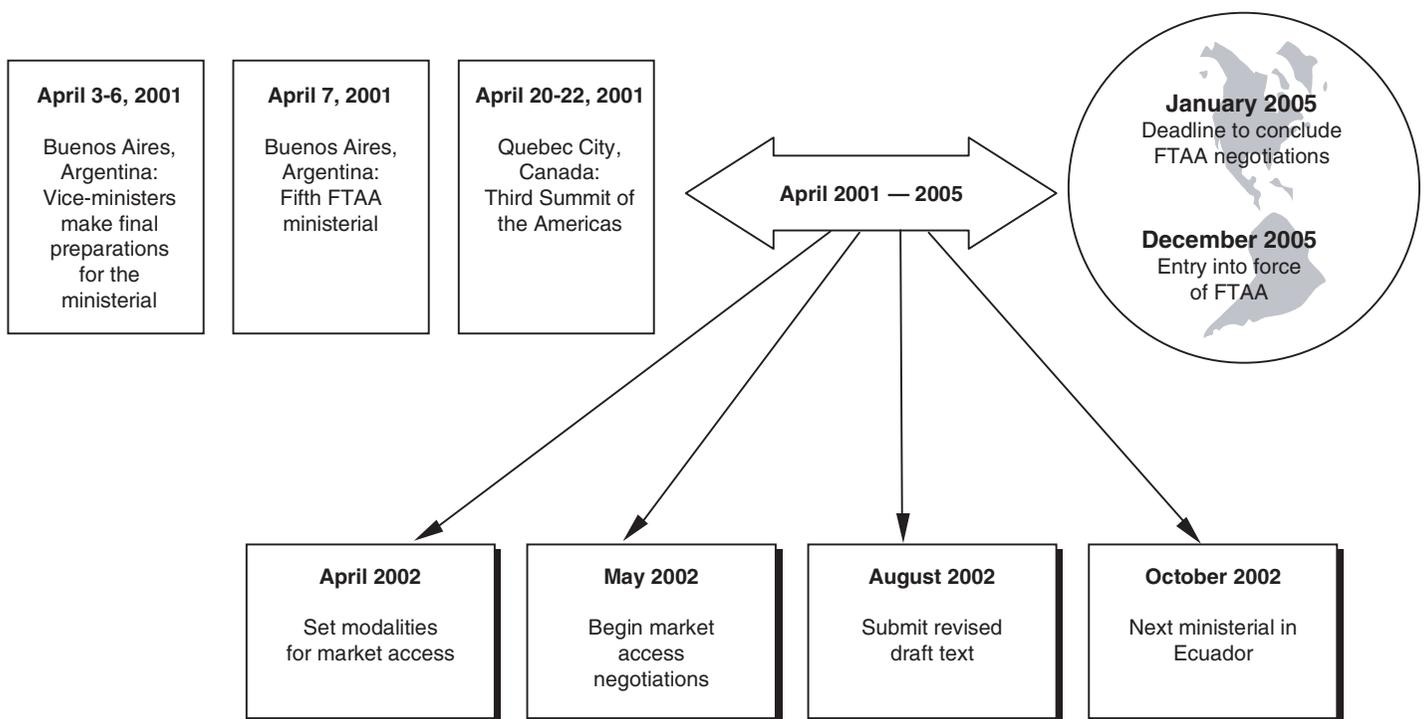
- To move toward consensus on draft rules, ministers directed negotiating groups to consolidate text and eliminate—to the maximum extent possible—material that is in dispute.
- To prepare to begin negotiations on market access schedules, ministers instructed specific groups to develop recommendations by April 1, 2002, on the methods and modalities (basic ground rules) for these negotiations.
- The ministers also asked the groups to develop, where appropriate, inventories by April 2002 of tariffs, nontariff barriers, subsidies, and other practices that distort trade.
- The ministers directed negotiating groups to initiate negotiations on market access schedules no later than May 15, 2002.

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<sup>7</sup>The term “bracketed” refers to the punctuation placed around language in the draft chapters for which agreement has not yet been reached. For example, if two countries submitted different proposals for language in a chapter, brackets would be placed around each proposal until a consensus is reached on the differences between the two.

In addition, heads of state and government agreed at the Quebec City Summit to conclude the negotiations no later than January 2005 and to seek the entry into force of the agreement no later than December 2005.

Figure 4: FTAA Time Frames and Milestones, 2001-05



Source: GAO analysis.

Despite this progress, numerous challenges remain. Among them are technical and substantive differences on the nine topics being negotiated. Chapter 2 of this report addresses five of the nine topics being addressed in an FTAA that relate to market opening: market access, agriculture, services, investment, and government procurement. Rules are also being developed on four other trade topics, which are addressed in chapter 3, including intellectual property rights (IPR); dispute settlement; subsidies, antidumping, and countervailing duties; and competition policy. Three special committees provide input to the TNC on crosscutting themes—namely, the treatment of smaller economies, civil society, and electronic commerce (e-commerce), which are addressed in chapter 4. Chapters 2, 3,

and 4 provide an overview of the topic or theme and its importance, describe the mandate of the group and its progress to date, identify controversial or otherwise important issues, and discuss next steps. Chapter 5 discusses the potential effect of a completed FTAA on U.S. trade and investment with other Western Hemisphere countries. Appendix I presents information on U.S. trade and investment with the 34 countries negotiating the FTAA.

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## Objectives, Scope, and Methodology

Our objectives for this report were to describe (1) the progress made to date and the issues that remain in negotiating greater market opening among FTAA countries, (2) the progress made to date and the issues that remain in developing other rules and institutional provisions for an eventual FTAA agreement, (3) the significant crosscutting themes affecting the FTAA negotiations and how have they been addressed to date, and (4) the potential effects of a completed FTAA on U.S. trade and investment with other Western Hemisphere countries.

To address the first three objectives, we reviewed executive branch documents, related publications, and economic literature, and we held discussions with lead U.S. government negotiators for each FTAA negotiating group. We also reviewed FTAA documents, including the draft FTAA agreement. We had discussions with foreign government officials representing each of the major negotiating blocks and with officials from the Inter-American Development Bank (IDB), the Organization of American States (OAS), and the United Nations Economic Commission for Latin America and the Caribbean (ECLAC), collectively known as the Tripartite Committee, which provides technical support to the negotiations. We reviewed formal comments about the FTAA that were made in response to *Federal Register* notices and submitted to the Office of the U.S. Trade Representative (USTR). We also met with experts on the FTAA and international trade negotiations and representatives from business and civil society groups that have expressed interest in the FTAA process. In addition, we traveled to Buenos Aires, Argentina, to take part in the Americas Business Forum and Academic Colloquium associated with the FTAA Trade Ministerial and attended public briefings by USTR and the Department of State for civil society representatives.

To address the fourth objective, we analyzed U.S. and regional trade and investment data from 1990 to 2000, current U.S. and regional trade barriers, and market-distorting government policies. We also examined the extent to which FTAA countries were members of multilateral and bilateral trade

and investment agreements with the United States. U.S. merchandise trade data came from Department of Commerce official trade statistics. Exports were measured in terms of domestic exports at “free alongside ship” value. Imports were measured in terms of imports for consumption at customs value. U.S. services trade and investment data came from the Bureau of Economic Analysis’ *Survey of Current Business*. World trade data came from the United Nations international trade database. U.S. tariff data came from the U.S. International Trade Commission. Some tariff rates are given as specific rates of duty (e.g., \$5 per bushel) rather than ad valorem (percentage of value) rates. Ad valorem equivalent rates are conversions of specific rates to ad valorem rates, which allow average tariff rates to be calculated. To the extent that they were available from the International Trade Commission, these rates were used in the calculation of overall average tariff rates. U.S. trade and tariff data were analyzed at the eight-digit level of detail based on the harmonized system. For determining U.S. imports subject to duties, the tariff schedule was combined with disaggregated trade data that identified imports by preferential trade program. Other FTAA countries’ average tariff rates came from the World Bank and the IDB. In some instances, these organizations calculated different average tariff rates for the same country in the same year. For example, the World Bank lists Uruguay’s average tariff rate at about 4.5 percent in 1999, while the IDB reports an average tariff rate at above 12 percent. For consistency, we reported World Bank calculated tariffs, unless they were not available for a particular country. In that case, we reported IDB tariff rates.

We relied on reports by the International Trade Commission on U.S. services trade; the International Trade Commission and the United Nations on U.S. and world investment; and the WTO, OAS, IDB, and ECLAC on each of the negotiating areas. We did not estimate an economywide model of the overall effects of the FTAA. We did review economic studies that analyze some aspects of FTAA liberalization in an economywide framework. We also did not estimate the impact of an FTAA on production, labor, and prices overall or for individual sectors of the U.S. economy.

For all four objectives, we relied on our past and ongoing work on trade liberalization in the Western Hemisphere.<sup>8</sup> Because FTAA negotiation ground rules only allow countries to divulge their own positions, this report generally does not name the countries holding particular positions unless officials from those countries told us that it was acceptable to do so. We acknowledge that we analyzed the FTAA from the U.S. perspective, not that of other countries participating in the process. Finally, given the relatively early stage of FTAA negotiations, and the recent emergence of key information, such as a public version of the draft agreement, U.S. civil society groups and the public that either favor or oppose the FTAA are likely to be forthcoming with more concrete positions on FTAA negotiating topics. For example, USTR issued a *Federal Register* notice on July 12, 2001, soliciting specific views from the public on the draft FTAA agreement,<sup>9</sup> but these comments were not received in time to be reflected in this report.

We conducted our work from September 2000 through August 2001 in accordance with generally accepted government auditing standards.

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<sup>8</sup>Early developments in the FTAA process are discussed in *Trade Liberalization: Western Hemisphere Trade Issues Confronting the United States* (GAO/NSIAD-97-119, July 21, 1997).

<sup>9</sup>*Federal Register*, Vol. 66, No. 134, pp. 36614-36615, July 12, 2001. Comments were due to USTR by August 22, 2001.

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# FTAA Efforts to Open Hemispheric Markets

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The five FTAA groups charged with negotiating market-opening opportunities—market access, agriculture, services, investment, and government procurement—have drafted rules and are now developing the databases and methods that they will use to schedule the reduction and elimination of trade barriers among FTAA participants. Each group faces a number of issues. The market access group has the broadest set of responsibilities, including tariff and nontariff barriers for industrial goods; rules of origin; customs procedures; and technical barriers to trade, such as product standards. Also, before this group can begin negotiations on tariff elimination—one of the principal goals of a free trade area—it must agree on which tariff rates to use as a starting point. The agriculture group faces many controversial issues in its discussions, including whether to include domestic support payments to farmers (subsidies) in the FTAA agreement and how to treat sensitive products. The services negotiating group faces tough choices on the scope, structure, and timing of liberalization. Discussions on investment reveal broad agreement on many basic principles, but they also reveal differences on coverage, investor-state dispute settlement, and labor and environmental provisions. Finally, government procurement is a relatively new area for many FTAA participants and presents both opportunities in terms of market opening and challenges in terms of common experience. The group also must resolve differences over how prescriptive FTAA rules should be. Table 1 provides an overview of the five FTAA groups charged with negotiating market-opening opportunities. The remainder of this chapter describes each of these topics, its importance, and the group's negotiating mandate; progress to date; significant issues; and next steps. Information on the potential economic impact of trade liberalization for these topics can be found in chapter 5.

**Chapter 2**  
**FTAA Efforts to Open Hemispheric Markets**

**Table 1: Overview of Market-opening Negotiating Groups**

<b>Topic</b>	<b>Significance for the United States</b>	<b>Mandate</b>	<b>Next steps</b>
Market access	Interregional industrial trade of about \$650 billion; high regional tariff and nontariff barriers; broadest scope of any negotiating group.	Progressively eliminate tariff and nontariff barriers.	November 2001 - Complete trade database. April 2002 - Agree on modalities. May 2002 - Begin tariff negotiations. August 2002 - Submit revised text.
Agriculture	Top trade priority for many FTAA countries; U.S. exports could increase by \$1.5 billion; high tariffs for sensitive products.	Progressively eliminate tariffs on agricultural goods, eliminate export subsidies, address other trade distorting practices; sanitary and phytosanitary measures.	April 2002 - Agree on modalities. May 2002 - Begin tariff negotiations. August 2002 - Submit revised text.
Services	United States is world's leading services exporter; many FTAA countries are new to services liberalization.	Progressively eliminate barriers to trade in services.	April 2002 - Agree on modalities. May 2002 - Begin services negotiations. August 2002 - Submit revised text.
Investment	United States is one of the largest foreign investors in Latin America; other countries see FTAA rules as way to attract foreign investment.	Establish a fair and transparent legal framework to promote investment.	April 2002 - Agree on modalities. May 2002 - Begin tariff negotiations. August 2002 - Submit revised text.
Government procurement	Potentially great market-opening opportunities.	Expand access to government procurement markets.	April 2002 - Identify scope of needed statistical information. April 2002 - Agree on modalities. May 2002 - Begin tariff negotiations. August 2002 - Submit revised text.

Source: GAO analysis.

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## Market Access

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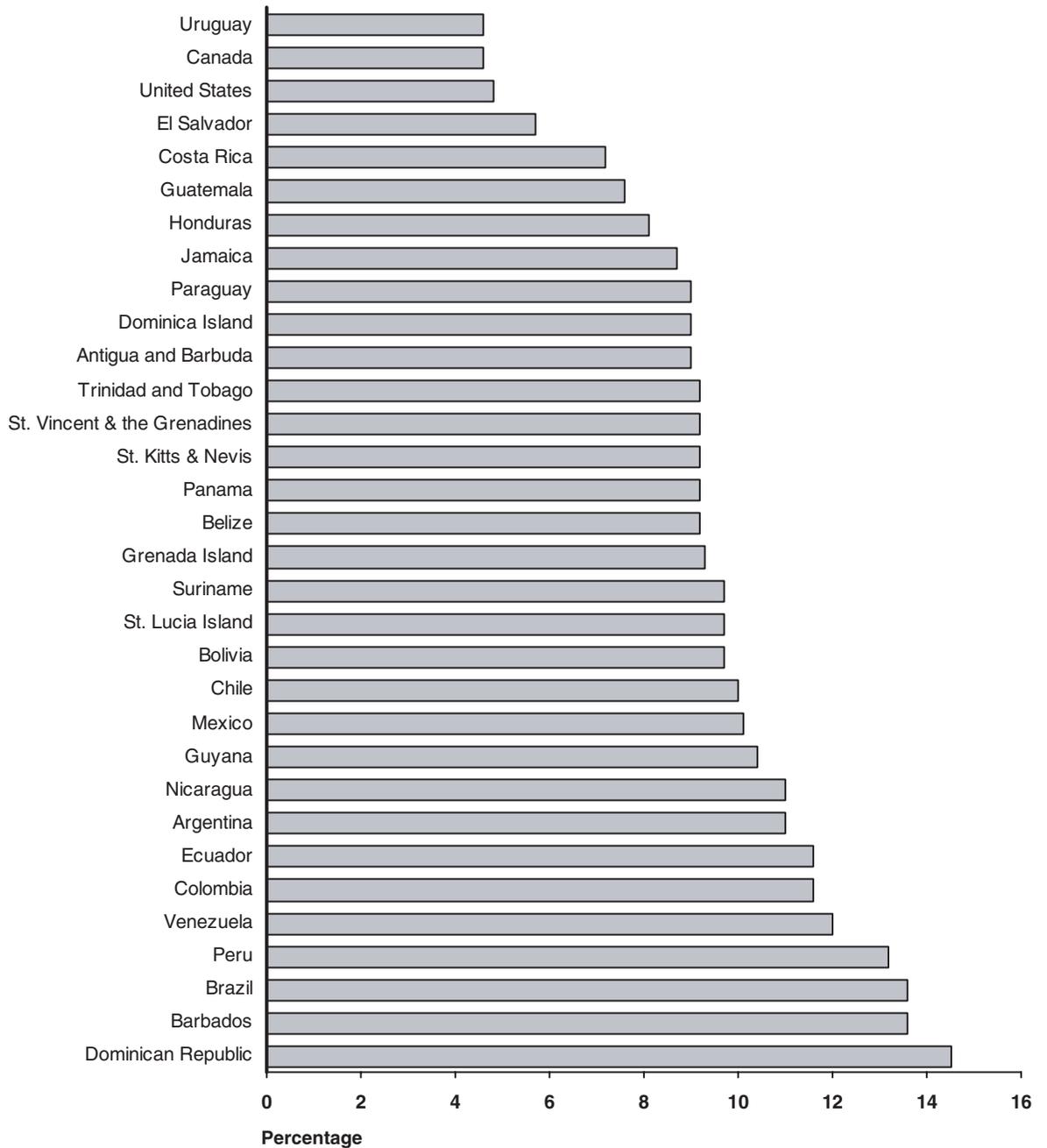
### Topic, Importance, and Negotiating Mandate

The market access negotiating group is crafting the rules and tariff elimination schedules for intraregional trade in industrial products, which was approximately \$650 billion in 1999. Through these market access negotiations, the United States is seeking to eliminate trade barriers and related impediments that restrict U.S. exports of goods to the hemisphere. Tariff barriers for FTAA countries on this trade, although falling, are still generally high, with applied tariffs of many FTAA countries set at rates double the U.S. average of 4.8, as shown in figure 5. Other impediments, such as inefficient customs procedures, can also hinder trade. The market access group covers a greater number of issues than any of the other eight negotiating areas. Its broad scope includes the elimination of industrial tariff and nontariff measures, rules of origin, safeguards, customs procedures, and standards and technical barriers to trade.<sup>1</sup> These issues affect whether a product can be imported, the ease with which the import occurs, and whether the product receives a preferential tariff rate. Trade ministers charged this negotiating group with a mandate to produce an agreement that progressively eliminates tariffs and nontariff barriers and other measures that restrict trade between participating countries.

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<sup>1</sup>Rules of origin are the production or processing requirements a product must meet to qualify as a product eligible for tariff preferences. Safeguard measures are suspensions of tariff elimination commitments or increased duties used to address injury to a domestic industry due to increased competition from tariff liberalization. Standards and technical barriers to trade are provisions that set requirements or restrictions on imported products to achieve domestic regulatory goals, such as the protection of human health and safety.

Figure 5: FTAA Countries' Average Applied Tariff Rates on Merchandise Imports



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Note 1: Average tariffs are the simple average ad valorem rate applied across all products. Data are for the most recent year available, mostly 1998 or 1999. Data for the Bahamas and Haiti are only available for the years before 1997 and are not included in this figure.

Note 2: Some countries may have preferential agreements with other FTAA countries and face lower average tariff rates than those listed in the table. For example, U.S. goods face preferential rates in Canada and Mexico. USTR estimated that trade-weighted Mexican tariffs on U.S. goods were 1.3 percent in January 2000.

Sources: Inter-American Development Bank and the World Bank.

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## Progress to Date

During the last 18-month negotiating period, the group compiled draft proposals for the rules governing market access issues. Participants have noted that all regional groups have been active in this process, which has been challenging, given the broad scope of the market access group. The resulting 113-page draft text includes a range of proposals, some of which are similar to WTO multilateral disciplines, while others recommend wholly new measures. The texts on rules of origin and safeguards, in particular, will be specifically tailored to a regional agreement.

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## Significant Issues

The market access group will ultimately produce three major products: a chapter on the overall rules covering market access, detailed country schedules for tariff liberalization, and detailed rules of origin. To meet these objectives, negotiators will need to cover a wide range of topics over the next 18 months. They will decide on the parameters for eliminating tariff and nontariff barriers and then begin negotiations on market access schedules. These decisions will affect the speed at which countries remove their barriers to FTAA imports. In addition, the negotiators will draft commitments on the other areas under their mandate. Rules of origin, which will determine how products qualify for FTAA preferential rates, will likely be complex to negotiate and potentially controversial for certain products. To craft a regional safeguard mechanism to protect industries harmed by surges in imports, negotiators will need to address countries' desire to provide temporary relief for seriously trade-affected industries without making it too easy to create new barriers to trade. Finally, as tariff barriers are reduced, burdensome customs procedures and potentially restrictive technical standards could become important impediments to importing into a particular market.

## Tariff and Nontariff Barriers

Tariff and nontariff barriers are the principal policy tools countries use to protect domestic markets. The FTAA negotiating group on market access is responsible for conducting the negotiations to eliminate tariffs on trade among the 34 countries. Before substantive negotiations can begin on the

elimination of tariffs on specific goods, however, participating countries must agree on the methods and modalities, or ground rules, they will follow during later negotiations. FTAA countries must agree on the following:

- *The base rate or starting point from which tariffs will be reduced.* This issue involves reaching consensus on whether to use current (applied) rates, bound rates, or some other measure as the base from which to start negotiating. Current or applied rates are the tariff rates a country currently levies on particular goods. Bound tariffs are the maximum duties that a country has committed in the WTO to apply on those goods. Under WTO rules, a country may increase its applied rates up to but no higher than its bound rates. In practice, applied rates are often significantly lower. FTAA countries must determine the starting point, or base rate, from which tariffs will be eliminated. The higher this initial starting point, the longer it may take for actual tariff reductions to be realized. For example, if countries use the bound rate as the starting point, they may not be required to cut their applied rates until later in the reduction period.<sup>2</sup> However, if the applied rate is used as the starting point, then importers will see liberalization within the first years of the agreement. To ensure that phased duty reductions produce genuine market openings, the United States is proposing that the base rate from which tariffs are phased out be the lower of either a product's most favored nation applied rate in effect during the FTAA negotiations or the WTO bound rate at the end of the FTAA negotiating process.
- *Pace of tariff elimination.* This issue aims to define the process and timing used by countries to reduce a product's tariff to zero. A common approach is to divide goods into baskets. For example, the tariffs on one basket of goods could be reduced to zero in 5 years, another basket in 7 years, and a third in 10 years. According to WTO rules tariffs must be eliminated on substantially all products within 10 years. The United States has proposed that products be grouped into three baskets with tariffs eliminated either immediately, in 5 years, or in 10 years for the most sensitive.

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<sup>2</sup>For example, a country with a bound rate of 50 percent and an applied rate of 10 percent would, in the first year of a 5-year reduction period, be required to charge a tariff no greater than 40 percent although it would only actually charge 10 percent. In the second year, the bound tariff rate would fall to 30 percent, while the actual charge stays at 10 percent, and so on. In the final year, the country would reduce its tariff from 10 percent to zero. Therefore, since the country could continue charging its applied rate of 10 percent on that particular product until the last year, no actual liberalization would be realized until the fifth year.

- *Reference period for trade data.* Negotiators must decide what years of trade data will be used to calculate each country's concessions on a trade-weighted basis and to identify which countries have been the primary suppliers of particular products over the reference period. If a country is a major supplier of a product, it may be entitled to special status in the negotiations on that product. This issue will be negotiated with the assistance of a database that is being compiled on tariff rates and information on trade flows from 1997 to 2001. The database is expected to be ready by November 1, 2001. The database also will be useful for countries in determining their negotiating priorities by providing information on current trade and tariff levels.

## Rules of Origin

FTAA negotiations on rules of origin requirements may be complex and sensitive. These requirements will determine whether a product qualifies for tariff preferences under the FTAA. For example, they may require that for a certain product to be considered from the FTAA region, at least 60 percent of its value must come from FTAA countries' labor, parts, and production. Negotiations on rules of origin may be complex if they are specified differently for specific products and entail unique requirements. Also, origin rules may be more restrictive for some sensitive products. For example, under two unilateral trade programs, the United States recently offered tariff preferences for import-sensitive apparel imports, but only if producers use certain U.S.-made fabrics and materials to produce them.<sup>3</sup> Rules of origin are intended to ensure that the benefits of a free trade agreement primarily accrue to the countries covered by the agreement. However, the more restrictive the requirements are for particular products, the more difficult it is for exporters to qualify for the preferential duty. Restrictive rules of origin requirements have been identified as a reason why some exporters do not fully use special tariff preferences offered to them.<sup>4</sup>

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<sup>3</sup>These benefits are offered to certain Caribbean and sub-Saharan African countries under the Caribbean Basin Trade Partnership Act (2000) and the African Growth and Opportunity Act (2000)—see the Trade Development Act of 2000, P.L. 102-600, Title II and Title I, respectively. Some American textile firms support this type of rule of origin for the FTAA because they argue that it encourages the use of U.S.-produced yarns and fabrics in apparel products.

<sup>4</sup> See *International Trade: Comparison of U.S. and European Union Preference Programs* (GAO-01-647, June 8, 2001).

Negotiators must agree upon the types of origin requirements they will use in the FTAA agreement. There are generally two types of origin requirements. The first are value tests, which confer origin on the basis of the percentage of value added in a country. For example, a value test may confer origin if at least 60 percent of the worth of a product comes either from FTAA inputs or the production process in an FTAA country. The second type of origin requirement is the tariff shift approach. This approach confers origin if the production process transforms a product and its inputs enough to classify it as a different product in the tariff schedule. For example, a tariff shift approach might confer origin if a final product, such as a washing machine, is categorized differently on the tariff schedule than its individual parts.

With the tariff shift approach, countries also must decide at what level of detail on the tariff schedule the shift takes place and whether to make those decisions on a product-by-product basis. For example, two products may be in the same aggregate grouping, such as automobiles and auto parts, but they may be in different groups at a more detailed level. The U.S. unilateral preference programs, such as the Generalized System of Preferences, generally follow a value-added approach, while NAFTA generally uses a tariff shift approach. Several Latin American trade agreements have used a combination of a value-added approach with a tariff shift approach at one uniform level of detail. The United States supports a tariff shift approach for the FTAA, but without a uniform rule for the level of detail for the shift. U.S. negotiators argue that the tariff shift approach is less complicated and burdensome to administer than the value-added approach, and that the level of detail at which the shift takes place should depend on the type of product.

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## Safeguard Measures

Negotiators have the challenge of crafting a safeguard mechanism that meets FTAA countries' desire to provide temporary assistance to industries seriously injured by increased regional competition without making it too easy to erect new trade barriers. Safeguards are temporary measures that either freeze or roll back trade liberalization when it is shown that the liberalization has caused injury to a domestic industry. These measures are intended to provide the industry with time to adjust to increased competition. However, if these measures are too easy to apply, they can potentially extend protections that the agreement intended to remove. The draft FTAA text includes a variety of proposals that cover (1) the procedures a country must follow to use a safeguard measure; (2) the degree of injury or impact on the domestic industry that must be shown; (3) the types of measures that could be applied (e.g., tariff or quotas); and (4) the length of time the measures can stay in place. Many proposals draw on the WTO safeguard measure, which allows for tariffs or quotas to be used for up to 4 years<sup>5</sup> if increased quantities of imports can be shown to cause or threaten to cause serious injury to a domestic industry. The United States has proposed that the FTAA only allow tariffs, not quotas, to be used (as in NAFTA), for up to 3 years, if imports are shown to be a substantial cause or threat of serious injury to a domestic industry. Also, the United States has proposed that FTAA safeguard measures would only be available for countries during a 10-year transitional period. Negotiators also must decide whether FTAA countries may be exempted in certain circumstances if other FTAA countries use the WTO safeguard mechanism. In addition, countries may decide to negotiate separate sector-specific safeguards that would provide separate rules for a particular product or sector, such as textiles.

## Customs Procedures

Negotiating customs procedures within a trade agreement in the Western Hemisphere is a new and challenging undertaking. Other trade agreements, including the WTO, have had few concrete applications in this area. Thus, many of the countries involved in the FTAA process lack experience in this subject. Other challenges include the countries' human capital and institutional capacity for implementing customs procedures and the overhaul of laws and procedures necessary to enforce these proposals.

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<sup>5</sup>The WTO safeguard provision allows the measures to be extended to 8 years when it can be shown that the safeguard measure continues to be necessary and that the industry is adjusting.

The San José, Costa Rica, Ministerial provided FTAA negotiators with a mandate to simplify customs procedures to facilitate trade and reduce administrative costs and also to promote customs mechanisms and measures to ensure that these operations be conducted with transparency, efficiency, integrity, and responsibility. The proposals as of July 3, 2001, in the bracketed text include proposals on transparency and information dissemination, automation, and combating fraud and other illicit customs-related activities. However, some countries have wanted to include only general customs principles, not specific policies.

The major objectives of the United States include transparency of customs procedures and their administration, establishment of an advance customs rulings regime, institution of a review and appeals process for customs decisions, and improvement of customs processing. To achieve these objectives, the United States has proposed that (1) the customs procedures chapter require all FTAA countries to make publicly available information regarding customs laws, regulations, guidelines, procedures, and rulings; (2) countries be required to provide a system for issuing advance rulings before importing a good, including determinations of tariff classification, customs valuation, or country of origin; and (3) a two-step entry process separate the release of merchandise from final payment of duty, thereby reducing time and costs associated with processing.

The FTAA negotiators have much work to do to reach consensus on customs procedures. Some countries reportedly view many of the proposals in the draft text as too politically sensitive, (e.g., proposals on anticorruption measures); others as technologically inappropriate for some nations to adopt (e.g., automation); and others as too burdensome.

## Standards and Technical Barriers to Trade

Standards and technical barriers to trade can be very significant to exporters because, despite tariff elimination, products still may be denied access if they fail to meet certain technical requirements. The WTO Agreement on Technical Barriers to Trade preserves the rights of countries to apply restrictions on imports for human health, safety, or environmental reasons while establishing procedures for avoiding measures that discriminate against imports unnecessarily. FTAA countries must decide if they want to apply additional rules in this area through the FTAA agreement. New rules may impact the balance between domestic regulatory interests and the elimination of trade barriers. The United States has not yet submitted a proposal in this area because it continues to develop its position on whether certain new disciplines would be appropriate. Proposals in the draft text are numerous and diverse and

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reflect FTAA countries' domestic perspectives on regulation. Countries may decide that additional rules are useful for expanding existing WTO commitments or that additional notifications and consultations are necessary when such measures involve FTAA partners.

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## Next Steps

During the current 18-month negotiation phase, the market access group will face a challenging workload, including negotiating the schedules of tariff elimination, drafting detailed rules of origin, and reducing differences in the draft text on the market access rules. Ministers specifically tasked the group at the April 2001 Ministerial to complete the hemispheric database on current applied and bound tariff rates by November 1, 2001;

- compile a preliminary inventory of nontariff measures along with a methodology for removing them by April 1, 2002;
- intensify negotiations on a safeguard regime and submit a report on their progress to trade ministers by April 1, 2002;
- decide the methods and modalities for negotiating the tariff schedules and rules of origin by April 1, 2002; and
- begin negotiations on tariff schedules and rules of origin by May 15, 2002.

The hemispheric database and preliminary inventory will provide negotiators with information on each country's current tariff and nontariff barriers that will be used in negotiating their elimination. The trade ministers also instructed the market access group to coordinate with the negotiating group on agriculture since both groups will be negotiating the modalities and country-specific schedules to eliminate tariffs on their respective products.

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## Agriculture

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### Topic, Importance, and Negotiating Mandate

Agriculture is one of the most hotly debated issues in the FTAA negotiations. According to the U.S. Secretary of Agriculture, the FTAA could expand U.S. agricultural exports to the hemisphere by more than \$1.5 billion annually. The U.S. Department of Agriculture's Economic Research Service estimates that an FTAA could increase agricultural exports and imports and increase agricultural income for almost every FTAA country. FTAA countries view agriculture as a top trade priority, with each

maintaining offensive and defensive interests. The United States, for example, would like to see increased access to South American grain markets but maintains high tariffs on sugar and orange juice and provides U.S. farmers with domestic support payments on a number of products. Chile, on the other hand, does not provide its farmers with domestic supports<sup>6</sup> but maintains a price band system for wheat, wheat flour, vegetable oil, and sugar that is designed to insulate domestic markets from international price fluctuations.

FTAA agriculture negotiators seek to move beyond WTO obligations in the hemisphere by further reducing and eliminating tariffs and nontariff barriers, eliminating export subsidies, addressing other trade-distorting practices, and facilitating the implementation of the WTO sanitary and phytosanitary (SPS) agreement.<sup>7</sup> The Negotiating Group on Agriculture, established by the San José declaration, was given several mandates to meet these goals. Because the agriculture and market access groups are closely related, the ministers decided that the objectives of the market access group should also apply to the negotiating group on agriculture. This means that the agriculture group will work to progressively eliminate tariffs and nontariff barriers, all agricultural tariffs will be subject to negotiation, and different trade liberalization timetables may exist. However, ministers agreed that rules of origin, customs procedures, and technical barriers to trade involving agriculture would be addressed solely in the market access group. The agriculture group was also mandated to (1) eliminate agricultural export subsidies affecting trade in the hemisphere, (2) identify and address other trade-distorting practices for agricultural products, and (3) ensure that SPS measures are applied consistently with the WTO SPS agreement. (See ch. 5 for more information on the economic impact of tariff reductions for agricultural products.)

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## Progress to Date

To date, the agriculture group has prepared a 45-page draft text that presents a range of proposals on market access for agricultural goods,

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<sup>6</sup>Domestic supports are payments made to farmers that raise or guarantee prices or income. They include such measures as market-price support programs, loan deficiency payments, and commodity loan programs.

<sup>7</sup>The SPS agreement under the WTO establishes rules on member countries' measures to protect the life and health of humans, animals, or plants. Under the agreement, such measures must be based on a scientific assessment of risk and should not be applied arbitrarily or in a way that constitutes a disguised restriction to trade.

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export subsidies, other practices that distort trade in agriculture, and SPS measures. The group is working toward agreement on this draft text and must also prepare schedules for the reduction of agricultural tariffs, nontariff barriers, export subsidies, and other trade-distorting practices. Before they can begin negotiations on the schedules, they must decide how to conduct these negotiations.

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## Significant Issues

The agriculture group faces four significant issues. FTAA countries have not agreed on whether the agreement will address domestic supports. They also have not determined whether sensitive agricultural products will receive exceptions in the tariff negotiations. While FTAA countries have agreed to eliminate export subsidies within the hemisphere, they have not determined how to address third-party export subsidies. Finally, while all FTAA countries seek the full implementation of the WTO SPS agreement, they have not agreed on how to treat it within the text of the FTAA.

One controversial issue within the agriculture group is the issue of whether to include domestic support programs in the negotiations on other trade-distorting measures.<sup>8</sup> Some countries have proposed that the FTAA go beyond the current WTO agreement on agricultural domestic supports by reducing and eliminating some supports that are currently permitted.<sup>9</sup> These countries feel that that much of their trade protection comes in the form of tariffs, and, if they eliminate tariffs, their products would be disadvantaged in the face of subsidized products. Brazilian officials have been particularly vocal on the issue of domestic supports, declaring that the negotiations could not proceed if the United States refuses to address domestic support programs. The United States, however, has publicly stated that commitments to domestic support reduction can only be achieved in multilateral negotiations, such as those in the WTO. U.S. negotiators argue that because U.S. competitors, such as the EU, employ such supports, reducing them in the FTAA instead of the WTO would amount to unilateral disarmament. At least one other country has a similar position on this issue. This impasse has led several FTAA experts to conclude an FTAA agreement on agriculture will depend on progress made in addressing domestic support in the WTO.<sup>10</sup>

Once the agriculture group begins tariff and nontariff negotiations, negotiators must determine how to handle each country's sensitive sectors. There has been no discussion on specific agricultural products beyond the San José declaration, which states that all products will be subject to negotiation. Two FTAA experts reported that they expect certain products will receive special treatment in the negotiations, such as longer phase-out

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<sup>8</sup>The draft text on other trade-distorting practices also contains proposals that seek to reduce or eliminate export taxes and state trading enterprises.

<sup>9</sup>The WTO agriculture agreement classifies agricultural domestic support measures into three categories identified by "boxes": green (permitted), amber (reduce), and blue (production limiting programs). For the WTO, most of the domestic support measures considered to distort production and trade fall into the amber box. Thirty WTO members, 8 of whom are FTAA participants (Argentina, Brazil, Canada, Colombia, Costa Rica, Mexico, the United States, and Venezuela), have commitments to reduce their trade-distorting amber box supports. One proposal within the FTAA draft text would eliminate some of these supports.

<sup>10</sup>The Uruguay Round agreements set up a framework of rules and began reductions in protection and trade-distorting support. Article 20 of the agriculture agreement committed members to begin negotiations on further reforms at the end of 1999. These negotiations are now in their second phase. Further substantial reductions in tariffs, domestic support, and export subsidies are prominent issues in the negotiations.

periods or outright exceptions to tariff elimination. Others have stated that they oppose exceptions to tariff elimination for agricultural products. The issue of product exceptions will be controversial because many of the products that are sensitive to one country are strong exports for another. For example, Brazil has called for increased access to the U.S. orange juice market and is a major producer of sugar, two products for which the United States maintains relatively high tariffs. However, both industries have asked U.S. negotiators to exclude their products from the negotiations. In addition, portions of the U.S. fruit, vegetable, and beef industries have requested some degree of product exception.

Although ministers have agreed to eliminate export subsidies in the hemisphere, they have not reached agreement on how to handle third-party export subsidies, nor have they agreed on what constitutes an export subsidy. If they eliminated their own subsidies within the hemisphere, they would face a disadvantage in the face of third-party countries that use export subsidies on products coming into the hemisphere. Similarly, FTAA countries disagree on whether they need to create rules on the use of export subsidies outside of the hemisphere. Solutions proposed so far have included negotiating with third parties not to apply their subsidies, suspending tariff preferences, and allowing for the option of fines if export subsidies are used in either of these situations. Some FTAA countries want to go beyond the definition of an export subsidy currently used by the WTO agreement on agriculture to include other programs, such as export credits, credit guarantees, insurance programs, and food aid. The United States, however, has proposed using the WTO definition of export subsidies. The United States does not want export credits; export credit guarantees or insurance programs, when provided in a manner consistent with WTO rights and obligations; and international food aid to be considered to constitute export subsidies for purposes of the FTAA, but it does call for the staged elimination of exclusive export rights granted to state trading enterprises (such as the Canadian Wheat Board).

FTAA countries have agreed to fully implement the WTO SPS agreement but have not agreed on how best to accomplish that goal. Some countries have put forward proposals that would include a detailed rewrite of the WTO SPS agreement in the FTAA text. Instead, the United States has proposed that FTAA countries agree to strengthen collaboration on matters within the purview of the WTO SPS committee and relevant international bodies. The United States also seeks agreement from FTAA countries to exchange information on new research data and risk assessment procedures and to coordinate technical assistance. In addition, several

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U.S. agriculture groups have identified SPS issues that they would like addressed within the context of an agreement. For example, the National Cattlemen's Beef Association has called for the full eradication of foot-and-mouth disease in the hemisphere.

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## Next Steps

Ministers directed the agriculture group to undertake several actions in the next negotiating phase, including establishing modalities for market-opening negotiations, beginning the market access negotiations, and intensifying efforts to resolve differences in the draft text. Among other things, ministers instructed the group to

- develop recommendations on the modalities for tariff negotiations by April 1, 2002, in order to begin these negotiations by May 15, 2002;
- accelerate the process of identifying nontariff measures so as to have, by April 2002, a preliminary inventory of such measures;
- submit recommendations on the scope and methodology for eliminating export subsidies affecting trade in agricultural products in the hemisphere by April 1, 2002;
- make recommendations on the types of measures and a methodology to develop disciplines on the treatment of all other practices that distort trade in agricultural products by April 1, 2002;
- establish a notification and counter-notification for SPS measures by April 2002 and develop mechanisms to facilitate the full implementation of the WTO SPS agreement; and
- submit a new version of the draft text by August 2002.

According to FTAA experts, many similar proposals in the text could be consolidated during this negotiating phase. This could result in a text that has more clearly stated positions by next August. Still, these experts believe that while the group may be able to negotiate away many of the brackets by consolidating and eliminating redundancies, it is doubtful that they will be able to resolve the major issues.

Finding common ground on the methods and inventories for negotiating export subsidies and other trade-distorting practices, including domestic supports, may be challenging. Latin American countries are looking for some progress on export subsidies in April 2002 before they proceed with the tariff negotiations. Specifically, they would like to see a commitment from the United States to negotiate domestic support.

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## Services

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### Topic, Importance, and Negotiating Mandate

As the world's leading exporter of services (\$253 billion in 1999) and with its market for services relatively open,<sup>11</sup> the United States has a broad interest in liberalizing services trade across most sectors. The FTAA negotiations include a range of service sectors, including telecommunications, financial, professional, distribution, and travel and tourism services. Although the services negotiating group has made progress, substantive negotiations lie ahead on key topics, including the scope, structure, and timing of market-opening commitments.

Many FTAA countries have just begun to liberalize their service sectors, and most have made limited multilateral commitments to open their markets. For example, an OAS study found that, except for Argentina, Canada, and the United States, all other countries in the FTAA made moderately low to very low service commitments in the WTO. However, many service sectors, such as telecommunications and distribution, are important to a domestic economy's overall productivity and development. Liberalizing these service sectors can foster greater competition and efficiency. Some countries, such as Argentina, Brazil, and Venezuela, have privatized previously state-owned service monopolies as part of their economic reform plans, and some subregional trade agreements, such as those among Mercosur and the Andean Communities countries, call for negotiations to liberalize services trade. FTAA trade ministers agreed that the mandate of the negotiating group on services is to establish disciplines that will progressively liberalize trade in services and create a free trade area under conditions of certainty and transparency. (See ch. 5 for more information on the economic impact of hemispheric services liberalization.)

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### Progress to Date

Over the 18 months leading up to the ministerial of April 2001, the services negotiators compiled a 38-page draft text of proposals covering the scope and provisions of the services chapter of the agreement. The draft text

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<sup>11</sup>Although generally maintaining a liberal environment for services, the United States also maintains some restrictions in the transportation sector, especially coastal shipping policies, as noted in its WTO and NAFTA commitments. Also, Brazil recently pointed to some restrictions in insurance, banking, and telecommunications that hampered its firms.

contains several broad topics that will be included in the agreement (such as provisions on most-favored nation and national treatment), but the specific disciplines and final language still must be negotiated. The draft text also includes proposals on numerous other topics that at least one country had recommended including in the final chapter. These additional topics include safeguards, subsidy provisions, general or security exceptions to the rules, and special rules for domestic regulations. In addition to the rules for services trade, the services group also will need to complete individual country schedules of market access commitments. In these schedules, each country will describe what they pledge to do to liberalize specific sectors and what reservations to the general rules they propose to take for individual sectors or measures.

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## Significant Issues

To produce a chapter with the rules for services trade and the individual countries' schedules of commitments, negotiators face several challenges. One such challenge negotiators face involves the scope of the services chapter. In the WTO services agreement, the coverage includes both a cross-border supply of services and the supply of a service by a company with a commercial presence in another country's market. Companies can establish a commercial presence by investing, but unlike the WTO, the FTAA has a separate negotiating group on investment (discussed below). The United States wants to deal with services-related investment primarily in the investment chapter. However, the current draft text contains other proposals that would include the commercial presence of a service provider under the scope of the services chapter.

Negotiators will need to reconcile other scope-related issues, including (1) the ways in which services provisions in the agreement apply to subnational levels of government and (2) the timing for developing additional disciplines for sectors, such as telecommunications or specialized provisions for financial services. The WTO already has additional agreements on basic telecommunications and financial services, but not all FTAA countries are signatories or have fully adopted these agreements.<sup>12</sup> The United States has recommended that there be

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<sup>12</sup>Twenty Latin American and Caribbean countries have made commitments under the Basic Telecommunications agreement, with most agreeing to adopt at least part of the reference paper on procompetitive regulatory principles, according to an OAS study. About 15 Latin American and Caribbean countries submitted newly improved schedules on financial services.

specialized provisions for financial services partly because of the regulatory issues related to the sectors' importance to the overall economy.

Negotiators also must address the structure of the market access schedules of commitments that each country will negotiate. There are two approaches to scheduling services commitments: a top-down "negative list" approach and a bottom-up "positive list" approach. In a negative list, all service sectors are subject to the core rules, and countries must then indicate which sectors or measures they would seek to exclude from coverage. For example, a services agreement may have a "national treatment" provision that foreign service providers will be treated at least as well as domestic service providers. If a country intends to subject foreign service providers in the insurance industry to additional regulations, then it would need to take an exception to the national treatment rule. The positive list approach works the opposite way. A country specifies in its schedule only the commitments it plans to make. If a sector is not included in the schedule, then it is not covered by the agreement. The WTO General Agreement on Trade in Services generally follows a positive list approach, and NAFTA follows a negative list approach.

The United States advocates using the negative list approach in the FTAA services chapter, arguing that it is ambitious but allows countries the flexibility to deal with domestic sensitivities (by scheduling reservations). Other FTAA countries, however, have proposed using a positive list approach or some variant. Although most major subregional agreements in the Western Hemisphere have used a negative list, Mercosur used a positive list approach for its services liberalization. Business representatives throughout the hemisphere that met at the April ministerial were split over whether the FTAA should use a positive or negative list approach. Some U.S. civil society and labor groups oppose using a negative list approach because they believe it later may limit government social policies if exceptions for particular sectors are not built into the agreement. They are concerned that countries could use a comprehensive services agreement to challenge government provision of social services, such as health and education, if those services compete with private sector firms. USTR has stated that it does not intend to use the FTAA to promote the privatization of social services.

Negotiators will also have to agree on the timing of liberalization to be achieved through the market access commitments. Countries will begin in May 2002 to negotiate the schedules of commitments to allow access into their markets. Since this phase has not yet begun, countries generally have not revealed their goals nor is it clear how difficult it will be to resolve differences. However, U.S. service companies are considered some of the most competitive in the world, and some FTAA countries may be concerned about the final commitments they will make and the speed at which liberalization will take place. Related to this, the draft text includes potential language on a safeguard mechanism for services.<sup>13</sup> A safeguard measure may provide negotiators some incentive to commit to greater liberalization because they will have a mechanism to ease potentially adverse effects. The negotiators' mandate calls for the progressive liberalization of trade in services, but achieving this may be difficult for two reasons. First, services involve domestic regulatory and qualitative provisions that may in practice restrict foreigner's access to markets. Given these domestic regulations, free market access may be hard to define. Second, countries may differ on whether to "progressively liberalize" services means to achieve full liberalization through one round of negotiations or through a series of rounds in future years, which would be scheduled in the agreement. Some subregional agreements, including Mercosur, have used successive rounds of negotiations, while NAFTA countries liberalized services through a single agreement. In addition, some members of subregional agreements are attempting to preserve preferences under those agreements from the scope of the FTAA liberalization.

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## Next Steps

During the current 18-month phase of negotiations, the services group will try to bridge differences in the draft text of proposed rules. These will include refining the text in agreed-upon areas of negotiation, such as most-favored nation and national treatment provisions, and deciding which additional subjects the agreement should cover. Simultaneously, negotiators will seek agreement on the modalities for negotiating specific country schedules of commitments by April 1, 2002, for negotiations set to begin May 15, 2002. These decisions include whether to use a positive or negative list approach, the structure of the schedules (i.e., the format), and the process to use in negotiating country commitment offers.

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<sup>13</sup>The WTO General Agreement on Trade in Services Agreement does not have a safeguard measure but does discuss the possibility of future negotiations on a safeguard measure.

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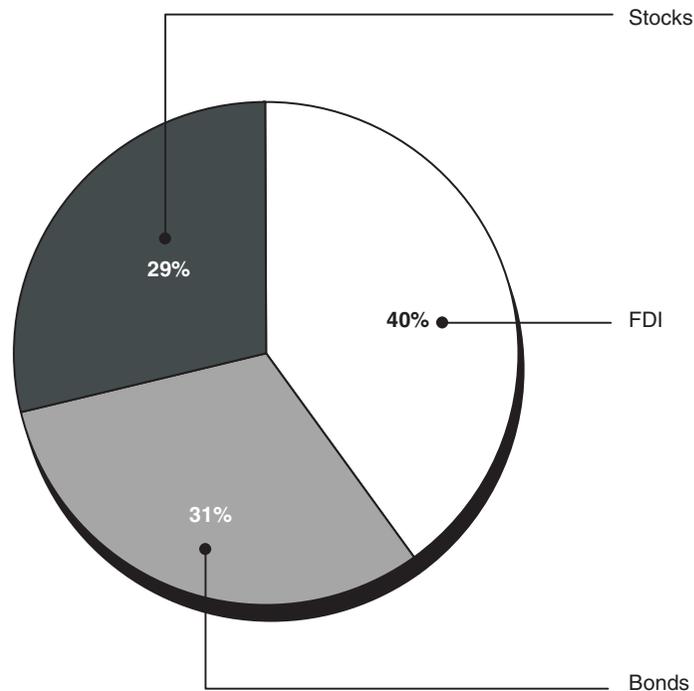
## Investment

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### Topic, Importance, and Negotiating Mandate

Although many outstanding details still need to be resolved, FTAA negotiations on investment have yielded broad agreement on the thrust of the chapter and the types of investment protection that the investment chapter will address. However, the breadth of the forms of investment that will be covered and whether the establishment or entry of investment will be covered remains controversial. Consistent with the agreed mandate for the negotiation, the United States proposes a comprehensive agreement that covers both entry and operation of investment and direct and portfolio investment. Portfolio investment, both stocks and bonds, is commercially important for the United States, accounting for 60 percent of the \$661 billion U.S. investment in FTAA countries in 1999. Figure 6 shows the relative shares of U.S. FTAA investments in foreign direct investment (FDI), stocks, and bonds. However, some other countries reportedly believe this comprehensive approach is too broad. The investment chapter is also where the outcome of internal U.S. debates could make it more or less difficult to reach an overall FTAA agreement. The debates center on two issues—the extent of the ability of investors to challenge government actions as contravening FTAA investment disciplines and the inclusion of labor and environmental provisions in the text of an FTAA.

**Figure 6: Share of U.S. Foreign Direct Investment and Portfolio (Stock and Bonds) Investments in FTAA Countries, 1999**



Source: GAO analysis of U.S. Department of Commerce data.

As one of the largest foreign investors in Latin America, with investment growing sharply in recent years, the United States has a keen interest in FTAA negotiations on this issue. Some U.S. investment is subject to conditions that hinder efficiency, and much of it is not protected by international agreements. For example, the United States has bilateral investment treaties in force with only 8 of the 33 other FTAA participants. NAFTA protects U.S. investment in another two FTAA participants (Canada and Mexico). But the United States does not have agreements with countries such as Brazil, the largest Latin American nation. Although unilateral liberalization of investment regimes has occurred, it could be reversed in the absence of international agreements. In addition to better protection of U.S. investors, an FTAA could further liberalize investment regimes and improve U.S. options for serving growing local markets throughout the hemisphere.

Other FTAA participants see FTAA investment rules as a way to send a positive signal to foreign investors, which they seek to attract to foster economic growth and stimulate competition and technology transfer. An investment agreement could set basic ground rules for entry and treatment of investment, increasing certainty, and lowering risk for potential investors. Companies from Chile, Mexico, and elsewhere in Latin America are also beginning to invest abroad. Indeed, the smaller nations in the region are reportedly the key drivers for an ambitious investment accord within the FTAA.

FTAA investment negotiations aim to go beyond the WTO's coverage of the issue, which is limited,<sup>14</sup> and to build upon subregional agreements such as NAFTA, which contains extensive investment disciplines with respect to the United States, Canada, and Mexico. Such an investment agreement could commit the parties to open their market to investment from elsewhere in the hemisphere, set minimum standards of treatment for investors, and establish mechanisms for the resolution of disputes.

The mandate of the negotiating group on investment, as established by the San José Ministerial Declaration, is to “establish a fair and transparent legal framework to promote investment through the creation of a stable and predictable environment that protects the investor, his investment and related flows, without creating obstacles to investments from outside the hemisphere.” The group is to develop (1) a framework incorporating comprehensive rights and obligations on investment and (2) a methodology to consider potential reservations and exceptions to the obligations.

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## Progress to Date

The negotiating group has produced a 43-page draft FTAA chapter on investment that incorporates the proposals received to date from FTAA participants. The draft chapter addresses a number of issues, including:

- scope of application;
- standards of treatment (national treatment, most-favored nation treatment, and a minimum or general standard of treatment);
- performance requirements;

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<sup>14</sup>The WTO's primary investment disciplines are found in the Agreement on Trade-Related Investment Measures, known by its acronym “TRIMS,” and the General Agreement on Trade in Services, which includes commercial presence as a “modes of supply” of services listed in national schedules of market access commitments.

- key personnel;
- transfers;
- expropriation and compensation;
- compensation for losses;
- general exceptions and reservations;
- dispute settlement, which accounts for 16 of the draft's 43 pages;
- basic definitions, including of investment and investor;
- transparency of laws and regulations; and
- commitments not to relax labor and environmental laws to attract investment.

The Tripartite Committee has also produced a compendium of investment agreements, a comparison of investment regimes, and annual reports on investment flows.

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## Significant Issues

Discussions to date reportedly reveal broad agreement among FTAA governments about many basic investment disciplines. In part, this is due to the foundation laid in more than 60 bilateral investment treaties by countries within the region and various subregional agreements. These agreements have established common approaches to defining investment and investor, setting standards of treatment for investors, and settling disputes. As a result, key participants report that the broad outlines of an FTAA agreement on investment are visible. However, several topics appear likely to be controversial or otherwise important in the negotiations and many other details must be resolved. The investment chapter has also fueled debate on two issues that are controversial domestically—the ability of investors to challenge government actions as contravening FTAA investment disciplines, and the inclusion of labor and environmental provisions in the FTAA. The outcome of these debates ultimately could affect the willingness of FTAA countries to conclude an overall agreement.

Investment is a lightning rod for opposition to the FTAA by U.S. environmental, labor, and consumer nongovernmental organizations, which are concerned that investment rules could undermine a government's ability to act in the public interest. The FTAA's draft investment rules have already drawn fire from such organizations, largely on the grounds that multinational corporations may be given too much power relative to governments and citizens. Their biggest concern is over the prospect that private investors would be given direct access to investor-state dispute settlement to challenge government noncompliance with the FTAA.<sup>15</sup> Governments can be required to pay the investor monetary damages if the investor's complaint is upheld by a final award. Such investor-state provisions have been widely embraced under NAFTA and bilateral investment treaties in effect throughout the world<sup>16</sup> and are favored by U.S. business as an efficient and impartial means for enforcing their rights, in lieu of local court systems, which might be very slow or otherwise deficient.<sup>17</sup> Although tribunals have no authority to recommend or require changes to domestic legislation that violates the provisions, proceedings brought under NAFTA have provoked concerns that such challenges could undermine a government's ability to protect health, safety, and the environment; affect the balance between federal and state control; and sideline U.S. courts in favor of international arbitration.<sup>18</sup>

FTAA investment negotiations are also the epicenter for another topic that has been controversial domestically, the treatment of labor and the environment in an FTAA. A U.S. proposal to include provisions on labor

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<sup>15</sup>Investor protections that entitle investors to compensation for measures "tantamount" to expropriation and require signatories to accord a minimum standard of treatment, apart from nondiscrimination, including "fair and equitable treatment," have also proved controversial, under NAFTA for example.

<sup>16</sup>For a description of NAFTA's investor-state dispute settlement mechanism, see *North American Free Trade Agreement: U.S. Experience with Environment, Labor, and Investment Dispute Settlement Cases* (GAO-01-933, July 20, 2001).

<sup>17</sup>For a discussion of this business perspective, see statement of Daniel M. Price, Member United States Council for International Business, Testimony Before the Subcommittee on Trade of the House Committee on Ways and Means, Hearing on Summit of the Americas and Prospects for Free Trade in the Hemisphere, May 8, 2001, available at [www.uscib.org](http://www.uscib.org).

<sup>18</sup>For a discussion of these concerns, see, for example, The Center for International Environmental Law, *Environmental Protection and Investment Rules in the Free Trade Area of the Americas* (Feb. 2001) and International Institute for Sustainable Development, *Private Rights, Public Problems*, Winnipeg, Canada (2001), available at [www.ciel.org](http://www.ciel.org) and [www.iisd.org](http://www.iisd.org), respectively.

and the environment in the FTAA investment chapter revealed deeply held and divergent opinions among FTAA participants on the overarching question of whether an FTAA should include labor and environmental provisions at all, and, if so, how they would be enforced. The United States remains divided domestically on this issue. Late in 2000, the United States tabled language similar to NAFTA stating that countries agree not to relax environmental or labor standards to attract investment. However, strong opposition from most other FTAA nations on the grounds that labor and environmental provisions were “off the table” in FTAA negotiations resulted in the initial exclusion of this proposal from the draft chapter. The controversy prompted a call for guidance. At their April 2001 meeting in Buenos Aires, FTAA ministers decided that “any delegation has a right to make proposals it deems relevant for the effective progress of the process, which may eventually be placed in brackets” (signifying that the language contained therein is not agreed on).

Within the FTAA negotiating group on investment, coverage is an important and difficult issue. One question is whether the agreement will only cover treatment of investment once admitted or include a general “right of establishment” obliging governments to permit investment to enter. Consistent with the goal of obtaining a comprehensive agreement, the United States proposed that nondiscriminatory treatment apply to the “preestablishment” phase of investment, which would, except where parties negotiate reservations for sensitive sectors, effectively accord the signatories’ investors the right to establish, acquire, or expand an investment on an equal footing with domestic and other foreign investors.<sup>19</sup> Other FTAA participants also support covering the preestablishment phase. However, even though many FTAA nations have unilaterally liberalized foreign investors’ entry, some are reluctant to guarantee a general right of establishment to foreign investors in an FTAA.

Another difficult issue is whether and how to cover portfolio investment. A majority of countries, including the United States, have proposed a broad, asset-based definition of investment that includes portfolio investment,<sup>20</sup> some contracts and concessions, and intellectual property. However, they

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<sup>19</sup>NAFTA, U.S., and Canadian bilateral investment treaties, and most free trade agreements negotiated in the region take this approach of allowing free entry, subject to specific reservations.

<sup>20</sup>Portfolio investment includes stocks, bonds, debt instruments, futures, options, and other derivatives.

differ on the specific details of this definition. For example, some propose to narrow the definition to exclude speculative and certain other transactions and to allow governments to limit transfers if problems arise. Given the Asian financial crisis and concern that short-term fluctuations in capital flows contribute to currency fluctuations and balance of payments crises, certain nations oppose covering portfolio investment in the definition at all. Other countries propose addressing this concern by providing an exception to the transfers protections for these situations, rather than foreclosing portfolio investment from all protections of the agreement.

Approaches to performance requirements also differ. Performance requirements—such as local content, trade balancing, local hiring or management, and technology transfer requirements—are sometimes conditions for obtaining incentives or benefits from the host government and can also be conditions for establishing an investment. The United States proposes to go beyond the WTO Trade-Related Investment Measures or "TRIMS" agreement and current bilateral investment treaties<sup>21</sup> in prohibiting (subject to certain exceptions)<sup>22</sup> several such performance requirements and is proposing disciplines similar to NAFTA. NAFTA and the U.S. FTAA proposal discipline certain performance requirements whether they are tied to an advantage or imposed as a condition for establishment. Other performance requirements, such as technology transfer, are only disciplined when they are a condition for establishment. Other FTAA participants also want to go beyond the WTO, but still others want to be able to employ such tools, which they see as important to promoting development.

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## Next Steps

The negotiating group on investment has been charged to come up with a second draft of its chapter by August 2002. In addition, it is also to present recommendations on negotiating modalities and procedures to the TNC by April 1, 2002. The TNC is to evaluate the negotiating group's

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<sup>21</sup>The TRIMS agreement explicitly disciplines a limited number of performance requirements, whether they are imposed as a condition for establishment or are a condition for the receipt of an advantage. U.S. bilateral investment treaties do not discipline performance requirements when they are a condition for receipt of an advantage.

<sup>22</sup>However, it has proposed exceptions, such as for measures necessary to protect human, animal, or plant life and to remedy competition problems; for government procurement; and for aid and export promotion programs.

recommendations on modalities at its first meeting after April 1, 2002, to initiate investment coverage negotiations no later than May 15, 2002.

There are two basic modality issues. One is the approach that will be taken to negotiating coverage. The United States is expected to propose a “top-down” or negative list approach to coverage, which starts from the premise that all sectors are covered unless specifically reserved or excepted. The alternative is a “bottom-up” or positive list approach, which starts from the assumption that nothing is covered and builds up from there by identifying covered sectors. Both methods could result in similar levels of market access commitments initially because a member would be expected to include a reservation in a negative list approach for any sector in which it declines to take commitments under a positive list approach. However, the choice of approach might have implications for future investment access. Under a negative list approach, new investment measures would have to conform (unless they fell within one of the general exceptions enumerated in the FTAA). Under a positive list approach, new discriminatory measures would be allowed in sectors or areas not included in members’ schedules. The second issue is the form that reservations will take. NAFTA bases reservations and exceptions primarily on existing law, permitting exceptions for sectors on a limited basis. In contrast, U.S. bilateral investment treaties except broad sectors. Again, the degree of specificity could have implications for future access.

The negotiating group on investment will need to coordinate with the FTAA negotiating group on services as it performs these tasks. The United States has proposed that the FTAA investment chapter apply to all investment, whether it relates to a good or a service. Because some services are provided through investment and others are provided through cross-border trade, how the issue of taking reservations is handled in both the investment and services chapter will be important to determining the ground rules for service providers in the hemisphere.

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## Government Procurement

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### Topic, Importance, and Negotiating Mandate

Government procurement in the FTAA negotiations offers potentially great market-opening opportunities for the participants. The OAS estimates that the market for government procurement in the Western Hemisphere is valued at approximately \$250 billion. U.S. observers are encouraged by potential market-opening possibilities in this area because most FTAA countries are not bound by international rules on government procurement. In addition, outside of North America, many FTAA countries have limited experience with international government procurement regimes. This is because, unlike other negotiating groups, the FTAA government procurement negotiations do not proceed from a commonly applied WTO agreement.<sup>23</sup>

At the FTAA San José Ministerial, the trade ministers formed the negotiating group on government procurement with the mandate to expand access to the government procurement markets of FTAA countries. More specifically, ministers directed the group to (1) achieve a framework to ensure transparency of government procurement processes, without necessarily implying an identical system for each country; (2) ensure nondiscrimination in government procurement; and (3) ensure impartial and fair review for resolving procurement complaints and appeals by suppliers.

The FTAA government procurement regime may be similar to other multilateral agreements, such as the WTO Government Procurement Agreement or NAFTA, which cover the terms of contracts for a wide range of goods and services. Under these agreements, the entities or enterprises to be covered are specified, as are minimum purchase values, called

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<sup>23</sup>Government procurement is addressed in the WTO by the Government Procurement Agreement, a “plurilateral agreement,” which means that accession to the agreement is voluntary. Only the United States and Canada of all FTAA countries are currently party to the Government Procurement Agreement. They, along with Mexico, are also subject to government procurement disciplines under NAFTA. Mexico also has NAFTA-like commitments with Costa Rica. An agreement between Chile, Costa Rica, El Salvador, Guatemala, and Honduras contains principles-based procurement commitments. Other Western Hemisphere subregional agreements, such as Mercosur and the Andean Pact, do not currently have binding market access provisions on government procurement.

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thresholds. Generally, the higher the number of entities and enterprises covered by an agreement and the lower the threshold, the more liberalizing the agreement.

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## Progress to Date

Although FTAA government procurement negotiations will begin to address market access concessions in the upcoming phase of the negotiations, the bulk of the 34-page draft text submitted by the negotiating group to the ministers in Buenos Aires focuses on ways to conduct the procurement proceedings. The text includes proposed language on a wide range of rules and technical matters, including

- the application of principles such as national treatment and most-favored nation treatment;
- special and differential treatment for smaller economies;
- the thresholds and valuation of contracts;
- procurement exceptions;
- publication of laws and rules governing procurement processes;
- specific procurement procedures, including the qualification of suppliers;
- the process for selecting and awarding contracts; and
- review and appeal procedures, including dispute settlement.

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## Significant Issues

One aspect of the negotiation-transparency<sup>24</sup> is significant for government procurement and is addressed in the draft text. According to IDB, government procurement has been considered a nontariff barrier due to the tendency to award contracts to national firms rather than to make decisions that are based only on price and quality. This tendency has resulted in an inefficient and sometimes corrupt process. Government procurement experts believe that an agreement that is transparent in its explication of procedures and its means to verify the application of rules provides a variety of benefits. For example, a transparent agreement renders fraud and corruption more difficult. It would also enhance the opportunity for competition in bidding, resulting in higher quality procurements and budgetary savings to governments. The United States is seeking an FTAA that would require publication and wide dissemination of

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<sup>24</sup>Transparency in this context refers to both the clarity of government procurement rules and procedures and the means by which procurements are made known to the public.

all laws, regulations, judicial decisions, and other measures governing government procurement.

Negotiators will have to resolve differences in two basic approaches to the government procurement chapter. One approach, backed by the United States, is rules-based, which would rely on detailed procedural provisions while avoiding unnecessarily burdensome requirements. The United States and other parties to the Government Procurement Agreement and NAFTA have considered that this approach is necessary because of the nature of government procurement, which can be influenced by government policy and politics, in addition to commercial considerations. As a result, the United States believes that, to enjoy the concessions that will be negotiated, the agreement must include specific procedural provisions on topics such as the publication of timetables and tendering procedures as found in both NAFTA and the Government Procurement Agreement. However, other countries prefer a principles-based approach to the FTAA government procurement chapter, which would rely on more general guidelines. Proponents of this approach argue that it is better to make a basic commitment to nondiscrimination but not prescribe specific procedures that all of the parties are to follow. It would thus be up to the local authorities to develop their own procedures. An advocate of this approach noted that no degree of specificity would prevent a country determined to avoid compliance from doing so, and that ultimately good faith in applying the principles has to be relied on. If discrimination was found, a challenge could still be brought under the dispute settlement provisions.

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## Next Steps

To move forward with government procurement negotiations, ministers at Buenos Aires instructed the government procurement group to

- submit recommendations to the TNC by April 1, 2002, on the guidelines, procedures, and deadlines for negotiations so that the negotiation of concessions can begin no later than May 15, 2002, and
- submit a new version of the draft text of the government procurement chapter to the TNC by August 2002.

The ministers also provided a directive to the government procurement negotiators to identify, by April 1, 2002, the scope and details of the statistical information that the countries should exchange with each other and use to support their negotiations. This directive was issued because some delegations felt it would be necessary in order to prepare for an

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exchange of statistical data on their government procurement markets before commencing the market access negotiations. On the basis of the ministerial directive, the negotiators must decide on the statistical systems and entity lists they need to undertake the negotiations. For example, there is no point in requiring statistical information on procurement by every government agency in the hemisphere before the FTAA governments have a clearer understanding of the likely scope of the market access negotiations, according to USTR.

# Other Rules and Institutional Provisions

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FTAA negotiators are also developing trade rules and institutional provisions for four other topics: IPR; subsidies, antidumping, and countervailing duties; dispute settlement; and competition policy. Negotiating groups have prepared draft chapters on their respective topics. Some issues under consideration in these groups are controversial. For example, FTAA participants have fundamental disagreements regarding IPR. The United States would like the FTAA to represent a state-of-the-art agreement that goes beyond the obligations of other relevant agreements. Some developing countries, on the other hand, are reluctant to go beyond their current obligations. FTAA countries' interests also diverge in the area of antidumping measures. A U.S. proposal to reserve its right to apply its trade remedies angered many other FTAA participants who want to curb the use of these measures. Other issues under consideration in these groups will require intense effort to finalize outstanding details. For example, FTAA participants must resolve dispute settlement issues such as compliance, appeals, and the participation of outside parties. Similarly, FTAA negotiators must determine the level of detail that the competition policy agreement needs to have to effectively proscribe anticompetitive business conduct. Table 2 provides an overview of the topics covered in this chapter. The remainder of this chapter describes each of these topics, its importance, and the group's negotiating mandate; progress to date; significant issues; and next steps. Information on the potential economic effect of trade liberalization for these topics can be found in chapter 5.

**Table 2: Overview of Negotiating Groups on Other Rules and Institutional Provisions**

Topic	Significance for the United States	Mandate	Next steps
Intellectual property rights (IPR)	Important to U.S. high-tech and knowledge-based industries.	Promote and ensure adequate and effective protection of IPR.	August 2002 - Submit revised text.
Subsidies, antidumping, and countervailing duties	Politically sensitive debate over trade remedy laws.	Enhance WTO compliance and improve application of trade remedy laws.	April 2002 - Submit recommendations on subsidies, antidumping, and countervailing duties. August 2002 - Submit revised text.
Dispute settlement	Linchpin of effective operation of overall agreement.	Establish a fair, transparent, and effective dispute settlement mechanism.	August 2002 - Submit revised text.
Competition policy	New area for 22 of the 34 participants.	Ensure that anticompetitive practices do not undermine FTAA benefits.	August 2002 - Submit revised text.

Source: GAO analysis.

## Intellectual Property Rights

### Topic, Importance, and Negotiating Mandate

According to the WTO secretariat, IPR is defined as the rights given to persons over the creations of their minds, such as a book or software program, usually providing the creator with an exclusive right over the use of his or her creation for a period of time. The goal is to reward creativity and to establish an environment conducive to the broad sharing of ideas. IPR is one of the most important issues to the United States because it enjoys a decisive competitive advantage in terms of high-tech, knowledge-based industries and advancing the interests of these industries in the FTAA through strengthening IPR could result in significant gains for the U.S. economy. U.S. software firms, for example, would benefit if FTAA nations agreed that their governments would use only legitimate software in their agency operations. On the other hand, developing countries want to include in IPR disciplines such as folklore, and traditional knowledge. Therefore, IPR negotiations clearly marks the vast differences in economic and technological interests of developed and developing countries.

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IPR negotiations in the FTAA promise to be challenging because FTAA nations have fundamentally divergent interests and have not, for a variety of reasons, made much progress on IPR negotiations. As a result, considerable work remains. Some of the topics under consideration are controversial or completely new to trade negotiations. The FTAA could go beyond the WTO and NAFTA by addressing technologies, treaties, and issues that have emerged since these landmark trade agreements were concluded in 1994 and 1993, respectively. For example, since then, industries such as biotechnology and e-commerce have emerged as commercially significant industries, a number of new IPR treaties have been concluded, and others are under negotiation.<sup>1</sup>

The specific mandate for the FTAA IPR negotiations as stated in the San José Ministerial is to reduce distortions in trade in the hemisphere and promote and ensure adequate and effective protection to IPR. The mandate notes in doing so, changes in technology must be considered.

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## Progress to Date

The IPR negotiating group has developed a 106-page draft chapter that compiles proposals from different FTAA nations involved on 15 topics: (1) trademarks, (2) geographical indications, (3) copyrights and related rights, (4) folklore, (5) layout designs of integrated circuits, (6) patents, (7) the relationship between the protection of traditional knowledge and access to genetic resources and intellectual property, (8) utility models, (9) industrial designs, (10) plant varieties, (11) undisclosed information, (12) unfair competition, (13) anticompetitive practices in contractual licenses, (14) enforcement of IPR, and (15) technical cooperation.

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## Significant Issues

A variety of factors have hindered progress in FTAA negotiations on IPR. First, some FTAA nations slowed progress in the previous phase of negotiations. In part, this was due to a fundamental reticence by some FTAA nations to go beyond their current obligations under the WTO Agreement on Trade-Related Aspects of Intellectual Property (TRIPS). Also, because of its importance to the overall FTAA package, which will be

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<sup>1</sup>The agreements concluded in or after 1994 include a trademark treaty, two copyright treaties dealing with challenges of digital technology, a convention on artistic and literary works, a new agreement on industrial designs, and a new patent treaty. Cesar Parga, "Intellectual Property Rights," in *Toward Free Trade in the Americas*, José Manuel Salazar-Xirinachs and Maryse Robert, Eds. (Washington, D.C.: Brookings Institution, 2001), p. 209.

a “single undertaking,” some nations reportedly tried to ensure that negotiations on IPR did not get ahead of negotiations on topics of more interest to them, such as agriculture or subsidies, antidumping, and countervailing duties, according to U.S. officials. Second, the subject of IPR is complex. Each area involves a different agency, specialty, or industry, which makes the negotiating environment challenging. Third, the interests of FTAA participants in IPR differ widely. The United States, the leading proponent in FTAA IPR negotiations, is pushing for a state-of-the-art IPR agreement that reflects changes in technology, improved international rules, and better enforcement. The U.S. proposal for the FTAA chapter on intellectual property goes beyond the obligations that the United States and most FTAA countries have undertaken through the TRIPS agreement. It would extend NAFTA disciplines to countries elsewhere in the region. The United States is particularly interested in strengthened enforcement of IPR because many FTAA countries have been lax in enforcing TRIPS provisions. (See ch. 5 for estimates of the economic impact of lax IPR enforcement.) Copyright piracy, for example, is still commonplace. The United States also wants to ensure that the FTAA does not undermine IPR protections secured under the WTO and NAFTA.

Developing countries in the region have not traditionally been strong supporters of IPR. However, in the past decade, along with other economic reforms and the advent of TRIPS, they have experienced a progressive evolution in views and policies in favor of greater IPR protection. Laws and institutions now exist in key nations such as Mexico, Brazil, and Argentina, according to trade experts. However, some FTAA countries are reluctant to take on obligations beyond TRIPS, particularly since many improvements in IPR resulting from the FTAA will have to apply unconditionally to all other WTO nations under the “most favored nation” principle contained in Article 4 of the TRIPS agreement. In addition, some FTAA countries have identified areas such as traditional knowledge and folklore that can benefit them within an IPR regime. However, these countries face resource and technical challenges to effectively enforcing IPR and believe that there may be trade-offs between stronger IPR enforcement and other domestic objectives.

Because IPR negotiations are at a relatively early stage, it is difficult to tell which issues will prove controversial, a U.S. official said. Potentially difficult subjects for negotiation include—copyrights in a digital era, compulsory licensing, limitations to patentability, enforcement, and the relationship of trademarks to geographical indications.<sup>2</sup> Proposals by other FTAA nations on folklore, genetic resources, and traditional knowledge also may pose difficulties for the negotiators.

In the area of copyrights, the United States is proposing to ensure protection of copyrighted works in a digital environment by having the FTAA incorporate the substantive provisions of two treaties concluded in 1996 under the auspices of the World Intellectual Property Organization (WIPO). These treaties deal with music, programs, and literary works provided over the Internet. Although a number of countries in the hemisphere already have acceded to the WIPO treaties, others have yet to do so. The WIPO provisions provide important new rights, such as an exclusive right for authors to make their works available on-line. However, the United States faces resistance to its proposal. Some nations do not want to go beyond their current TRIPS obligations. Others object to the U.S. proposal because it contains language intended to clarify certain principles contained in WIPO treaties. For example, the WIPO treaty prohibits tampering with technology designed to prevent unauthorized access to protected works, performances, and phonograms. The U.S. FTAA proposal clarifies that this prohibition must cover both the building of devices capable of tampering with the protected subject matter (e.g., decoding devices) and the actions of actually doing so (e.g., hacking), with appropriate exceptions permitted.

There are also many contentious issues in the area of patents. For example, compulsory licensing, or government permission to produce a patented product or process without authorization of the patent holder, is a contentious issue in the IPR debate over the proper balance between providing incentives for research and the need for public access. This is especially acute with regard to making medicines affordable and accessible. In FTAA negotiations, the United States proposes to clearly specify the circumstances under which FTAA members can grant compulsory licenses. Another FTAA participant has proposed that FTAA

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<sup>2</sup>U.S. proposals to extend the term of copyright protection, require protection of data submitted for regulatory approvals, and only allow competitors to manufacture or use patented products for regulatory approval also face resistance.

members should be given greater scope to grant compulsory licenses, including if a patent holder does not “work” the patented product within a specified period of time. The positions of other FTAA participants range from keeping the status quo under TRIPS—which does not specify the circumstances when governments can grant compulsory licenses, but sets procedural requirements when doing so—to easing TRIPS’ procedural requirements.

The issue of whether certain items can or should be excluded from patentability is another on which FTAA members diverge significantly, with three major options proposed. First, reflecting U.S. leadership in medical and agricultural biotechnology, the United States is trying to narrow (from TRIPS) the categories of products or processes for which patents may be refused.<sup>3</sup> The United States is proposing that the FTAA result in a requirement for members to grant patents for all subject matter except medical and diagnostic procedures, provided that the basic criteria for granting a patent are met—namely, that they are new, involve an inventive step, and are capable of industrial application. FTAA countries would retain the right under TRIPS to refuse patents for products or processes whose commercial use in FTAA countries would jeopardize public order or morality, or seriously jeopardize human, animal, or plant health or the environment. The second option, proposed by other FTAA countries, is that FTAA members retain the right to exclude plants and animals (other than microorganisms) and biological processes from patentability, even if they otherwise met the criteria for patentability. The third option proposed is that FTAA members be prohibited from granting patents for plants, animals, and biological processes.

Enforcement is also an important issue in the FTAA negotiations. The United States has serious concerns about the enforcement of IPR in the FTAA region and has proposed various steps to bolster enforcement through the FTAA. For example, the United States has proposed that violators may be required to pay damages for IPR violations commensurate with the harm suffered, including compensation that is based on the full retail value. Other FTAA participants, particularly developing countries, have resisted the United States on the issue of enforcement. Many of these

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<sup>3</sup>TRIPS, Article 27.3 currently allows governments to exclude from patentability (1) diagnostic, therapeutic, and surgical methods; (2) plants and animals other than microorganisms; and (3) essentially biological processes for the production of plants and animals, other than nonbiological and microbiological processes.

FTAA participants are already facing difficulty implementing their TRIPS obligations and say that they lack the resources and capacity to enforce IPR and face other problems that are more pressing, such as violent crime and drug trafficking.

In the area of trademarks, the main concern involves the relationship between trademarks and geographical indications. Both trademarks and geographical indications provide consumers with information about the source of products; both marks are considered distinct IPR rights that entitle the owner to exclusive use of the mark once it is registered. Geographical indications, such as Idaho potatoes, Florida oranges, and Washington State apples, are marks that identify a good as originating from a geographic area where the quality, reputation, or other characteristic of the good is essentially attributable to that area. FTAA negotiators must decide whether the registration of one type of mark should preclude the later registration of the other type of mark. The United States wants the FTAA to establish the principle that the owner of the mark that was registered first—regardless of whether the original (first) mark is a trademark or a geographical indication—has the right to preclude registration of another mark sought at a later date. This would prevent problems such as the one that occurred in Europe when a geographical indication was granted for Budweiser beer (made in a town by the name Budvar Ceske in the Czech Republic), despite the fact that a trademark on the same name was already registered earlier to the U.S. company Anheuser-Busch. Other FTAA participants from developing countries strongly resist the U.S. proposal because they perceive it as going beyond their current TRIPS obligations.

To capture greater returns from IPR, some developing FTAA countries are proposing to go beyond TRIPS and include topics such as traditional knowledge, folklore, and genetic resources in the FTAA's IPR chapter. Traditional knowledge involves knowledge and practices such as traditional healing methods. Some claim that this knowledge, which exists in local communities and is often passed from generation to generation, can be valuable in the pursuit of innovative medicines. Other countries prefer that a technical forum, such as the WIPO, continue to vet those issues before they are addressed in the FTAA. They are also skeptical that these concepts should be considered new forms of intellectual property.

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## Next Steps

The IPR negotiating group is now working to remove or consolidate duplicative language from the bracketed text. This process is expected to

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be completed over the summer of 2001, and substantive negotiations are expected to begin October 2001. The group will work to eliminate differences in the updated draft text by August 2002.

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## Subsidies, Antidumping, and Countervailing Duties

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### Topic, Importance, and Negotiating Mandate

A politically sensitive issue for FTAA negotiators involves the trade remedies used to counter “unfairly traded” imports. These measures are (1) antidumping duties, which are imposed on “dumped” imports (i.e., imports sold at a price lower than normal value) and (2) countervailing duties, which are imposed on subsidized imports.<sup>4</sup> An importing country imposes antidumping or countervailing duties to remedy the injury to the domestic industry caused by the dumped or subsidized imports. Of these trade remedy measures,<sup>5</sup> antidumping has been very controversial. Proponents believe an antidumping regime is necessary to offset unfair trade practices, while opponents view it as a protectionist system that shelters noncompetitive firms or industries while penalizing domestic consumers.

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<sup>4</sup>A subsidy is generally considered to be a financial contribution provided by a government that provides benefit to a specific company, industry, or group of industries for the production, manufacture, or distribution of goods or services. Government subsidies include direct cash grants, preferential loans, loan guarantees, and tax credits.

<sup>5</sup>Trade remedies also include safeguard actions, which are discussed in the section of this report on market access.

The United States is one of the most frequent users of antidumping measures, which are allowed under rules established in the WTO, and is strongly in favor of having the use of these measures be governed by WTO rules rather than FTAA-specific rules. Many other FTAA countries also employ antidumping measures as a way to address unfairly traded imports. The OAS reports that most regional trade agreements involving countries in the Western Hemisphere allow their members to use antidumping measures as long as they comply with WTO rules. Five FTAA countries predominantly account for the use of antidumping measures in the region.<sup>6</sup> However, the OAS also reports that 19 FTAA countries had never used antidumping measures as of 2000. In addition, the Canada-Chile free trade agreement would eliminate the use of antidumping between the two countries. A Chilean trade negotiator explained that Chile believes the use of safeguard measures is preferable to antidumping because safeguard measures are a more specific instrument and are temporary. (See ch. 5 for more information on the hemispheric use of antidumping.)

Ministers at the San José Ministerial created the negotiating group on subsidies, antidumping, and countervailing duties with a mandate to (1) examine ways to deepen disciplines, if appropriate, and enhance compliance with the terms of the WTO Agreement on Subsidies and Countervailing Measures and (2) achieve a common understanding with a view to improving, where possible, the rules and procedures regarding trade remedy laws to avoid creating unjustified barriers to trade in the hemisphere.

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## Progress to Date

In advance of the ministerial meeting in Buenos Aires, the subsidies, antidumping, and countervailing duties group prepared a fully bracketed, 17-page draft text covering a range of issues. The text includes detailed technical provisions on such topics as

- the determination of dumping and injury,
- investigations and evidence,
- the application of provisional measures,
- assessing and collecting duties,
- special provisions for developing countries, and
- dispute settlement proceedings.

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<sup>6</sup>These countries, listed in the order of the number of antidumping measures taken, are the United States, Canada, Mexico, Argentina, and Brazil.

The draft proposals submitted by the various FTAA negotiators vary widely in their implications for a hemispheric antidumping regime—from maintaining the status quo to eliminating antidumping measures altogether within the region. The United States strongly advocates an approach that would maintain the current WTO rules on antidumping and countervailing duties in the FTAA. Many other proposals in the draft text are modifications to the WTO rules on antidumping measures that, according to the U.S. negotiator, would make it more difficult to use such measures within the FTAA. For example, a WTO threshold for sales below cost (a measure used to determine the cost of a dumped product) would be doubled,<sup>7</sup> and another proposal would have the effect of raising the standard for the determination of injury.<sup>8</sup> The United States strongly opposes these modifications, arguing that they would weaken the U.S. antidumping law. Further, modifications would present serious legal and practical problems by effectively creating dual trade remedy regimes that would greatly complicate dumping investigations, which often include suppliers from multiple countries. Another proposal introduces a procedure not now included in the WTO agreement, which would provide for a public interest inquiry that could result in the imposition of reduced dumping or countervailing duties.<sup>9</sup> Yet another very different proposal contained in the draft text calls for the outright renunciation of antidumping measures on imports from within the region once the free trade area is established.<sup>10</sup>

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## Significant Issues

FTAA subsidies, antidumping, and countervailing duties negotiators have addressed three topics of note so far: the proposed antidumping draft text, the possibility of deepening disciplines on nonagricultural subsidies, and the relationship between trade and competition policy. The most difficult of the three issues involved the draft text. The United States' publicly stated position is that its ability to maintain effective remedies against

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<sup>7</sup>Article 2.2.1 of the draft text contains a footnote proposal that would increase the threshold for the percentage of sales below cost that must be considered in determining normal value from 20 to 40 percent.

<sup>8</sup>Article 3.4 of the draft text includes a proposal that would require a domestic industry to suffer a loss for the period of time in question, which is not required by the WTO agreement.

<sup>9</sup>Article 18 of the draft text contains proposals incorporating consumers' rights and public interest concepts in antidumping investigations.

<sup>10</sup>Article 19 of the draft text reflects this proposal.

dumped or subsidized imports is essential to achieving support for the overall goal of trade liberalization. To this end, the United States proposed draft text stating that each party reserves the right to apply its antidumping and countervailing duty laws, and that no provision of the agreement shall be construed as imposing obligations with respect to these laws. According to U.S. negotiators, the United States proposed that this draft text be included as a stand-alone proposal, separate from the other draft text, because it represents an entirely different approach to the draft chapter. They further explained that this language was intended to maintain the status quo under WTO trade remedy rules, which the other proposals would have the effect of modifying.

The U.S. proposal created a controversy among FTAA participants. According to one of the foreign lead negotiators, many other participants were angered by the U.S. proposal because they believed the United States wanted to take antidumping off the negotiating table. U.S. negotiators stated that their proposal represented a different approach under which, although substantive WTO rules would remain unchanged, some improvements in the areas of transparency and due process could be explored. The controversy was defused by several ministerial directives, as discussed below. Because the issue of antidumping is so politically sensitive, other such flare-ups may recur throughout the course of the FTAA negotiations.

Deepening the WTO disciplines on domestic subsidies on nonagricultural goods is a much less controversial aspect of the process to date.<sup>11</sup> The United States has advocated exploring options for deepening WTO-level subsidy disciplines and improving transparency, consistent with the mandate of the negotiating group. This issue should receive more attention during the next phase of the negotiations than it has so far.

A final issue that has been addressed by this negotiating group is the relationship between trade and competition policy. At the outset of the FTAA discussions, for example, some countries wanted to examine the possibility of injecting antitrust concepts into antidumping rules to more narrowly circumscribe the antidumping remedies. Both the antidumping and competition policy negotiating groups undertook studies to examine the relationship, which were then reviewed by the groups. The United States believes that competition rules and trade remedies address distinctly

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<sup>11</sup>Agricultural subsidies are addressed in the FTAA agriculture negotiations.

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different problems. At their April 2001 meeting, the FTAA ministers directed the two negotiating groups to use the studies for further discussion, rather than to solicit additional studies.

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## Next Steps

To move the negotiations forward, ministers directed the subsidies, antidumping, and countervailing duties group to undertake several actions during the next negotiating phase. Specifically, the ministers instructed the group to

- intensify its efforts to reach a common understanding with a view to improving, where possible, the operation and enforcement of hemispheric trade remedy laws, and submit recommendations on the methodology to be used to achieve this objective to the TNC by April 1, 2002;
- intensify its work of identifying options for deepening, where appropriate, existing disciplines on subsidies in the WTO Agreement on Subsidies and Countervailing Measures, and submit recommendations on the methodology to be used to achieve this objective to the TNC by April 1, 2002;
- identify, using a previously prepared study on trade and competition, any interaction between trade remedies and competition policy that may merit further consideration by the TNC, and provide the results to the TNC by April 1, 2002; and
- submit a new version of the draft text by August 2002.

As part of the compromise reached to move the process forward, the ministers at Buenos Aires required the subsidies, antidumping, and countervailing duties group to prepare recommendations on its methodology to meet the ministerial mandates concerning trade remedy laws and subsidy disciplines. Some FTAA experts believe that this requirement was put in place to ensure that all negotiating groups move forward in tandem and that progress on subsidies and antidumping is commensurate with the rest of the negotiations. The U.S. negotiator believes that the methodology directive is not as significant for this group as reaching agreement on the draft text, which will be more challenging.

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## Dispute Settlement

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### Topic, Importance, and Negotiating Mandate

Although the issues involved are arcane, the topic of dispute settlement in the FTAA process is recognized as a linchpin for the effective operation of the FTAA agreement as a whole. FTAA participants, including the United States, appear to agree on the nature of the dispute settlement mechanism to be created, but three specific issues are likely to be controversial: how to handle compliance, whether to allow appeals, and the extent of public access to the process. Finalizing an FTAA dispute settlement chapter also will require resolving other issues, such as the FTAA's jurisdiction versus other international agreements, third-party rights, and institutional issues.

The FTAA's dispute settlement mechanism will serve a critical role in a final FTAA agreement for three reasons. First, it will ensure that the rights secured and commitments made in an FTAA are upheld. Because the FTAA is expected to go beyond the WTO and other international agreements, FTAA dispute settlement is viewed as the only meaningful way to enforce those commitments. Second, a well-functioning FTAA dispute settlement system will deter countries from adopting measures that do not comply with the FTAA. Third, it will bolster members' confidence by preserving the balance of benefits attained in negotiations and ensuring they have recourse to effective and impartial redress.

The FTAA dispute settlement chapter is expected to create a way to resolve government-to-government disputes over the application and implementation of the FTAA agreement. Specifically, the negotiating group's mandate is to

- establish a fair, transparent, and effective mechanism to settle disputes among FTAA countries and
- design ways to promote the use of arbitration and alternative dispute settlement mechanisms to solve private trade controversies in the framework of the FTAA.

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### Progress to Date

The primary achievement of the negotiating group has been to develop a draft 30-page chapter on dispute settlement that consolidates proposed legal text from all FTAA participants. Negotiations on the chapter are at an early stage, and positions continue to evolve as domestic consultations

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continue. Participants report considerable work will be required to bridge substantive differences and resolve technical and practical issues. The draft chapter on dispute settlement covers

- definitions, scope of application, principles, general provisions, and choice of forum;
- procedures for dispute settlement, including consultations and resort to a neutral body or panel;
- the nature of a final FTAA dispute settlement decision and consequences of failure to implement a decision;
- the obligation to use FTAA dispute settlement to redress violation or impairment of benefits of the FTAA agreement;
- the extent to which the dispute settlement procedure will be confidential or transparent in nature;
- differences in levels of development and effective access; and
- alternative dispute resolution, such as private commercial arbitration.

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## Significant Issues

Discussions on dispute settlement in FTAA are at an early stage, but participants report that there is agreement on many of the fundamentals. For example, there appears to be wide agreement about the nature of the FTAA dispute settlement process—namely, that it have both diplomatic and quasi-judicial features to secure a positive and mutually acceptable resolution to the dispute at hand. A dispute settlement process would likely have three stages: (1) mandatory consultations between the complaining country (or countries) and the country whose measure is at issue; (2) if such consultations fail, establishment of a neutral panel to rule on whether the complaint of noncompliance is warranted; (3) the expectation that a country found to be in violation of its FTAA obligations would respond by complying or by offering compensation. Failing either response, it could face retaliation in the form of new restrictions on its trade. That said, important differences in the negotiating process remain and many complex issues must be worked out.

A major substantive difference in the FTAA negotiations concerns compliance. The two models of dispute settlement under active consideration are the WTO and NAFTA.<sup>12</sup> A key difference between the two models are the steps taken at the compliance stage. Under the WTO, before a complaining party that has won a favorable ruling can retaliate, it must wait for the outcome of a possible appeal; the passage of a “reasonable period of time” for the party found to be in breach to comply; and, if it still fails to comply, the possibility of up to three additional authorization or arbitration procedures. Under NAFTA, the aggrieved country can automatically retaliate 30 days after the panel ruling.<sup>13</sup> The United States has aggressively, and often successfully, employed dispute settlement in complaints against foreign nations’ measures in the WTO.<sup>14</sup> However, the WTO process has been accused of taking too long and failing to reliably produce compliance.<sup>15</sup>

Resolving the different approaches to compliance will require FTAA participants to balance a desire for certain enforceability against practical and defensive considerations. Recent events highlight that the United States may be forced to defend its own measures and could have difficulty meeting short deadlines or complying with adverse rulings. For example, the United States is now struggling to comply with rulings in two recent cases involving a multibillion dollar U.S. tax program known as the Foreign Sales Corporation and U.S. restrictions on Mexican trucking services.

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<sup>12</sup>A third model is for a supranational court, similar to the Andean Court of Justice, but this model is seen as less viable given the expected nature of an eventual FTAA.

<sup>13</sup>The party subjected to retaliation may request a panel to determine whether the level of suspension is “manifestly excessive,” but retaliation may continue while the panel deliberates.

<sup>14</sup>For a discussion of the U.S. experience, see World Trade Organization: U.S. Experience to Date in Dispute Settlement System (GAO/NSIAD/OGC-00-196BR, June 14, 2000).

<sup>15</sup>Our evaluation of the U.S. experience with WTO dispute settlement found that 80 percent of the cases filed by the United States that went to WTO panel or appellate adjudication took longer than the agreed on timetables and that in one out of four WTO rulings, compliance was not deemed satisfactory and had been challenged. See World Trade Organization: Issues in Dispute Settlement (GAO/NSIAD-00-210, Aug. 9, 2000), pp. 21 and 25.

Another major difference in the FTAA negotiations is evident on the subject of appeals. Some FTAA nations have proposed a standing appeals body that would, upon request of either party, examine the legal bases for panel rulings and accept, reject, or modify them. Other nations did not propose an appeals stage. Although the U.S. proposal did not include an appeals stage, the U.S. government is currently evaluating its position. Legal experts that we contacted noted that appeals can add time and expense. However, they stated that the WTO's track record of dispute settlement is more extensive and better regarded than NAFTA's, in part because the WTO Appellate Body helps promote consistency and legal rigor in panel decisions. Moreover, the WTO Appellate Body has served as an important check in the system, substantially revising panel rulings against the United States that raised sovereignty problems.<sup>16</sup> NAFTA's general dispute settlement process does not contain an appeals mechanism, and this dispute settlement process has rarely been used.<sup>17</sup>

FTAA governments differ widely on the subject of the openness (or transparency) of the dispute settlement procedure. The United States has proposed that FTAA dispute settlement include several transparency guarantees, such as open hearings; immediate public access to documents, such as legal briefs; and opportunities for interested private persons, organizations, or companies to be notified of the initiation of FTAA dispute settlement and to provide input into the process. Other FTAA countries not only oppose the U.S. stance on openness but have proposed language for the draft FTAA dispute settlement chapter that requires a confidential process that generally precludes direct or indirect input and participation by nongovernmental organizations.

While not inherently controversial, several complex issues also face FTAA negotiators on dispute settlement. The first is known as "choice of forum" and has to do with who makes the decision regarding whether the FTAA will be used as the forum to settle a dispute among FTAA participants and on what basis. This issue arises because most FTAA participants are members of the WTO and subregional integration agreements such as NAFTA. These agreements may contain substantive obligations on the

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<sup>16</sup>For a discussion of key issues in WTO dispute settlement—namely, its impact on U.S. sovereignty, its record of securing compliance, its timeliness in producing decisions, and its transparency (openness)—see GAO/NSIAD-00-210.

<sup>17</sup>Indeed, the United States tends to choose the WTO when it has cases against NAFTA partners. In fact, only three NAFTA cases have actually gone to a panel for resolution.

same topic and provide separate dispute settlement forums. A problem could arise if (1) jurisprudence built up in one forum that is at odds with another or (2) a country sought to pursue a complaint about the same measure in two different forums on the same or different grounds. The United States has proposed that, as a rule, the complaining country choose the forum in which to pursue a given complaint and, by that choice, foreclose recourse to any other forum. However, the U.S. proposal recognizes that in situations where the FTAA goes beyond the WTO, the FTAA may express a preference that FTAA dispute settlement be used.

Second, the relationship of FTAA dispute settlement to other agreements can also affect third-party rights. Third-party rights are the rights of parties other than the complaining country and the country complained against to participate in a dispute as a co-complainant or as a third party after proceedings have been initiated by another country. Problems could arise if (1) one FTAA country wanted to pursue a complaint about a given measure in the FTAA and another FTAA country wanted to pursue a complaint about the same measure in the WTO or (2) an FTAA country proposed to pursue a complaint under a subregional agreement, such as NAFTA, to which other FTAA participants did not have access. The challenge is to minimize multiple litigation while ensuring that all parties' rights are not diminished. To address this challenge, the United States proposed that FTAA countries be notified of the intent to file a formal WTO complaint against an FTAA member's measure. A third party's stated desire to complain about the same measure would give rise to consultations with an aim to reach agreement on a single forum. The United States also proposed that if a country failed to join an FTAA dispute as a complaining party, it would normally forego litigation about the same matter at the WTO or the FTAA.

Third, making an FTAA dispute settlement system operational will require resolution of institutional issues and the outcome of negotiations on other substantive chapters of the FTAA. For example, the WTO has an institutionalized secretariat that provides considerable support to WTO dispute settlement. Smaller economies are anxious to ensure that they have the monetary and technical resources required to participate meaningfully in FTAA dispute settlement, including secretariat support. The question of whether the FTAA dispute settlement system will handle all disputes regardless of which agreement (or chapter) is involved depends on the outcome of negotiations on other substantive chapters. The alternative is that the general dispute settlement procedure would be supplemented by special dispute settlement rules for specific topics or discrete dispute settlement procedures.<sup>18</sup> A related issue is whether any general or specific standards of review would apply to guide panels. The WTO, for example, contains deferential standards of review with respect to antidumping.

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## Next Steps

The negotiating group on dispute settlement has three mandates for the current phase of FTAA negotiations: (1) prepare a revised draft chapter for presentation to the TNC by August 2002, (2) submit to the Technical Committee on Institutional Issues the negotiating group's preliminary views on the institutions needed to implement FTAA dispute settlement mechanisms, and (3) consider whether proposals for special dispute settlement mechanisms made by other FTAA negotiating groups are compatible with the general dispute settlement procedures developed for the FTAA as a whole and report their conclusions to the TNC or to the Technical Committee on Institutional Issues, as appropriate.

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<sup>18</sup>For example, NAFTA exempts antidumping from the general dispute settlement chapter and adds special procedures regarding disputes over financial services.

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## Competition Policy

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### Topic, Importance, and Negotiating Mandate

FTAA countries, including the United States, agree that each FTAA signatory should implement measures to proscribe anticompetitive business conduct but disagree over the level of detail needed in the agreement. Competition policy, a new legal area for most FTAA participants, consists of the rules and regulations that foster a competitive environment in a national economy, partly through more efficient allocation of resources. Competition policy laws, also referred to as antitrust laws, typically address price-fixing, the misuse of market power by monopolies, and the control of mergers and acquisitions. Only 12 of the 34 FTAA countries currently have such laws,<sup>19</sup> and current agreements in the Western Hemisphere treat competition policy in differently.<sup>20</sup> For example, the Andean Community and CARICOM have adopted supranational institutions to deal with regional competition disputes. Mercosur seeks to build a common competition policy framework among its members. NAFTA promotes a strengthening of national competition policy laws and increased cooperation among national competition agencies.

The competition policy group was established to develop rules to guarantee that the benefits of FTAA liberalization are not undermined by anticompetitive business practices. Specifically, the group has been mandated to (1) establish competition policy juridical and institutional coverage at the national, subregional, or regional level and (2) develop mechanisms that promote competition policy and guarantee the enforcement of regulations on free competition among and within countries of the hemisphere.

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### Progress to Date

As of July 3, 2001, the 15-page draft text contained sections on what competition law should look like, how official monopolies and state

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<sup>19</sup>Countries in the Western Hemisphere that currently have competition policy laws include Argentina, Brazil, Canada, Chile, Colombia, Costa Rica, Jamaica, Mexico, Panama, Peru, the United States, and Venezuela.

<sup>20</sup>Competition policy is not currently covered by the WTO, although the organization has formed a working group on the topic.

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enterprises should be treated, what national and subregional institutions on competition policy should cover, what mechanisms for cooperation and exchange of information should exist, what type of dispute settlement might be appropriate for the provisions in the chapter, and what technical assistance is necessary.

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## Significant Issues

FTAA countries disagree over the level of detail the FTAA agreement should provide on the implementation of competition policy law and the formation of competition policy agencies. All FTAA countries, including the United States, believe that each FTAA country should have a competition agency at the national or subregional level responsible for the enforcement of antitrust laws. However, they disagree over how much detail is needed to define competition policy and develop competition policy agencies. The United States, seeking minimal detail, does not believe it is appropriate to specify detailed provisions on the substantive coverage of antitrust laws. Other countries have submitted detailed proposals that seek to identify specific actions that qualify as anticompetitive. One FTAA expert explained that other countries prefer greater detail either because it is helpful for their civil code legal systems, as opposed to common law in the United States, or because they fear they would not get adequate resources for the implementation of competition policy from their home country governments without strong language in the FTAA agreement.

FTAA countries also have not reached agreement on what type of dispute settlement procedures should be developed to oversee the implementation and operation of competition policy laws within the hemisphere. The draft text currently contains two alternative proposals on dispute settlement—one that calls for disputes to be settled through the general FTAA dispute settlement mechanism and another that calls for the development of a Competition Policy Review Mechanism. The United States supports the creation of a forum within the FTAA to provide a peer review of each FTAA country's implementation of the competition policy chapter and to serve as a venue for the discussion of competition policy issues. According to a U.S. government negotiator, other countries also prefer an FTAA peer review of competition policy laws and implementation in lieu of a binding dispute settlement process because they fear that dispute settlement would subject their national laws to supranational judgments. If formed, the peer review mechanism also could serve as the oversight body for the implementation of the competition policy chapter and a mechanism for providing technical assistance.

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## Next Steps

Ministers mandated the competition policy group to reach agreement on as much of the text as possible by August 2002. Some FTAA experts stated that it would be relatively easy to negotiate the competition policy chapter because countries differ only on the level of detail, not the text's major thrust and purpose. They believe the group may be able to eliminate many, but not all, of the brackets during this negotiating phase. In addition, language from new trade agreements such as the recently concluded Canada-Costa Rica trade agreement may also be submitted for consideration.

# FTAA Efforts to Address Crosscutting Themes

FTAA ministers have taken steps to address three themes that cut across the FTAA negotiations—smaller economies, e-commerce, and civil society—creating “non-negotiating groups” to address them. These groups serve as a conduit for information but do not produce text on trade rules as do the negotiating groups. The theme of smaller economies is significant because many FTAA countries consider themselves small or developing. While FTAA countries have agreed to take differences of size and levels of development into account in negotiating the FTAA, they have not agreed on what form this treatment should take. E-commerce is an emerging theme that intersects the negotiations on market access, services, and IPR. The third crosscutting theme, civil society, has been controversial. To foster public support for the FTAA, ministers have solicited input on the FTAA from business and other nongovernmental groups within the Western Hemisphere, collectively known as civil society. However, many observers questioned the negotiators’ commitment to transparency and willingness to use the public input. Table 3 provides an overview of the three crosscutting themes. The remainder of this chapter describes each of these themes, its importance, and the group’s mandate; progress to date; significant issues; and next steps.

**Table 3: Overview of Crosscutting Themes in the FTAA Negotiations**

Topic	Significance	Mandate	Next steps
Smaller economies	As many as 25 of the 34 countries could be considered smaller economies.	Follow FTAA process; provide recommendations on smaller economy issues.	November 2001 - Assist TNC in developing guidelines for the treatment of smaller economies.
E-commerce	New and growing area for most participants.	Forum to share experience, provide input to process.	October 2002 - Submit recommendations to trade ministers on e-commerce.
Civil society	Key to securing public support, participation in process.	Solicit and transmit views of civil society.	September 2001 - Develop options to foster communication with civil society.

Source: GAO analysis.

## Smaller Economies

### Theme, Importance, and Mandate

By various estimates, as many as 25 of the 34 FTAA countries could be considered to be smaller or developing economies. These economies are

generally characterized by a high degree of trade openness, a lack of economic diversity (high dependence on only a few industries for exports), a dependence on trade taxes for government revenues, and relatively small firms. The treatment of these economies is a crucial crosscutting theme in the FTAA negotiations because smaller economies are concerned about their ability to effectively implement and benefit from a new agreement. According to some experts, these participants are concerned that they may not have sufficient resources to implement new trade obligations. Countries that base much of their government revenues on tariffs, for example, may have difficulty finding alternative sources for that revenue if tariffs are phased out. These participants are also concerned that the very factors that make trade beneficial to small countries may make it difficult for some of them to achieve these benefits under the agreement. For example, the dislocation of a key sector has a proportionately larger impact on a small economy than on a larger, more diversified economy.

Because so many FTAA participants consider themselves to be small or developing, the theme of smaller economies has repeatedly been discussed throughout the negotiations. At their first ministerial in Denver, Colorado, in 1995, FTAA countries, including the United States, acknowledged the wide differences in levels of development and size of economies, and pledged to actively look for ways to provide opportunities to facilitate the integration of smaller economies and increase their level of development. FTAA countries have repeatedly reaffirmed this principle in subsequent meetings.

One step that ministers took to address the concerns of smaller economies was to form a consultative group on the issue. As set out in the San José Ministerial Declaration, the Consultative Group on Smaller Economies was established with a mandate to (1) follow the FTAA process and (2) provide the TNC with information on issues of concern to smaller economies and to make recommendations on these issues.

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## Progress to Date

Since its inception, the consultative group has served as a forum for the discussion of issues relevant to smaller economies. For example, certain FTAA countries have begun sharing their negotiating group proposals on smaller economies in the group's meetings. In addition, the group has served as a mechanism for the discussion and coordination of technical assistance. The Tripartite Committee prepared a technical cooperation needs assessment for the group, which outlines the technical assistance needs of 17 of the FTAA participants. The group also has invited

prospective donors to share any information they may have on their technical assistance programs.

In addition to the consultative group, ministers have directed the negotiating groups to take the concerns of smaller economies into account in their negotiations. All negotiating group texts contain proposals on technical assistance or treatment for smaller economies. For example, the draft text on competition policy contains a section on technical assistance provisions to help countries develop and implement competition policy laws and institutions. Similarly, the market access draft text contains proposals for safeguard provisions that, under certain circumstances, would exempt products from smaller economies from the safeguard measures applied by other FTAA countries.

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## Significant Issues

The term “smaller economy” within the context of the FTAA has not been defined. Although various methods exist to identify the size of economies, including population, land area, and gross domestic product, each method produces a different set of countries. While these different sets do overlap, not all countries designated small by one method are considered small by others. For example, a 1998 study states that per capita gross domestic product in the Bahamas, which has only 0.16 percent of Brazil’s land area, is three times larger than Brazil’s per capita gross domestic product. According to one FTAA expert, the smaller economies group tried to define a “smaller economy” in the FTAA context but failed to agree on a single definition. To solve this dilemma, the United States has proposed that the treatment of smaller economies be decided on a case-by-case basis in the negotiations instead of grouping countries by a single definition. Other countries oppose this plan because they feel it may exclude them from receiving special consideration that they might otherwise receive under a categorical definition.

The type of treatment that countries with smaller and less developed economies will receive under the FTAA has not been determined. The WTO allows for the special and differential treatment<sup>1</sup> of developing countries by giving them longer time periods to implement tariff

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<sup>1</sup>The term “special and differential treatment” is the product of the coordinated political efforts of developing countries, which began as early as 1947-48. These efforts were to correct the perceived inequalities of the postwar international trading system by introducing preferential treatment for developing countries.

reductions, more favorable thresholds for applying certain commitments such as countervailing duties, and greater flexibility with regard to certain obligations. Under the FTAA negotiations, decisions about the treatment of smaller or developing economies will be important for the tariff and nontariff barrier modality discussions because they are supposed to define which countries may be eligible for what type of treatment. All FTAA countries agree that the rights and obligations of the FTAA need to be assumed by all countries participating in the process. However, the United States and others recognize that some countries may need longer phase-in periods to effectuate such rights and obligations. Other countries would like to see more aggressive and categorical treatment of smaller economies, similar to what has occurred under the WTO.

In addition to special treatment, smaller economies are seeking technical assistance to strengthen their participation in the negotiations and increase their ability to carry out FTAA objectives. Developing countries have already faced resource constraints in their attempts to carry out existing international trade obligations under the WTO. According to U.S. officials, smaller FTAA economies, particularly the Caribbean nations, have been vocal about their need for technical assistance and have influenced some negotiating dates due to their concerns over resource constraints. The Tripartite Committee has already provided several countries with assistance in preparing for the negotiations and in implementing FTAA business facilitation measures. Several negotiating groups have incorporated into their texts specific language on technical assistance. The United States would like to see the smaller economies group spend more time on the issue of technical assistance, with countries identifying their technical assistance needs through their country-specific proposals.

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## Next Steps

An important step concerning smaller economies during the next negotiating phase will be the development of guidelines for the treatment of differences in size or level of development. The Buenos Aires declaration states that the TNC, with the assistance of the consultative group, must develop no later than November 2001 some guidelines or directives for negotiating groups to apply treatment that takes into account differences in levels of development and size of economies. The smaller economies group is currently in the process of developing recommendations on these guidelines, which it will forward to the TNC in September 2001.

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Another important next step involves the provision of technical assistance. At the Buenos Aires Ministerial, the United States and the IDB indicated that they would further explore ways to meet these technical assistance needs. Their success in identifying funding for smaller economies may affect the negotiations, if smaller economies feel their technical assistance needs are not being met.

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## E-commerce

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### Theme, Importance, and Mandate

As e-commerce and the use of the Internet have expanded over the past several years, trade negotiators have begun to grapple with how existing trade agreements cover these activities and whether new commitments are needed. Since the development of e-commerce is relatively new, few government regulations or border measures currently exist to control the flow of electronic transmissions. FTAA governments generally share the goals of fostering a supportive environment and maintaining an open trading regime for e-commerce. The United States, as a leading user and developer of e-commerce, has a commercial interest in expanding its use and maintaining an open trading environment for digital products and services. Other FTAA partners also perceive economic and social benefits from expanded use of e-commerce and the Internet for their own countries and want to remain technologically integrated into the global economy. To address their mutual interests in developing a digitally connected hemisphere, trade ministers established the Joint Government-Private Sector Committee of Experts on Electronic Commerce in 1998. The committee's mandate is to make recommendations to the ministers on how to increase and broaden the benefits to be derived from the electronic marketplace. However, the committee is a non-negotiating group and will not develop rules for the FTAA agreement.

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### Progress to Date

Made up of government and private sector representatives, the joint committee has provided ministers with recommendations on issues related to its mandate. The committee has also provided a forum for countries to share their experiences and develop approaches to encouraging the development of e-commerce activities. The committee has issued two public reports that made recommendations on topics such as strengthening information infrastructure; increasing participation of governments, smaller economies, and small businesses; clarifying the rules of the market;

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developing on-line payment services; and addressing certification and authentication issues. Participants say that the committee has provided a useful role in facilitating information sharing among FTAA countries on best practices and e-commerce concerns.

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## Significant Issues

E-commerce issues are closely connected to several areas of the FTAA negotiations, including market access, services, IPR, and government procurement. Since the FTAA e-commerce group is a non-negotiating group, any commitments countries want related to e-commerce must be agreed on in one of the negotiating groups. For example, competition among Internet service providers and access to telecommunications networks are issues likely to be addressed in the services negotiating group. Protection of copyrighted materials and original works distributed over the Internet would be addressed in the IPR negotiating group. Market access negotiations on goods also may entail e-commerce-related issues because certain goods, such as books and videos, can be transmitted digitally or shipped physically.<sup>2</sup> Because many countries, including the United States, use e-commerce to conduct government procurement, issues may also arise in the negotiating group on government procurement.

Negotiators must be aware of the interrelationship between e-commerce issues and their specific topic because the use and efficiency of e-commerce transactions rely on an open environment across all steps in the production, marketing, sale, and distribution of a product. For example, if a country maintains an open telecommunications environment with high levels of Internet use, e-commerce still can be stymied if the country's custom procedures are onerous and deter shipments of small packages. In addition, negotiators also need to be aware of any e-commerce-related decisions made at the WTO or other multilateral fora since they may have an impact on the FTAA negotiations.

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## Next Steps

At the April FTAA ministerial, trade ministers instructed the joint committee to continue to identify and review specific issues. The

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<sup>2</sup>Discussions are ongoing in the WTO over the classification of digital products. Some countries recommend their classification as goods, others as services. The United States argues that these products should receive the most liberal treatment possible and that, before deciding on classification, more information is needed on the potential impact of the various options.

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committee also recommended that it continue to share national experiences and broadly analyze the factors that led to their success or failure. The joint committee's work for the third phase of discussions will address the

- digital divide,
- consumer protection, and
- e-government and other issues.

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## Civil Society

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### Theme, Importance, and Mandate

The views of civil society groups (nongovernmental groups representing business, labor, environment, and other interests) will likely affect the level of U.S. public support for the FTAA. Although multilateral trade agreements, such as the FTAA, are conducted at a government-to-government level, public support for the outcome is an important factor in generating the political will to conclude an agreement. Civil society parties thus need information about the progress of the negotiations and a vehicle for expressing their viewpoints. At the outset of the negotiations, the ministers committed to a transparent process and welcomed the contributions of the private sector.<sup>3</sup> In 1998, at the San José Ministerial, the trade ministers reaffirmed their commitment to transparency to facilitate the constructive participation of different sectors of society. The ministers formed the Committee of Government Representatives on the Participation of Civil Society with a mandate to receive civil society views on trade matters and present them to the ministers.

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### Progress to Date

The committee pursued its mandate by soliciting the views of civil society on two occasions through a formal submissions process. Acceptable submissions had to meet a specified format and present the views constructively. The committee issued an open invitation; countries also solicited input through their own national mechanisms. For example, the United States solicited input via the *Federal Register* process, through the Internet, and by direct solicitation. The first round of submissions

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<sup>3</sup>As stated in the first FTAA Ministerial Declaration in Denver, 1995.

occurred before the Toronto Ministerial in 1999 and garnered about 60 acceptable responses from civil society groups in the hemisphere. A second round of submissions in 2000 before the Buenos Aires Ministerial resulted in 77 acceptable responses. In both cases, the committee submitted a report on the results at the ministerial meetings.

The United States has championed this theme, in part because the committee on civil society provides a vehicle for discussing labor and environmental issues in the FTAA. The United States had sought to create an FTAA study group to address the relationship between the FTAA's goals and labor issues, but many other FTAA countries objected, arguing that labor issues were more appropriately addressed in another international forum such as the International Labour Organization. In addition, according to FTAA experts, some countries believe that participants bear the responsibility of taking their citizens' views into account and are skeptical of the value of including civil society input in the negotiations. The committee's formation provided a compromise solution. Open to submissions on an array of FTAA-related topics, the committee gives organizations and individuals interested in the FTAA a way to voice their concerns within the FTAA process.

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## Significant Topics

As the negotiations enter the next phase, three aspects of the discussion on the participation of civil society in the FTAA process are worth noting. These are the transparency of the process, the difficulty the committee has had in reporting submissions by civil society, and the extent to which submissions are considered by negotiating groups.

First, the level of transparency in the negotiation process has been in question. While the FTAA ministers continue to declare that they are committed to a transparent process that facilitates the constructive participation of nongovernmental sectors, the specific means to do so had not been spelled out before the Buenos Aires Ministerial. As a result, nongovernmental organizations and business and government representatives in the United States and elsewhere in the hemisphere criticized the FTAA process as lacking transparency. For example, although USTR released public summaries of U.S. positions, 50 Members of Congress, along with business representatives and nongovernmental organizations, all called for the release of the actual negotiating text. U.S. negotiators hope that the implementation of new outreach measures will go some way toward dampening the criticism that the process lacks transparency.

In response to broad demands for a more transparent process, the FTAA ministers agreed on April 7, 2001, in Buenos Aires to publicly release the draft text of the nine negotiating groups. They determined that publication of the text would help increase the transparency of the negotiating process and help build broad public support for the FTAA. The text, which had been negotiated in English and Spanish, was translated into French and Portuguese and released to the public on the FTAA internet site on July 3, 2001.<sup>4</sup> This text gives a snapshot of the status of the FTAA negotiations as they stood as of the Buenos Aires Ministerial, including the range of topics and proposals before the negotiators. The publicly released text is the same text from which negotiations are now proceeding, according to USTR. Because the text is heavily bracketed, it may be difficult for outside observers to understand or to assess potential areas of agreement or consensus. In addition, the FTAA governments agreed not to include country identifiers in the text in order to keep the negotiations more fluid. Further, there is no guarantee that future revisions to the text will be made available to the public. This is important for two reasons. Entirely new proposals may be made, and the text is likely to change significantly as the negotiating groups work to eliminate brackets and duplication.

Second, the committee has had difficulty in reaching consensus on how to report the results of public submissions through the TNC to the trade ministers. This indicates the sensitivity of discussions about civil society in the FTAA as well as the challenges associated with a process run by consensus. During the first round of submissions, one FTAA country blocked the committee from preparing recommendations on the basis of the public input received, which was an objective sought by the United States. The committee's report was thus limited to statistical information about the submissions with minimal description of the contents, according to U.S. officials. During the second round of submissions before the Buenos Aires Ministerial, the committee again had difficulty reaching consensus on the reporting issue, but eventually reached a compromise. The committee's report to the TNC on the second round of submissions provided a more comprehensive and descriptive summary of the input.

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<sup>4</sup>The draft FTAA text can be accessed at [www.ftaa-alca.org/Alca\\_e.asp](http://www.ftaa-alca.org/Alca_e.asp).

Third, some are concerned about the extent to which the public submissions are considered by the negotiating groups. Civil society representatives we interviewed told us that they were disappointed because there was little evidence that their input was being given serious consideration in the negotiations. Since the ministers had not initially directed that the civil society submissions be provided to the negotiators, the submissions were channeled through the committee. Negotiators theoretically could request the submissions through the committee, but U.S. officials noted that due to translation and logistical problems, the U.S. negotiators who were interested in considering the submissions were forced to rely on executive summaries rather than the complete submissions.<sup>5</sup> The negotiators during the next phase of the negotiations should have access to civil society submissions because, at Buenos Aires, the FTAA ministers directed the committee to transmit the submissions to the appropriate negotiating groups. The United States has been actively pressing for each negotiating group to consider civil society input, according to U.S. negotiators.

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## Next Steps

The participation of civil society in the FTAA process is expected to increase following the Buenos Aires Ministerial, according to U.S. officials. The FTAA ministers declared in Buenos Aires that the committee was “to foster a process of increasing and sustained communication with civil society, to ensure that civil society has a clear perception of the development of the FTAA negotiating process.” To do so, the committee as instructed to take the following steps:

- develop a list of options to increase and sustain communication with civil society for consideration by the TNC at its next meeting in September 2001;
- forward to the nine negotiating groups the submissions made pertaining to their respective issues;
- forward to the nine negotiating groups the submissions related to the FTAA process in general; and
- invite civil society groups to present their conclusions about the FTAA negotiations from other fora and seminars within the hemisphere.

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<sup>5</sup>The executive summaries of the civil society submissions can be viewed on the Department of State’s Internet site at [http://www.state.gov/www/issues/economic/ftaa/0011\\_ftaa\\_summaries.html](http://www.state.gov/www/issues/economic/ftaa/0011_ftaa_summaries.html).

The ministers did not explicitly request another round of formal civil society submissions after the ministerial. U.S. officials stated that the committee is going to consider a variety of approaches as it develops its list of options for the TNC to consider, including, among others, the possibility of a third open invitation to civil society. Options may also include seminars, outreach briefings in the hemisphere, and other methods for providing information to the public on the progress of the negotiations. In addition, according to FTAA experts, other FTAA participants are being much more supportive of the civil society committee than they were earlier in the process. U.S. negotiators believe that by providing a means to communicate civil society views to ministers, the committee also offers an opportunity to begin to build broad-based support within the hemisphere for an eventual agreement.

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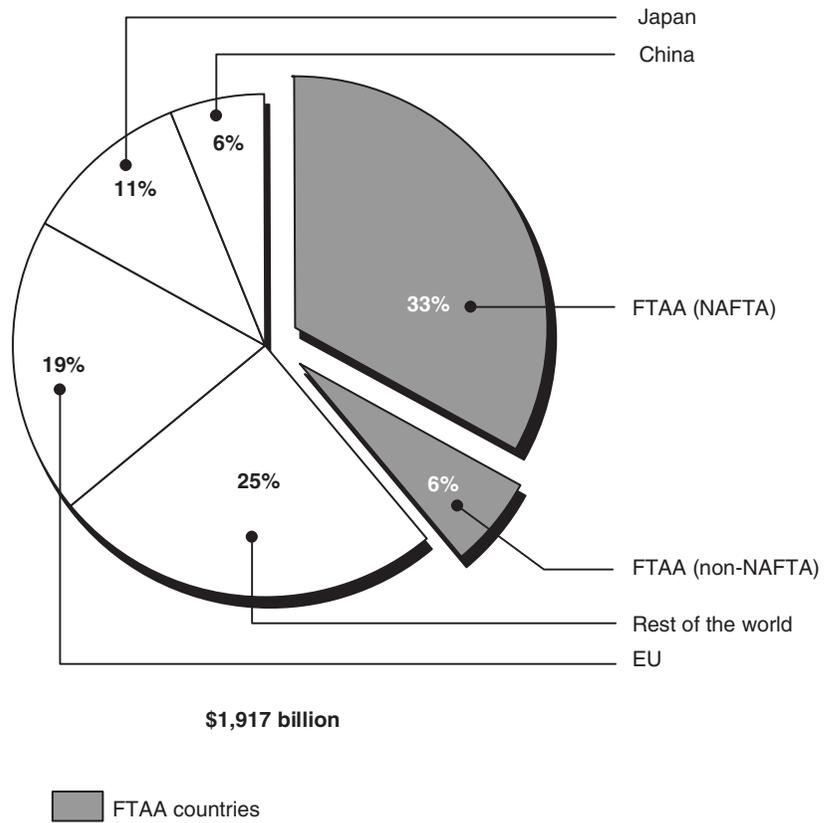
# FTAA Would Secure and Expand Trade Access and Rights for the United States

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A comprehensive FTAA would unite a diverse set of economies into the world's largest trading bloc involving nearly 40 percent of the world production and significant shares of U.S. trade and investment. Such an agreement would benefit U.S. exporters by reducing some relatively high trade barriers on U.S. exports to the region. By comparison, most FTAA exports to the United States entered duty-free in 2000. However, some U.S. import-competing industries, such as textiles, apparel, and certain agricultural goods, have traditionally received higher levels of protection. These industries would face increased competition and potentially lower production and employment if current U.S. barriers were lowered. The overall impact on the U.S. economy of removing U.S. and other FTAA countries' tariff barriers may be relatively small since the total U.S. trade with non-NAFTA FTAA countries is only about 1 percent of the \$11 trillion U.S. economy. An FTAA agreement, however, would cover much more than merchandise trade. Services, investment, IPR, and government procurement are commercially important areas in which the United States may gain improved market access and privileges. The FTAA would provide new coverage in investment and government procurement because the United States currently has only a few bilateral agreements with other FTAA countries in those areas. The United States also hopes to expand coverage in services and IPR beyond existing WTO agreements.

U.S. trade and investment in the Western Hemisphere have increased rapidly over the past decade. Over 80 percent of U.S. merchandise trade and about half of services trade and investment in the region are with NAFTA partners Canada and Mexico. However, merchandise trade with non-NAFTA FTAA countries has more than doubled over the past decade, and services trade and FDI have increased in both value and share relative to the rest of the world. Figures 7, 8, and 9 show the shares of U.S. merchandise trade, services trade, and FDI with key trade partners. Appendix I provides more information on current U.S. trade and investment with FTAA countries.

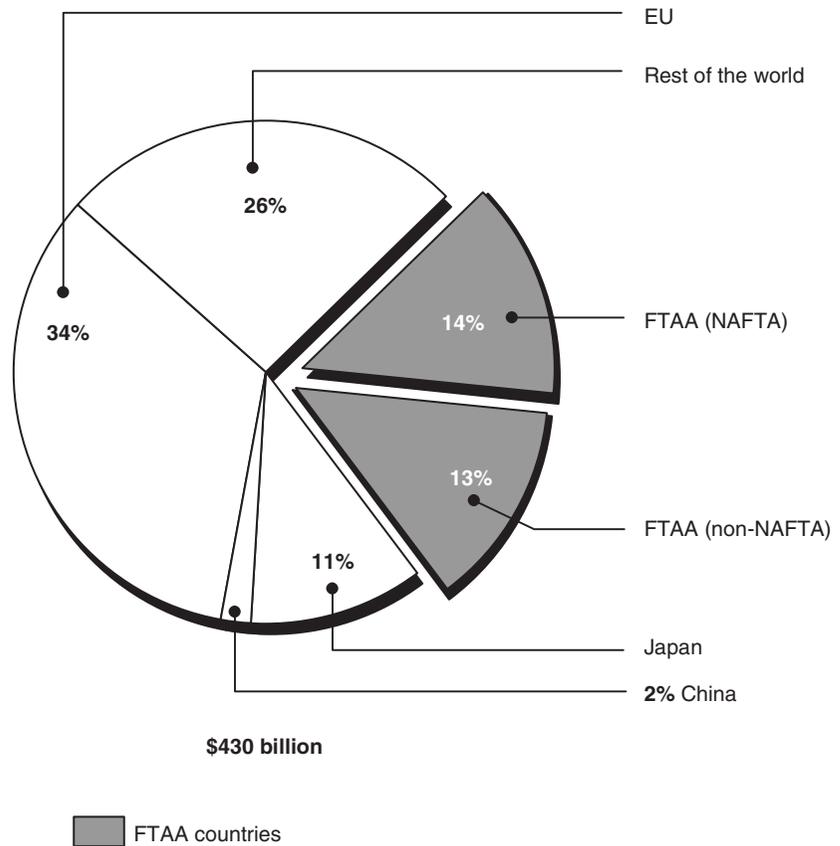
Figure 7: U.S. Merchandise Trade With Key Trade Partners, 2000



Note: Merchandise trade is exports plus imports of industrial and agricultural goods.

Source: GAO analysis of U.S. Department of Commerce data.

Figure 8: U.S. Trade in Services With Key Trade Partners, 1999

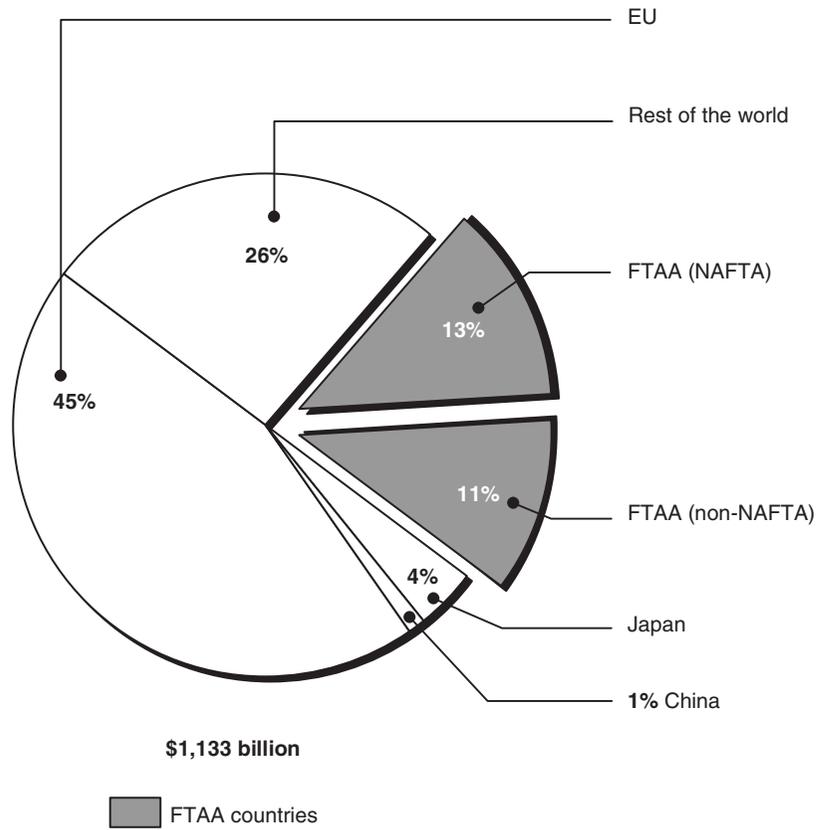


Note 1: Services trade is exports plus imports of cross-border private (nongovernment) commercial services.

Note 2: The most recent year available for services data was 1999.

Source: GAO analysis of U.S. Department of Commerce data.

Figure 9: The Stock of U.S. Foreign Direct Investment in Key Trade Partners, 1999



Note: The most recent year available for investment data was 1999.

Source: GAO analysis of U.S. Department of Commerce data.

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## Liberalization of Merchandise Trade Would Bring New Opportunities for U.S. Exporters and Increased Competition in Some Protected U.S. Sectors

Over the past decade, FTAA countries have pursued the liberalization and integration of their economies through a wide variety of interregional free trade and customs union agreements. These changes have lowered barriers to U.S. exports, but tariffs and other barriers still remain relatively high on many U.S. exports. FTAA countries' overall average tariff rates are about twice that of the United States, with about one-third above 10 percent. Barriers on agricultural products are generally higher than industrial goods. Some U.S. products also face higher tariff rates than other competitors that have preferential access to some FTAA markets through subregional trade agreements. For FTAA countries, the U.S. market is relatively open with 87 percent of FTAA imports entering duty-free and an average trade-weighted U.S. tariff on FTAA imports of less than 1 percent.<sup>1</sup> However, the United States maintains high barriers on certain agricultural products, such as sugar, peanuts, and citrus, and on textiles and apparel products, which are important exports of various FTAA countries. For some of these products, imports are limited by quota or by prohibitively high tariffs after an initial quantity has been imported. Reductions in these barriers may increase imports, lower prices, and reduce U.S. production. FTAA negotiations also include antidumping measures, which place additional duties on products if a country finds that the products have been sold at less than their normal value. Changes in antidumping rules may have mixed results for the United States because it is the country that has initiated the most cases and had the most cases initiated against it within the FTAA region. Overall, some economic studies suggest that the elimination of tariff and nontariff barriers in the region would likely have a small impact on the U.S. economy because of the relatively small size of U.S. trade with the region compared with U.S. production.

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## FTAA May Benefit U.S. Exporters by Eliminating Remaining Duties on U.S. Products

The FTAA could expand opportunities for U.S. exporters by removing tariff and nontariff barriers on U.S. products. Average tariff levels in the region fell from over 40 percent in the mid-1980s to 12 percent in the mid-1990s, prompting sizable increases in both intra- and extra-regional trade flows, according to the IDB. In 1985, Brazil's simple average tariff rate was 51

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<sup>1</sup>Trade-weighted average tariff rates are the average of all tariffs on imported products multiplied by the share of total imports accounted for by each product. Therefore, products that account for more trade are weighted more in the overall average. If these products have high tariff rates, then the average will be higher than a simple unweighted average tariff.

percent, while Argentina's was 35 percent. In 1999, these rates fell to 14 and 11 percent, respectively. Current tariff averages for FTAA countries are generally significantly lower than the averages during the 1980s and early 1990s. However, compared with the U.S. and Canadian simple average tariff rates of less than 5 percent, other FTAA countries' rates are still relatively high.

Some countries, such as Chile and Bolivia, have relatively uniform tariff schedules that apply an across-the-board rate for most products, with some exceptions. Chile recently lowered its uniform rate from 9 to 8 percent on January 1, 2001. It is scheduled to continue lowering the rate until it reaches 6 percent in 2003. Other countries tend to apply a wider range of rates, with the highest duties applied to sensitive products. Brazil, for instance, charges its highest duties (35 percent) on automobile parts; Nicaragua charges rates between 45 to 55 percent on certain types of corn and rice imports; and Canada maintains out-of-quota tariff rates of over 250 percent on certain dairy imports.<sup>2</sup> In addition, only Canada, Costa Rica, El Salvador, Panama, and the United States have agreed to eliminate tariffs on certain high-technology products through the WTO Information Technology Agreement. These products are important exports for the United States, and some countries, including Brazil, maintain high tariffs on them.

In addition to lowering the tariff rates that exporters are currently charged, the FTAA would also commit countries to not raise these rates in the future. Through their WTO commitments, FTAA countries have already bound most of their tariffs at certain levels. However, in many cases these bound rates are relatively high and countries charge much lower rates in practice. A World Bank study found that for the 10 Latin American countries it examined, the overall trade-weighted average bound rates ranged between 25 and 57 percent and were at least two or three times as high as the current rates the countries charged. Under WTO rules, countries can increase their current rates to their bound levels at any time. The FTAA would reduce these higher bound rates, in many cases to zero, and provide additional certainty for FTAA exporters.

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<sup>2</sup>Out-of-quota tariffs are part of tariff-rate quotas that some countries apply to agricultural goods. A tariff-rate quota allows a certain amount of a product to be imported at a generally low "in-quota" rate. Any additional imports face a higher out-of-quota duty.

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**Agricultural Trade May Be  
More Affected by FTAA  
Because Current Barriers  
Tend to Be Higher**

U.S. agricultural exporters also stand to gain from tariff elimination through the FTAA. Since agricultural tariffs are generally higher than those on industrial goods, the FTAA may lead to more substantial changes in agricultural trade than in other sectors. For example, Costa Rica's average tariff on imports of manufactured goods is 5.4 percent compared with 16.8 percent on agricultural goods. Agricultural tariffs in Barbados, Belize, Guyana, and Jamaica all average over 20 percent and are generally twice the average tariff on industrial goods. Table 4 shows simple average tariff rates across FTAA countries for all agricultural and industrial goods. The pattern of higher tariffs on agricultural goods holds true for all FTAA countries except Chile and the Mercosur countries of Argentina, Brazil, and Uruguay. For Mercosur countries, protection of certain industrial goods, such as automobiles, raises their average rates on industrial goods slightly higher than tariffs on agricultural goods. The bound rates that countries committed to in the WTO are even higher, with the average across all agricultural goods in South America at 39 percent, in Central America at 54 percent, and in the Caribbean Islands at 86 percent. The U.S. Department of Agriculture's Economic Research Service estimated that elimination of agricultural barriers would lead to the expansion of U.S. exports to FTAA countries by 8 percent in the first 5 years and an increase in U.S. imports from FTAA countries by 6 percent. The study predicted that U.S. exports of wheat to Brazil and exports of corn, soybeans, and cotton across the hemisphere would increase.

**Chapter 5**  
**FTAA Would Secure and Expand Trade Access**  
**and Rights for the United States**

**Table 4: Average Tariff Rates for All Agricultural and Industrial Goods**

<b>Country</b>	<b>Year</b>	<b>All goods (percent)</b>	<b>Agriculture (percent)</b>	<b>Industrial (percent)</b>
Argentina	1999	11.0	10.4	11.0
Barbados	1999	13.6	20.2	12.0
Belize	1998	9.2	21.0	8.2
Bolivia	1999	9.7	10.0	8.9
Brazil	1999	13.6	10.8	13.9
Canada	1999	4.6	4.6	4.5
Chile	1999	10.0	10.0	10.0
Colombia	1999	11.6	13.1	11.6
Costa Rica	1999	7.2	16.8	5.4
The Dominican Republic	1997	14.5	15.3	14.2
Ecuador	1999	11.6	15.5	11.0
El Salvador	1998	5.7	10.0	4.4
Guatemala	1999	7.6	10.7	7.0
Guyana	1998	10.4	23.1	9.3
Honduras	1999	8.1	12.2	7.5
Jamaica	1999	8.7	21.6	6.6
Mexico	1999	10.1	11.5	10.0
Nicaragua	1999	11.0	16.4	10.3
Panama	1998	9.2	11.4	8.5
Paraguay	1999	9.0	10.2	9.0
Peru	1998	13.2	14.7	13.0
Trinidad and Tobago	1998	9.2	20.0	8.4
The United States	1999	4.8	8.7	4.3
Uruguay	1999	4.6	4.2	4.7
Venezuela	1999	12.0	12.5	11.9

Note: Data were not available for nine FTAA countries. Averages are the simple average ad valorem tariff rate across all goods or agricultural and industrial goods.

Source: World Bank data.

Certain agricultural products also tend to face trade-distorting measures, such as price bands and export subsidies, which the FTAA may address. For example, the United States has initiated a WTO dispute case against Canada over its export programs involving dairy products and has initiated a review of the Canadian wheat marketing board to determine how its status as a state-trading monopoly may restrict competition and harm U.S. producers. Chile has used complex price bands, which apply additional duties on imports, to maintain domestic prices within a certain range for wheat, wheat flour, edible vegetable oils, and sugar. For example, due to recent low international prices for wheat products, Chile applies duties as high as 90 percent on imports of wheat, a key U.S. export. FTAA negotiations may address these and other agricultural trade practices that distort domestic and international markets. Negotiators already have reached agreement on the elimination of agricultural export subsidies, another trade-distorting practice. The WTO agriculture agreement allows exports subsidies, but only if the WTO is notified and the subsidies are reduced over time.<sup>3</sup>

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### FTAA May Eliminate Disadvantages That U.S. Exports Face Due to Subregional Trade Agreements

Proponents of the FTAA argue that it will eliminate the disadvantage U.S. exporters face from subregional agreements within the hemisphere and help them maintain or expand market share. Subregional trade agreements have proliferated in the Western Hemisphere as part of a larger reform process undertaken by many FTAA countries that has included lowering tariffs on all partners. However, for those countries that are members of free trade agreements or custom unions, duties are even lower or are eliminated.<sup>4</sup> The United States is only party to one (NAFTA) of numerous trade agreements in the region. USTR, the U.S. Department of Agriculture, and some business associations have cited the Chile-Canada free trade agreement as an important example of how U.S. exports are disadvantaged because the agreement provides preferential access for Canadian products in sectors such as forest products, wheat, vegetable oils, and potatoes. Both Canada and the United States are major producers of these products and compete in Chile and elsewhere. In addition, the EU has recently

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<sup>3</sup>Of the FTAA countries, only eight have notified the WTO of export subsidies. These countries are Brazil, Canada, Colombia, Mexico, Panama, the United States, Uruguay, and Venezuela.

<sup>4</sup>Because trade may be diverted from the most efficient suppliers to less efficient ones with preferential access, subregional agreements may have some negative effects in addition to the traditional benefits associated with trade liberalization.

concluded a free trade agreement with Mexico and is pursuing negotiations with Chile and Mercosur. An FTAA might, however, undercut existing U.S. trade preference programs by eliminating similar disadvantages faced by some FTAA countries in the U.S. market compared with Canada and Mexico through NAFTA. For example, Congress recently improved textile and apparel access for Caribbean Basin countries through the Caribbean Basin Trade Partnership Act, partly to match the expanded access Mexico achieved through NAFTA. Andean Community countries have also sought similar provisions, citing lost sales to Caribbean competitors.

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**Many U.S. Imports of FTAA  
Products Will Face Limited  
Changes Since Most Already  
Enter U.S. Market Duty-Free**

For most U.S. sectors, tariff liberalization through the FTAA would likely have a limited impact on U.S. imports. This is because the U.S. market is already relatively open to imports from FTAA nations. For example, in 2000, most FTAA goods entered the United States duty-free or at very low rates. The overall average tariff rate on products entering the U.S. market is less than 5 percent.<sup>5</sup> However, the United States also provides countries with further tariff reductions on certain products through several specialized programs. These include nonreciprocal trade preference programs, such as the Generalized System of Preferences, and reciprocal trade preference programs, such as the Agreement on Trade in Pharmaceutical Products.<sup>6</sup> Most of these programs offer duty-free entry or very low tariff rates on a range of products. Therefore, the average tariff rates facing many countries' products imported by the United States are even lower than the normal average U.S. tariff rate. For example, the trade-weighted average U.S. tariff rate on imports from FTAA countries is only 0.79 percent.<sup>7</sup> However, the trade-weighted tariff rates vary across countries and regional groups depending on the types of products imported by the United States. Table 5 shows that NAFTA countries face the lowest U.S. tariff rates, while Central American countries face the highest overall average.

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<sup>5</sup>This is a simple average tariff rate based on "ad valorem" tariffs (a percentage of the value of a good) and some ad valorem equivalent rates of "specific" tariffs (a fee per unit of a good) calculated by the U.S. International Trade Commission. See Chapter 1, Objectives, Scope, and Methodology.

<sup>6</sup>The nonreciprocal programs include the General System of Preferences, the Caribbean Basin Economic Recovery Act, the Caribbean Basin Trade Partnership Act, and the Andean Trade Preference Act. Reciprocal trade preference programs include the Automotive Products Trade Act, the Agreement on Trade in Civil Aircraft, the Agreement on Trade in Pharmaceutical Products, and the Uruguay Round Concessions on Intermediate Chemicals for Dyes. For more information on nonreciprocal trade preference programs, see GAO-01-647.

<sup>7</sup>Trade-weighted tariff averages place lower weights on products that are imported less. Since prohibitively high tariffs and quotas restrict imports of a product, the product's tariff is weighted less in the overall average. Therefore, trade-weighted averages can understate the importance of high tariff rates or quotas on products that might be imported more if barriers were lowered.

**Table 5: Trade-weighted Tariff Averages for U.S. Imports From FTAA Countries**

Regional group	All products (percent)
Andean Community	0.91
CACM	10.38
CARICOM	2.67
Mercosur	2.02
NAFTA	0.27
Other	6.09
<b>Total FTAA</b>	<b>0.79</b>

Note: "Other" category includes Chile, the Dominican Republic, and Panama.

Source: GAO analysis.

About 87 percent (\$376 billion) of FTAA imports entered the United States duty-free in 2000. Another 7 percent paid duties between 0 and 5 percent, and only about 3 percent faced duties of above 15 percent. Through NAFTA, Canada and Mexico had an even higher share of their products (94 percent) enter duty-free. The Andean Community and Central American nations had the lowest shares of duty-free products, with about 40 percent of their imports facing no duties. Table 6 shows the share of imports facing different ranges of tariff rates by each regional group.

**Table 6: Share of Imports Facing Different Ranges of Tariff Rates for Each FTAA Regional Group, 2000**

Regional group	Share of duty-free U.S. imports	Share of U.S. imports facing tariffs that are:			
		Between 0 and 5 percent	Between 5 and 10 percent	Between 10 and 15 percent	Greater than 15 percent
Andean Community	39.7%	55.7%	0.5%	0.3%	2.6%
CACM	40.4	2.2	7.7	1.2	47.9
CARICOM	63.4	21.2	1.6	0.2	12.9
Mercosur	61.4	25.9	8.8	2.1	1.4
NAFTA	94.4	2.3	0.2	0.1	0.9
Other	50.9	15.1	6.1	1.2	26.2
<b>All FTAA</b>	<b>86.9%</b>	<b>7.1%</b>	<b>0.9%</b>	<b>0.2%</b>	<b>2.9%</b>

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Note: "Other" category includes Chile, the Dominican Republic, and Panama.

Source: GAO analysis of U.S. Department of Commerce trade statistics and U.S. International Trade Commission tariff schedules.

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### **Some Import-Sensitive U.S. Products May Face Increased Competition If Barriers Are Lowered**

The United States maintains high tariffs on certain sensitive products whose production may decline if current trade barriers are reduced and competition from imports increases. The tariffs on some of these products are as high as 48 percent, and some products are subject to tariff-rate quotas with out-of-quota duties as high as 350 percent.<sup>8</sup> Central American FTAA countries have the largest share of imports facing tariffs greater than 15 percent. A large portion of these products is accounted for by textile and apparel goods, which until recently had only limited coverage under preference programs. Tariff rates on these products generally are between 20 and 33 percent. Textile and apparel products are important exports for Mexico, Caribbean Basin (including Central America) countries, and Andean Community countries. Mexico and the Caribbean Basin each account for about 14 percent (\$9.7 billion) of U.S. apparel imports in 2000 (Andean exports are very small in comparison). Mexico has preferential access through NAFTA, and Caribbean Basin exports have recently gained preferential access through the Caribbean Basin Trade Partnership Act. However, the United States offers the Caribbean Basin Trade Partnership Act unilaterally and can withdraw or modify it. Some FTAA countries would prefer to lock in access to the U.S. market through a reciprocal agreement like the FTAA.

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<sup>8</sup>A tariff-rate quota allows a certain amount of a product to be imported at a generally low "in-quota" rate. Any additional imports face a higher out-of-quota duty.

In addition to textiles and apparel, several agricultural products also receive protection through higher U.S. tariff rates and tariff-rate quotas. These include products such as tobacco, sugar, peanuts, dairy, and citrus products. For example, the out-of-quota tariff rate quota is 350 percent for tobacco and is above 100 percent for peanut products. The United States also provides domestic support programs for some of these industries, particularly dairy, sugar, and peanuts. Since limiting access to the market is essential for maintaining certain price levels, removal of trade barriers and increased competition from FTAA suppliers will impact these programs. U.S. Department of Agriculture's Economic Research Service reported that, while providing consumers access to more inexpensive imports, the FTAA might lead to significant declines in U.S. prices and production in the sugar, peanut, and orange juice markets. Brazil is a major producer of both sugar and orange juice, and Argentina already supplies over 85 percent of U.S. peanut imports. Sugar also has been a sensitive product in trade negotiations among Brazil, Argentina, and Chile.<sup>9</sup>

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### If FTAA Modifies Antidumping Rules, Effect on United States Could Be Mixed

More restrictive rules on antidumping investigations under the FTAA may have mixed effects on the United States because it is both the largest initiator and defendant in these cases in the hemisphere. Protections for import-competing U.S. industries, such as steel and fertilizers, might be more limited. However, U.S. exporters facing antidumping measures abroad might benefit. U.S. consumers and producers that would gain access to relatively cheaper imports may also benefit. Although antidumping duties are only applied on specific products and generally involve a small share of overall imports, they affect sensitive goods, and the threat of an investigation may lead exporters to restrain shipments.<sup>10</sup> Proponents of antidumping argue that it is important to some industries in the United States as protection against unfair competition when other trade barriers are lowered. The degree to which the FTAA agreement augments or modifies WTO provisions in these areas will affect how important the agreement is to current FTAA countries' practices. The United States has

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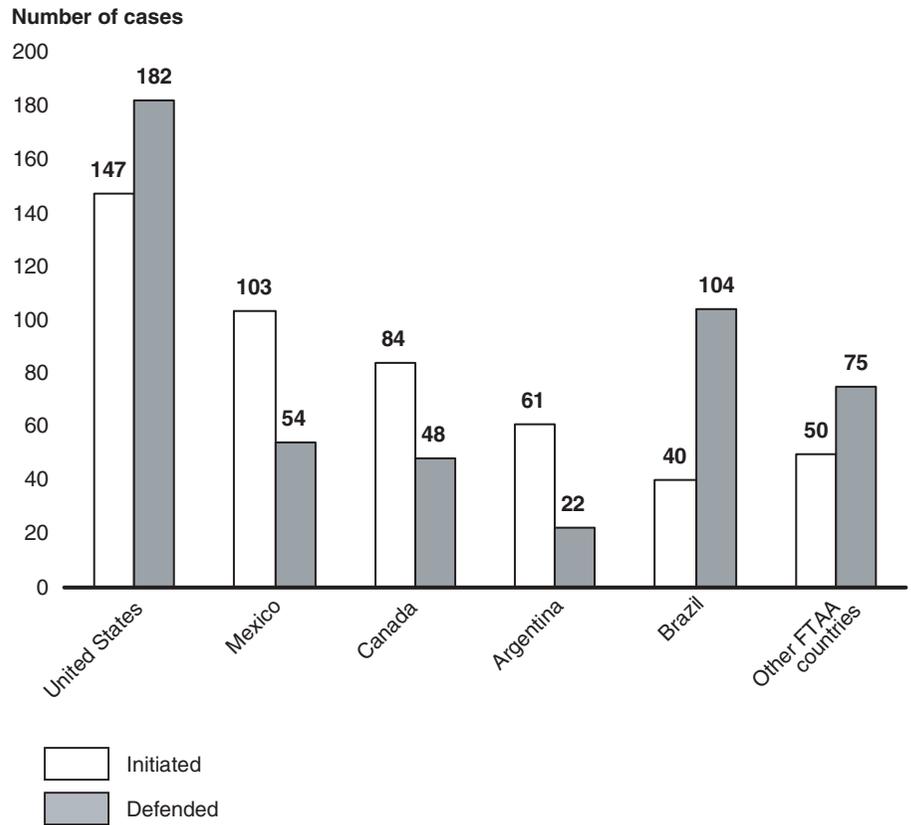
<sup>9</sup>For information on the U.S. sugar program, see *Sugar Program: Supporting Sugar Prices Has Increased Users' Costs While Benefiting Producers* (GAO/RCED-00-126, June 9, 2001).

<sup>10</sup>For example, the U.S. International Trade Commission found that all outstanding antidumping and countervailing duty orders in place in 1991 only affected approximately 1.8 percent of the total U.S. merchandise imports. The study found that the overall effect of removing these orders would be a \$1.59 billion net benefit gain for the United States.

argued for no changes that would restrain the use of antidumping by FTAA countries (see ch. 3 for more information on antidumping negotiations).

Until the early 1980s, Canada and the United States were the primary users of antidumping measures. However, Argentina, Brazil, and Mexico recently have become important users of antidumping measures. Of the 485 antidumping investigations initiated by one FTAA country against another between 1987 and 2000, the United States was the largest initiator (with 30 percent of the cases) and the largest defender (with 38 percent of the cases). Brazil, which was the fourth largest initiator (with 8 percent of the cases), was the second largest defender (with 21 percent of the cases). Figure 10 shows the number of cases initiated and defended by the top five FTAA users of antidumping. U.S. antidumping orders in effect as of April 2001 against FTAA countries include (1) certain steel products from Argentina, Brazil, Canada, and Mexico; (2) frozen concentrated orange juice from Brazil; and (3) salmon from Chile. The duties placed on these imports can be substantial and vary by product. For example, duties on imports from Brazil of silicon metal ranged between 87 and 94 percent in 2000, and duties on frozen concentrate orange juice were about 15 percent in 2001. The largest number of antidumping investigations against the United States are by its NAFTA partners Canada and Mexico, which account for 73 percent of all cases. Brazil is third with 14 percent, including measures in effect on certain chemical imports from the United States.

Figure 10: Antidumping Cases Initiated and Defended, by FTAA Country, 1987-2000



Source: United Nations Economic Commission for Latin America and the Caribbean.

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**Studies Suggest Overall  
Impact of FTAA  
Merchandise Trade  
Liberalization on U.S.  
Economy Will Be Small**

The relatively small size of non-NAFTA FTAA U.S. merchandise trade compared with the size of the U.S. economy will limit the overall impact of FTAA tariff liberalization on the U.S. economy. U.S. trade with FTAA countries outside of NAFTA was \$123 billion in 2000, only about 1 percent of the approximately \$10 trillion U.S. economy. However, certain sectors that are relatively more protected (both in the United States and abroad) may see significant changes in trade flows.<sup>11</sup> For example, some economic impact studies that use economywide models have found that U.S. exports in sectors such as furniture, textiles, and clothing and some agricultural products could increase substantially, while exports in sectors such as mining, base metals, and petroleum could fall slightly. Likewise, imports of certain metals, nonelectrical machinery and leather products could increase, while paper and wood imports could fall. Overall, these studies estimate a small but positive impact of an FTAA, with an increase in U.S. output annually of about 1 percent or less. However, the models focus only on tariff elimination and do not generally include other aspects of the FTAA agreement that are difficult to quantify, such as services and IPR.<sup>12</sup>

Some supporters of the FTAA argue that U.S. exports to non-NAFTA countries could grow significantly with a free trade agreement, just as U.S. exports to Mexico did through NAFTA. While U.S. exports to Mexico and other FTAA (non-NAFTA) countries in 1990 were about 7 and 6 percent of total U.S. exports, respectively, exports to Mexico rose to 14 percent (\$100 billion) of total U.S. exports by 2000.

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<sup>11</sup>Although trade barriers can be an important factor in determining how much trade occurs in a particular product, other factors also are important. For example, as the price of an import falls when a tariff barrier is removed, the degree to which trade and production change depends on how responsive consumers, domestic producers, and foreign producers are to the change in price.

<sup>12</sup>These studies generally do not capture dynamic effects that may come through specialization and economic growth.

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## Comprehensive FTAA Offers New Opportunities in Services, Investment, Intellectual Property Rights, and Government Procurement

The FTAA negotiations involve several areas in which the United States has important commercial interests but has few multilateral and bilateral agreements with FTAA countries. The United States is the world's leading exporter of services and one of the largest investors in Latin America. FTAA countries began liberalizing their service sectors and opening their economies to foreign investment as part of their economic reform programs. However, these reforms are relatively new and are not yet bound by international or bilateral commitments with the United States, as they would be under an FTAA. Also, as the leading producer of software, pharmaceuticals, and other cutting-edge technologies, protection of IPR is also an area of commercial importance to the United States. FTAA countries have been implementing relatively new multilateral and bilateral IPR commitments, and the United States is seeking to expand these in the FTAA. Finally, no FTAA countries besides the United States and Canada are party to the WTO Government Procurement Agreement. FTAA negotiations in this area present an opportunity to provide new commitments that would guarantee the opportunity for U.S. merchandise and services suppliers to compete for contracts in regional procurement markets.

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## FTAA May Expand Access for U.S. Service Providers and Secure Recent Liberalization

U.S. service providers stand to gain from liberalization in the FTAA as existing trade barriers are lowered in the region. The service sector is a commercially important area for the United States. World services exports were \$1.3 trillion in 1998, and the United States was the largest exporter, accounting for nearly 20 percent of services exports. By comparison, Canada, the next largest FTAA exporter, accounted for just 2.5 percent. Domestically, services account for 78 percent of the U.S. gross domestic product and a growing share (21 percent) of U.S. exports. Many FTAA countries' service sectors, such as telecommunications and energy, have traditionally been highly regulated and controlled by monopoly or state enterprises. However, as part of their larger reform process, many FTAA countries have begun privatizing state enterprises and opening some sectors to increased international competition.<sup>13</sup> For example, Brazil, Argentina, Chile, and Venezuela recently have begun privatizing segments of their telecommunications sector, and Argentina opened its domestic

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<sup>13</sup>Some U.S. civil society groups have raised concerns that the FTAA would lead some countries to also privatize state-provided social services, such as health and education. See chapter 3 for more information on this topic.

telecommunications market to full competition in 2000. Countries have initiated these reforms partly because service sectors provide resources for other elements of the economy and can be important engines for economic development.

However, the reforms are relatively new and countries have made only limited multilateral commitments in the WTO. For example, the number of commitments most FTAA countries (except for Canada, Argentina, and the United States) made in the WTO services agreement was ranked in a recent OAS study as moderately low to very low. Additional multilateral agreements on basic telecommunications and financial services have since been concluded and enjoyed greater participation.<sup>14</sup>

Also, U.S. service providers may receive less favorable treatment and access than other competitors. FTAA countries have engaged in numerous subregional trade agreements, many of which include services. These include Mercosur, CARICOM, the Andean Community, and many Mexican and Chilean bilateral free trade agreements. As they do for merchandise trade, such subregional agreements put countries not party to the agreement at a disadvantage.

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<sup>14</sup>Of the 34 FTAA countries, 22 made specific commitments under the Agreement on Basic Telecommunications. In addition, all of the countries except Brazil committed to adopt in whole or in part the Reference Paper on Pro-Competitive Regulatory Principles, which is a voluntary accompaniment that fosters competition in the telecommunications sector by providing regulatory principles to curb the anticompetitive behavior of telecommunications providers with monopolistic characteristics.

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## FTAA Investment Provisions May Help Secure Recent Reforms and Expand U.S. Investor Rights

A comprehensive FTAA could provide new protections for existing and future U.S. investments. The United States is one of the largest investors in Latin America, and the stock of U.S. FDI in FTAA countries accounted for about a quarter (\$265 billion) of all U.S. FDI abroad. Canada was the largest recipient, followed by Brazil and Mexico. FTAA countries, primarily Canada, accounted for only about 10 percent of FDI in the United States. Although FTAA countries have sought to attract more investment in their economies, the United States has investment treaties protecting the rights of investors with only a few FTAA countries. An FTAA agreement could provide stronger protections for U.S. investment in Latin America. Along with direct investment, capital also is provided to countries through short-term portfolio investments such as stocks and bonds.<sup>15</sup> The United States has proposed that each form of investment be covered under the FTAA agreement.

Investment is a commercially important area to the United States and one that is increasingly interconnected with trade. About 35 percent of goods exports and about 19 percent of services exports were related to U.S. investments abroad from 1990 to 1997. Multinational companies choose between producing a product in the domestic market and exporting it across the border, locating in the foreign market and producing the product there, or producing a product jointly in several countries. When trade barriers are high, the incentive to locate abroad is increased. Free trade agreements coupled with investment provisions can enable businesses to make more efficient investment decisions that are not distorted by government policies. Also, for some industries, particularly certain service sectors, local production of the service is preferred due to legal reasons and because it is more efficient. U.S. service sales through U.S.-owned foreign affiliates recently exceeded U.S. cross-border sales. Worldwide, sales by multinational corporations in the 1990s expanded at a much faster rate than global exports, and their levels of production grew from 5 percent of gross domestic product in 1982 to 10 percent in 1999, according to the United Nations. Sales of foreign affiliates worldwide (\$14 trillion in 1999 and \$3 trillion in 1980) are now nearly twice as high as global exports.

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<sup>15</sup>Foreign investment can be broken into two categories: FDI, in which an investor gains a certain share of ownership of an asset or company, and portfolio investment, in which an investor provides capital to an entity but has limited or no ownership of the borrower. The U.S. government defines direct investment as ownership of at least 10 percent of voting shares in a corporation. Other investments are considered portfolio investment. Whether portfolio investments will be included in the FTAA investment provisions is subject to negotiation. See chapter 3 for more information on these negotiations.

Economic reforms in many FTAA countries have recently opened some markets to increased investment, and the privatization of state-owned firms also has drawn significant foreign capital from the United States, Europe (particularly Spain), and elsewhere. Brazil was the largest recipient of new FDI in Latin America, receiving 41 percent (\$30 billion) in 2000, with Mexico second at 18 percent (\$13 billion). A high percentage of these investments went toward acquiring assets in the telecommunications, energy, and finance sectors. FDI in Brazil has been particularly large because the government privatized state-owned electric power companies, banks, and retail establishments. Brazil also changed its constitution to allow foreign investment in petroleum, shipping, telecommunications, and natural gas sectors and passed patent reform legislation that increased incentives for direct investment, according to the U.S. Department of Commerce. FDI in Argentina, Chile, and Venezuela also has increased substantially in recent years due to acquisitions of state-owned service enterprises. Overall, new FDI in Latin America was \$74 billion in 2000.

For U.S. investors, many of these new investments are not covered by bilateral or multilateral investment agreements. The United States has investment agreements in force with only 10 countries in the FTAA region. NAFTA provides strong protections for investments in Canada and Mexico, and the other eight agreements are bilateral investment treaties.<sup>16</sup> Not covered by any bilateral agreement with the United States are Brazil, which accounts for \$35 billion (13 percent) of the U.S. stock of FDI in FTAA countries; Chile, which accounts for about \$10 billion (4 percent); and Venezuela, which accounts for \$7 billion (3 percent). Multilateral provisions covering investments are limited. The WTO includes provisions related to investment in three of its agreements: services, goods, and IPR. However, there is no broad multilateral agreement that protects investment specifically. The Organization for Economic Cooperation and Development began negotiations on such an agreement, but these were suspended over differences among countries and complaints from civil society groups.

On the other hand, numerous subregional trade agreements and bilateral investment treaties exist within the FTAA region that do not include the

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<sup>16</sup>Some U.S. civil society groups have argued that the investor rights provided by NAFTA give corporations too much ability to challenge domestic social and environmental regulations. See chapter 3 for more information on this topic.

United States. Countries have liberalized their investment provisions to encourage reform and competition and to attract needed capital for economic development. Currently, all but three countries in the region (the Bahamas, St. Kitts and Nevis, and Suriname) have signed at least one bilateral investment treaty with another FTAA country. Many Caribbean countries have signed bilateral investment treaties with European countries, and Brazil has one with the EU. Subregional trade agreements also have included investment provisions, including NAFTA, Mercosur, the Andean Community, and several of the Mexican and Chilean bilateral free trade agreements.

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**United States May Gain  
Additional Intellectual  
Property Protections  
Through the FTAA**

As a leader in several areas of technology and medicine and with large investments in the research and development of new products and processes, the United States has important commercial interests in promoting the protection and enforcement of IPR abroad. The existing WTO agreement on IPR provides important disciplines that protect copyrights, patents, and other intellectual properties. The United States seeks to expand these provisions in the FTAA to provide greater protections.

Cross-border transfers of royalties and licenses provide one measure of international sales of intellectual properties.<sup>17</sup> These are fees collected by those who sell the rights to use industrial processes, techniques, formulas, and designs; copyrights and trademarks; business format franchising rights; broadcast rights; and the right to distribute and use computer software. In 1999, U.S. exports of these intangible intellectual properties amounted to \$4.3 billion to FTAA countries, with Canada accounting for 39 percent; Mexico, 18 percent; and Brazil, 12 percent. U.S. imports of intellectual properties were only \$844 million and came primarily from Canada (72 percent). Software licensing was one of the fastest growing segments of trade in intangible intellectual properties. In addition to intangible intellectual properties, the United States also is a large exporter of numerous products that embody intellectual properties such as videos, recordings, software, pharmaceuticals, chemicals, and other physical products. According to the U.S. International Trade Commission, the continued growth of U.S. intellectual property exports depends, in part, on the ability of U.S. trade partners to protect such properties. Also, a country's ability to attract foreign investment is partly tied to the strength of its protections on intellectual properties because companies want assurance that the intellectual properties they transfer to their new operations will be protected. Some U.S. industry associations have identified piracy and lost sales in the region due to IPR problems.<sup>18</sup> For example, piracy losses for software in Latin America were estimated by the industry at around \$870 million in 2000. At 58 percent, Latin America had the second highest piracy rate of all world regions, behind Eastern Europe.<sup>19</sup> Also, the pharmaceutical industry attributes lost sales ranging from \$66 to \$82 million in Argentina and Brazil to inadequate intellectual property protections.

Although FTAA countries' adoption on laws protecting IPR has improved significantly over the past decade, problems still exist. For example, the

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<sup>17</sup>The overall value of IPR to the United States is difficult to quantify because such an exercise would entail estimating intangible assets, calculating past expenditures for research and development, and covering a wide variety of industrial and service sectors.

<sup>18</sup>Estimates of lost intellectual property revenues are also difficult to construct because they require knowledge of the extent of piracy and estimates of the potential size of the market if piracy were eliminated. While difficult to estimate, piracy losses for certain sectors do exist.

<sup>19</sup>Piracy rates were estimated as the share of pirated software out of total demand for new software.

United States has initiated WTO dispute settlement procedures against Argentina and Brazil over limitations in their IPR laws.<sup>20</sup> Also, Paraguay was designated a priority foreign country under Special 301 provisions of the Trade Act of 1974 because of its role as a regional center for piracy, particularly of optical media. Other FTAA countries designated in the USTR Special 301 report on intellectual property protections included the Dominican Republic, Guatemala, and Peru.

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**FTAA May Provide U.S. Suppliers With Market Access in Government Procurement Where Few Commitments Exist**

Government procurement is a relatively important component of many FTAA countries' economies. FTAA countries' government expenditures comprise 10 to 15 percent of the gross domestic product and can be higher for some smaller economies. The IDB estimated the size of the Latin American procurement market in 1996 at between \$131 billion and \$197 billion. Currently, only the United States and Canada are party to the WTO Government Procurement Agreement. NAFTA also provides some government procurement access among the United States, Canada, and Mexico. The United States does not have any multilateral or bilateral agreements with the remaining FTAA countries. Therefore, the FTAA could provide significant new access to procurement markets for U.S. exporters of goods and services. U.S. agricultural and electrical manufacturing and pharmaceutical companies are among those supporting stronger government procurement provisions through the FTAA. Also, FTAA governments could benefit through reduced expenses due to more competitive and inexpensive products. Some civil society and labor groups argue that the FTAA should allow for government discretion for social or environmental reasons when making procurement decisions, and some U.S. companies favor maintaining programs that provide preferences for domestic suppliers. Since most FTAA countries have not yet made bilateral or multilateral commitments in this area, the degree to which they will grant access to their procurement markets in an FTAA is unclear.

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<sup>20</sup>The USTR recently announced that the dispute with Brazil would be negotiated through a newly created bilateral mechanism.

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# U.S. Trade and Investment With Countries in the Western Hemisphere

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U.S. trade and investment with Free Trade Area of the Americas (FTAA) countries has expanded rapidly over the past decade. Although comprising a relatively small share of the total, U.S. merchandise trade (exports plus imports) with non-North American Free Trade Agreement (NAFTA) FTAA countries more than doubled in the past decade. Machinery and transportation equipment was the largest merchandise trade category, followed by chemicals and plastics. Clothing, vegetable products, and minerals (including petroleum) were also important categories for some regional groups. U.S. cross-border trade in services (exports plus imports) is dominated by travel services, but non-NAFTA FTAA countries are important markets for a wide variety of private services, particularly insurance. Overall, U.S. investment in FTAA countries was \$660 billion in 1999. U.S. foreign direct investment (FDI) accounted for 40 percent of this total, while portfolio investments in stocks and bonds accounted for 60 percent.

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## U.S. Trade and Investment With FTAA Countries Grew Rapidly

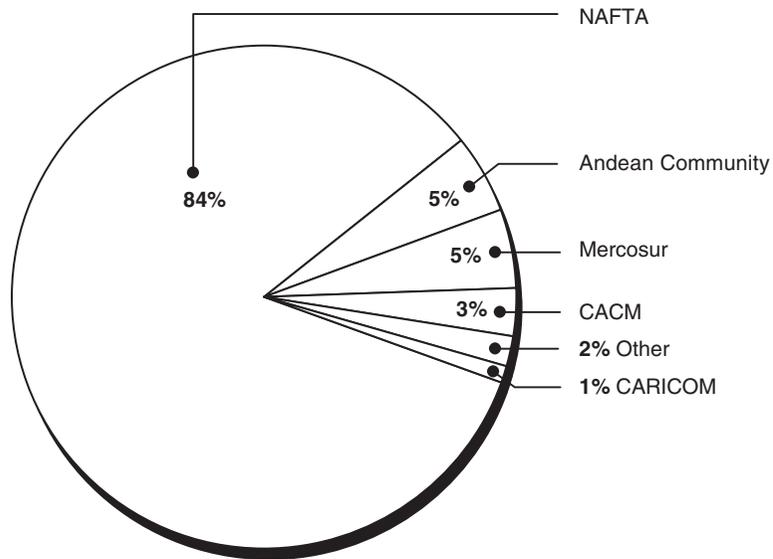
Over the past decade, U.S. trade and investment in the Western Hemisphere grew considerably, increasing both in value and as a share of overall U.S. trade and investment. U.S. merchandise trade with FTAA countries increased over 160 percent from 1990 to 2000 (\$282 billion to \$743 billion). Services trade increased nearly 60 percent from 1992 to 1999 (\$71 billion to \$112 billion), and the stock of U.S. FDI in FTAA countries increased 123 percent from 1990 to 1999 (\$119 billion to \$265 billion).

Through NAFTA (1994), the United States substantially increased its integration with Canada and Mexico, its two largest trading partners. NAFTA trade accounted for 32 percent of total U.S. merchandise trade in 2000, 14 percent of services trade in 1999, and 13 percent of U.S. FDI abroad in 1999. Trade with Mexico grew rapidly, accounting for 12 percent (\$235 billion) of U.S. merchandise trade in 2000, up from just 7 percent (\$57 billion) in 1990.

Compared with NAFTA, overall trade with the rest of the FTAA countries is relatively small. Trade with NAFTA partners Canada and Mexico accounted for 84 percent of U.S. merchandise trade with all FTAA countries (see fig. 11), as well as over 50 percent of U.S. services trade and U.S. FDI with FTAA countries.

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**Figure 11: Share of U.S. Merchandise Trade With FTAA Regional Groups, 2000**



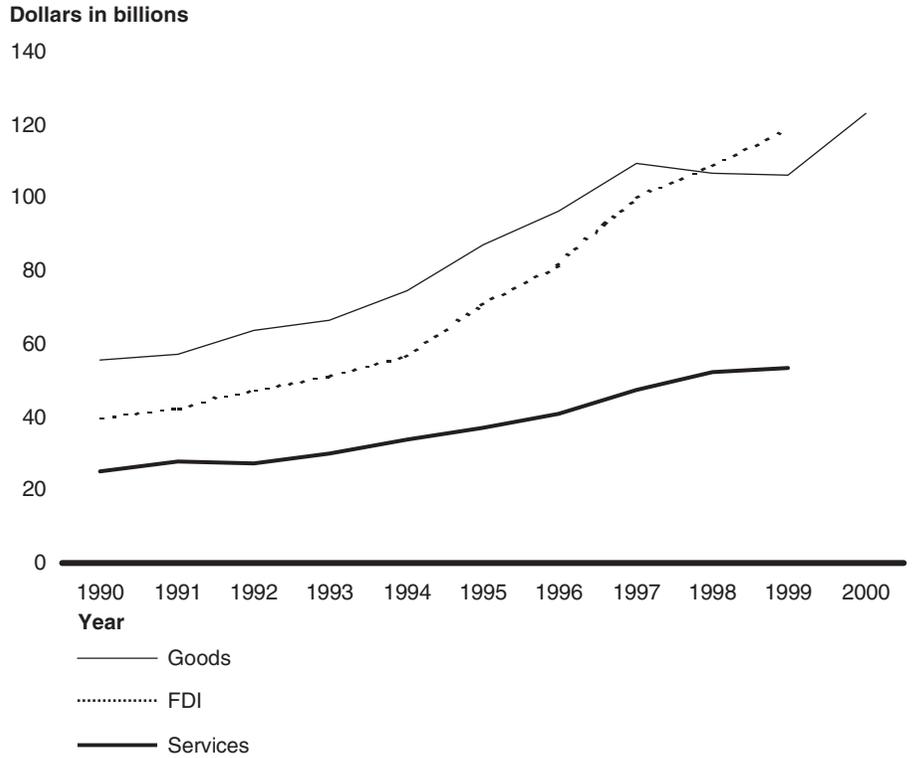
Note: Merchandise trade is exports plus imports of industrial and agricultural goods.

Source: GAO analysis of U.S. Department of Commerce data.

However, non-NAFTA FTAA countries' shares rose in services and investment. Figure 12 illustrates increases in U.S. trade and investment with non-NAFTA FTAA countries over the last decade. U.S. services trade with non-NAFTA FTAA countries increased from 10 to 13 percent of the total U.S. services trade, doubling from 1990 to 1999 (\$27 billion to \$54 billion). U.S. FDI in non-NAFTA FTAA countries nearly tripled (\$40 billion to \$119 billion), rising from 9 to 11 percent. In terms of merchandise trade, non-NAFTA FTAA countries maintained about a 6-percent share of growing U.S. trade from 1990 to 2000 (\$56 billion to \$123 billion).

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**Figure 12: U.S. Foreign Direct Investment, Merchandise Trade, and Services Trade With Non-NAFTA FTAA Countries, 1990-2000**



Note 1: Data were not available for trade in services and FDI in 2000.

Note 2: Values are in current (not constant) U.S. dollars.

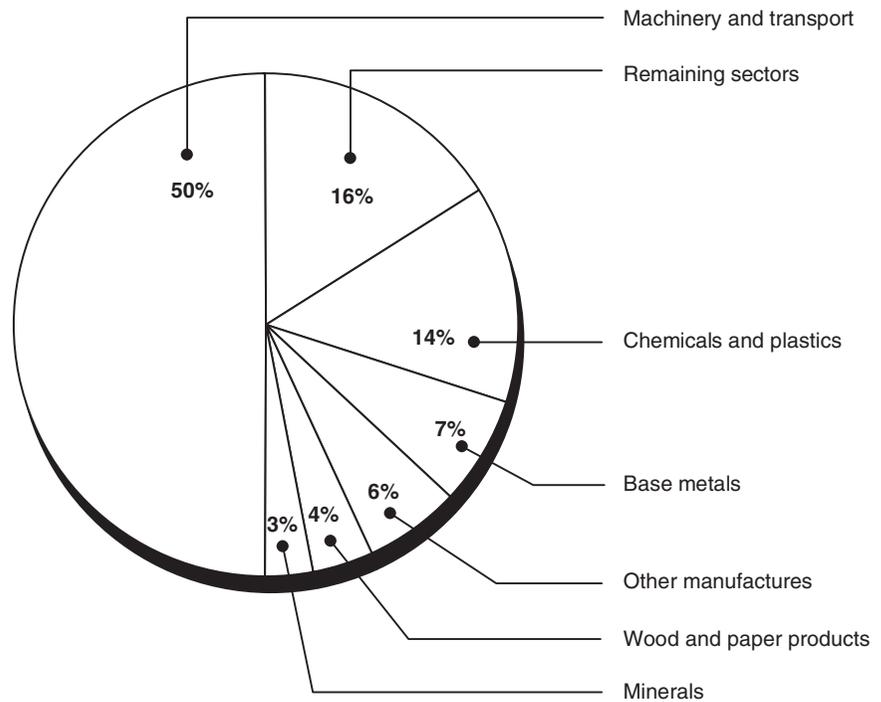
Note 3: Goods and services trade are exports plus imports. FDI is U.S. direct investment in non-NAFTA FTAA countries.

Source: GAO analysis of U.S. Department of Commerce data.

**U.S.-FTAA  
Merchandise Trade  
Was Dominated by  
Machinery and  
Transport Equipment;  
Agriculture Was a  
Relatively Small  
Share**

One-half of U.S. exports to FTAA countries were machinery and transportation equipment (see fig. 13). These included products such as computer equipment, airplane engines, and motor vehicle parts. Chemicals and plastics comprised the next largest export category at 14 percent. Table 7 shows the top three categories of exports and imports for each regional group. There is some variation in the importance of certain products among regional groups. For example, clothing rather than machinery and transport equipment was the largest U.S. export to Central America, partly because clothing producers in these countries use some U.S.-produced inputs to make clothing destined for the U.S. market.

**Figure 13: Share of U.S. Exports to FTAA Countries, by Sector, 2000**



Source: GAO analysis of U.S. Department of Commerce data.

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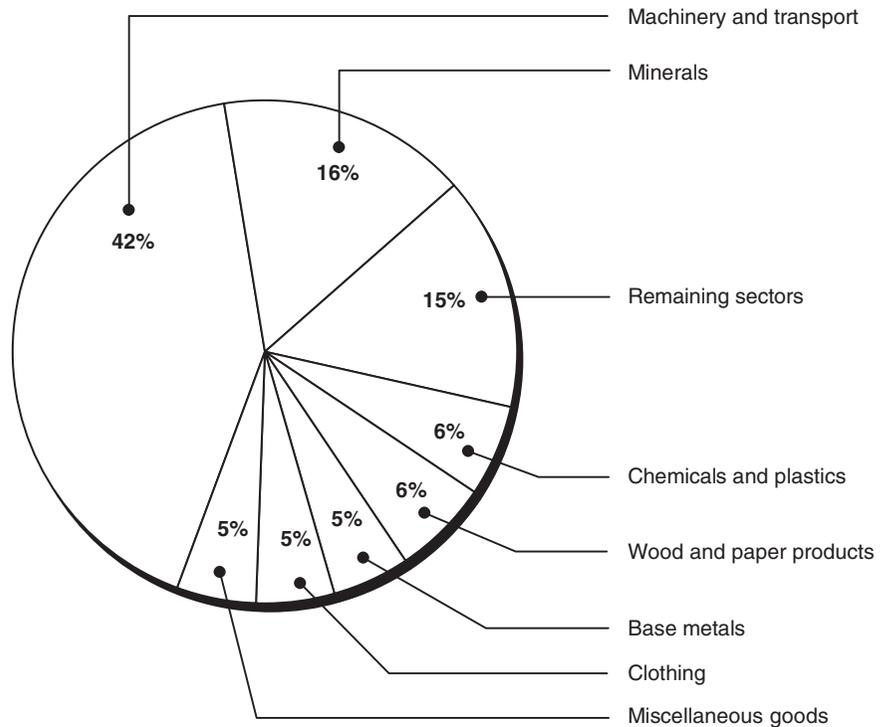
**Table 7: Top U.S. Export and Import Sectors by Regional Group, 2000**

<b>Regional group</b>	<b>Top three export sectors</b>	<b>Share (percent)</b>	<b>Top three import sectors</b>	<b>Share (percent)</b>
Andean Community	Machinery and transport	47	Minerals	71
	Chemicals and plastics	20	Vegetable products	6
	Vegetable products	6	Base metals	5
CACM	Clothing	30	Clothing	57
	Machinery and transport	22	Vegetable products	15
	Chemicals and plastics	11	Machinery and transport	12
CARICOM	Machinery and transport	33	Minerals	36
	Chemicals and plastics	11	Chemicals and plastics	25
	Miscellaneous	10	Clothing	15
Mercosur	Machinery and transport	55	Machinery and transport	26
	Chemicals and plastics	23	Base metals	12
	Other manufactures	8	Minerals	12
NAFTA	Machinery and transport	52	Machinery and transport	49
	Chemicals and plastics	14	Minerals	12
	Base metals	8	Wood and paper	7
Other	Machinery and transport	39	Clothing	30
	Clothing	13	Vegetable products	11
	Chemicals and plastics	12	Base metals	10

Source: GAO analysis of U.S. Department of Commerce data.

Like exports, U.S. imports from FTAA countries were dominated by machinery and transportation equipment (see fig. 14). However, minerals (especially petroleum) were the second largest import category, comprising 16 percent of the total. Wood and paper products were also important, comprising 6 percent of U.S. FTAA imports along with chemicals and plastics. There was greater diversity in U.S. imports from various regional groups compared with U.S. exports. For example, clothing was the one of the largest import categories for Central American and Caribbean countries and vegetable products were important imports from the Andean Community, Chile, and Central America. However, U.S. imports from some FTAA countries were dominated by one type of product group. For instance, U.S. imports of minerals accounted for 88 percent of all U.S. imports from Venezuela (56 percent for Ecuador and 51 percent for Colombia). Similarly, clothing accounted for 88 percent of U.S. imports from Haiti (84 percent for El Salvador and 78 percent for Honduras).

Figure 14: Share of U.S. Imports From FTAA Countries, by Sector, 2000



Source: GAO analysis of U.S. Department of Commerce data.

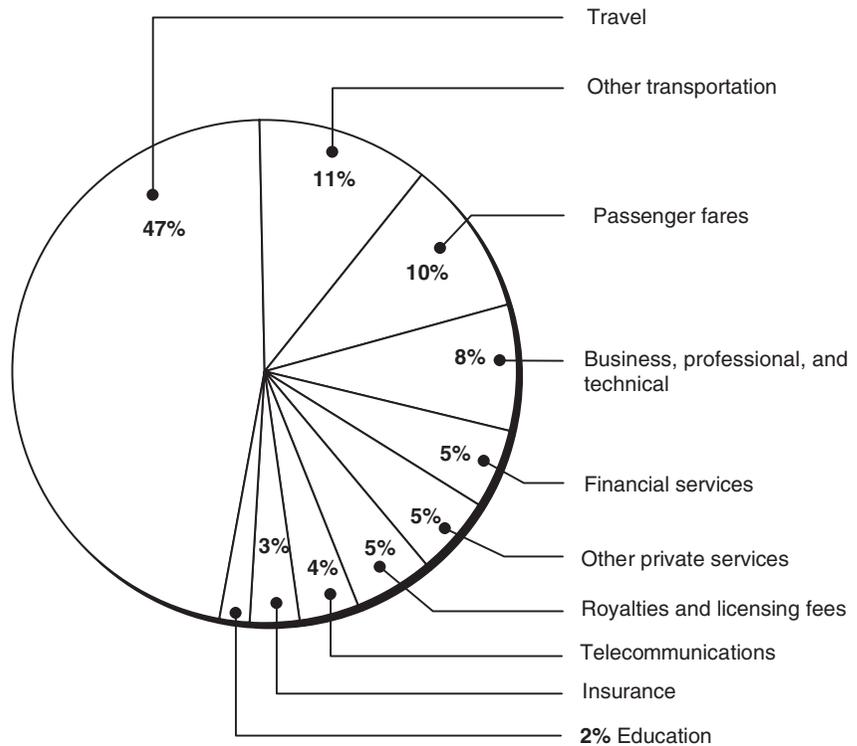
Agricultural trade was a relatively small and decreasing portion of overall trade between the United States and FTAA countries. Although increasing in value over the decade, agricultural trade with FTAA countries fell from 8 percent in 1990 to 6 percent in 2000 as a share of the total U.S. FTAA trade. The majority of U.S. agricultural exports were accounted for by vegetable products (41 percent, \$7 billion) and prepared food and beverages (36 percent, \$6.4 billion). Imports were somewhat more diversified with 36 percent accounted for by vegetable products (\$9.7 billion), 33 percent by prepared food and beverages (\$8.8 billion), and 29 percent by animal products (\$7.7 billion). Fats and oils made up the remainder of trade, accounting for a small share of both imports and exports (about 1 to 4 percent). FTAA agricultural trade is an important component of overall U.S. agricultural trade. About 54 percent of all U.S. agricultural imports came from the Western Hemisphere, while about 36 percent of U.S. agricultural exports went to FTAA countries. Agricultural trade with

Mercosur was minimal, accounting for only 1 percent of U.S. agricultural exports and 8 percent of Mercosur's world agricultural imports.

## Travel and Transportation Were the Largest Sectors in U.S. Cross-Border Trade in Services

For U.S. services trade with FTAA countries, travel was the largest sector in cross-border trade, accounting for nearly half of the total in 1999. Passenger fares and other transportation services combined accounted for 21 percent of U.S. services trade. Other types of services, such as business, telecommunications, insurance, and financial services, each accounted for small shares of total cross-border transactions, generally between 2 and 8 percent. This pattern of distribution is relatively similar to the pattern of overall U.S. services trade with the world. (See fig. 15.)

Figure 15: Share of Service Subsectors in U.S.-FTAA Trade, 1999



Note: Service trade is exports plus imports of private cross-border services. Private services exclude government and military services.

Source: GAO analysis of U.S. Department of Commerce data.

Canada was generally the largest U.S. export market for each of the service subsectors, followed by Mexico and Brazil. Some sectors have experienced rapid growth. For example, U.S. exports of insurance services to Latin America increased by 81.3 percent in 1999 to \$1.6 billion.<sup>1</sup> These exports accounted for 71 percent of U.S. world cross-border insurance exports.<sup>2</sup> At the same time, some service subsectors contracted. U.S. exports of computer and data processing services to South and Central America decreased by 17.7 percent in 1999, for a total of \$190 million and accounting for 8.3 percent of total U.S. exports of such services. Overall, U.S. services exports and imports with FTAA countries increased nearly 60 percent from 1992 to 1999.

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## U.S. Investment in FTAA Countries Nearly Evenly Split Between FDI, Stocks, and Bonds

The FTAA region was an important destination for U.S. FDI and purchases of bonds. U.S. FDI in FTAA countries accounted for about a quarter (\$265 billion) of all U.S. FDI abroad. International investment can take the form of long-term FDI through acquisition or new operations and short-term portfolio investments through stocks and bonds. U.S. holdings of FTAA bonds accounted for 37 percent (\$206.2 billion) of U.S. investments in foreign bonds. However, U.S. holdings of FTAA stocks only accounted for 9 percent (\$189.8 billion) of U.S. investments in foreign stocks (see fig. 6). FDI was the largest category of U.S. investment in FTAA countries, accounting for 40 percent of the total. Canada accounts for over 40 percent of each category. However, Canada's share of U.S. FDI to FTAA countries fell from 58 percent in 1990 to 42 percent in 1999, while Brazil and Mexico both increased their shares to 13 percent each.

In 1999, 43 percent of the stock of U.S. FDI in non-NAFTA countries was in finance, insurance, and real estate, while 26 percent was in the manufacturing sector. For the NAFTA countries of Canada and Mexico, the ratio was nearly reversed with 43 percent of U.S. FDI in the manufacturing sector and 22 percent in finance, insurance, and real estate. For some countries, U.S. investment was concentrated in particular subsectors. For example, Venezuela received a larger share of its U.S. FDI in the petroleum sector, and Brazil, Argentina and Chile received a larger portion in the

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<sup>1</sup>Cross-border insurance exports are measured as the net between foreign premiums paid in minus claims paid out.

<sup>2</sup>Due to data limitations, it is not possible to determine which countries within the region account for the majority of these exports.

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banking sector. The automobile sector has already received large investments from U.S. automakers, particularly in Mercosur, where trade barriers exist and investment incentives are offered. General Motors is the second largest multinational in the region in terms of sales.

FTAA countries are responsible for a relatively small share of overall investment in the United States. Total FTAA FDI in the United States accounted for only 10 percent of all FDI in the U.S. market. Canada was the largest FTAA holder of FDI in the United States, accounting for 8 percent of overall FDI. Latin American countries combined accounted for between 1 and 3 percent of total foreign investment in U.S. FDI, stocks, and bonds in 1999.

# GAO Contacts and Staff Acknowledgments

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## GAO Contacts

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