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A Free Trade Area of the Americas: Status of Negotiations and Major Policy Issues

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Summary

In 1994, 34 Western Hemisphere nations met at the first Summit of the Americas, envisioning a plan to create a Free Trade Area of the Americas (FTAA) by January 2005. Nine years later, the third draft text of an agreement is being readied for the eighth trade ministerial scheduled for November 17-21, 2003 in Miami. However, serious differences between Brazil and the United States, similar to those that led to the collapse of the September 2003 WTO talks in Cancún, Mexico, invite a cautious assessment. The Miami ministerial may determine if the FTAA negotiations proceed on time and with the goal of achieving a comprehensive agreement, as first conceived. The 108th Congress has followed developments closely as it exercises its expanded consultative and oversight role per the Trade Promotion Authority (TPA) provisions of the Trade Act of 2002 (P.L. 107-210). This report will be updated periodically.

Background and Negotiation Process

For two decades, growing trade liberalization in Latin America has raised the prospect of a previously unrealized idea – a Free Trade Area of the Americas (FTAA) involving 34 nations of the region. Latin America's trade reform has been christened the "New Regionalism" to reflect the evolution from an "old" system of closed subregional agreements that dominated in the early post-war era, to one based on more open and deeper commitments both within and outside the region, and all part of broader policy reform efforts that emerged in the aftermath of the 1980s debt crisis. Examples include the North American Free Trade Agreement (NAFTA), the Southern Cone Common Market (Mercado Común del Sur), and the Central American Common Market (CACM), as revitalized in the 1990s. Combined with unilateral, bilateral, and multilateral efforts, these subregional agreements have fostered trade opening, with average tariff rates in Latin America having fallen from 40% in the mid-1980s to under 12% by 2000.¹

¹ Inter-American Development Bank. *Beyond Borders: The New Regionalism in Latin America. Economic and Social Progress Report*. Washington, D.C. 2002, pp. 25, 32-33, and 62.

Many see the FTAA as the next important step for Latin American trade opening and an essential element of an export-led development strategy. There are three important aspects to this strategy: 1) increased trade within the Latin American region; 2) increased Latin American trade with the U.S. market; and 3) increased foreign investment. Intraregional trade has grown precipitously and is recognized as a key factor in output and productivity growth for the region. Latin America's trade has grown faster than the world average over the last decade, in part due to growth in traditional exports such as agriculture and other commodities. Increasingly, as in cases such as Mexico and Central America, diversification into light manufacturing has been a direct result of closer trade and investment ties with the large industrial U.S. market. Therefore, the FTAA raises expectations that it will lead to growth in traditional exports as well as promote trade diversification with the help of foreign investment.²

Despite the noted progress in Latin America's trade liberalization, the multitude of free trade agreements (FTAs) that the "New Regionalism" has spawned can also lead to inefficient and discriminatory trade. The impetus to correct this situation, combined with the conviction that trade liberalization is a cornerstone for reform and development, has generated widespread official support for the FTAA, although skeptical attitudes prevail as well. This includes the United States, which acknowledges its growing trade relationship with Latin America, and the potential for the FTAA to support broader U.S. goals in the region such as promoting democracy, regional security, and drug interdiction efforts. But, these goals must be reconciled with interests of import competing industries, as well as those of labor and environment groups. Still, an FTAA is expected to reduce barriers to trade region wide, allowing all countries to trade and invest more with each other under the same rules. Defining those "rules," however, is no small task.

Writing the FTAA agreement falls to nine negotiating groups responsible for: market access; agriculture; investment; services; government procurement; intellectual property rights; subsidies, antidumping, and countervailing duties; competition policy; and dispute settlement. Each group is chaired by a different country and the overall process is directed by the Trade Negotiations Committee (TNC). The TNC chair has rotated every 18 months or following a trade ministerial meeting, as have chairs of the various negotiating groups. In addition, there is a consultative group on smaller economies, a committee on civil society to provide input from non-government parties (labor, academia, environmental groups), a technical committee on institutional issues, and a joint government-private sector committee of experts on electronic commerce. Draft FTAA texts reflect the input of all countries, and in some cases groups of countries such as Mercosur, with "bracketed text" reflecting areas of disagreement. In an unprecedented nod to transparency in the trade negotiating process, the draft texts are being released upon completion in all four official languages.³

Since 1994, there have been three summits and seven trade ministerial meetings. The first draft of the FTAA was adopted at the Quebec City Summit in 2001 and a second draft was completed at the Quito ministerial in November 2002. At that time, Brazil and

² Ibid., pp. 24-29 and Weintraub, Sidney. *Development and Democracy in the Southern Cone*. Center for Strategic and International Studies, Washington, D.C., February 2000. pp. 12-13.

³ See: [<http://www.ustr.gov/regions/whemisphere/ftaa.shtml>] and [<http://www.ftaa-alca.org>].

the United States became co-chairs of the TNC and were charged with guiding the negotiating process to its completion.⁴

Major Negotiation Issues

The FTAA involves a commitment by 34 countries to consider a broad trade policy agenda, the difficulty of which has become increasingly clear of late. Essentially, the United States has many different priorities than some key Latin American countries, making a balanced and mutually acceptable agreement difficult to define, as seen in a short review of the negotiating issues.

Market Access and Trade Remedy Issues. The negotiating committee on market access faces one of the most difficult challenges, particularly given that the two largest regional economies, Brazil and the United States, have different priorities. The United States, along with Canada, has the lowest average tariff rate in the Western Hemisphere of 4%. But Brazil and other countries argue that many of their exports are subject to U.S. tariff rate quotas (TRQs) and their related high peak tariffs, as well as countervailing duty and antidumping actions. Brazil, by contrast, has much lower peak tariff rates, but has the second highest average regional tariff rate of 15% and relies on other trade barriers, as well.⁵ The United States has focused its negotiation position on reducing overall tariff rates as the primary goal in market access discussion, but its specific offer differs significantly from what Brazil proposes (see next section).

Latin American countries, by contrast, have been pressing to address U.S. trade remedy laws, domestic support for farmers, and peak tariff rates, with Brazil specifically focused on opening the U.S. market further to its agricultural, steel, and textile exports. Specific instructions were given in Quito to the agriculture negotiating group. Agriculture is the most protected sector in most economies and for many Latin American countries, is critical for their economic well being. Historically, it has proven to be among the most difficult areas to liberalize, yet many Latin American countries consider tackling U.S. agricultural trade policies central to any discussion on market access. The United States has made clear, however, that it is uninterested in negotiating an agricultural subsidies agreement that does not include Europe and Japan, which will require resuscitating World Trade Organization (WTO) talks following their September 2003 collapse in Cancún, Mexico, in part over agricultural issues.⁶

Other Trade Barrier Issues. Services trade is another vital issue for the United States given its competitive strength in such areas as financial services, transportation, engineering, and technology consulting. Beyond market access, there are issues critical to the United States that will take center stage, if the recently completed U.S.-Chile FTA

⁴ Summits of the Americas took place in Miami (1994), Santiago (1998), and Quebec City (2001). Trade ministerial meetings were hosted in Denver (1995), Cartagena (1996), Belo Horizonte (1997), San Jose (1998), Toronto (1999), Buenos Aires (2001), Quito (2002), and will be followed by Miami (November 17-21, 2003).

⁵ 2000 unweighted average Most Favored Nation (MFN) applied tariff rates reported in: Inter-American Development Bank, *The New Regionalism in Latin America*, p. 62.

⁶ For details on agricultural trade issues, see: CRS Report RL30935, *Agricultural Trade in the Free Trade Area of the Americas*, by Remy Jurenas.

negotiation is any indication. Intellectual property rights (IPR), government procurement, and competition policy are among the most important. Intellectual property rights violations have hurt U.S. producers throughout the world and few countries have laws protecting intellectual property to the extent the United States does. Copyright issues and protection of digital products are among the more important issues to resolve. This proved difficult to resolve in the Chile bilateral agreement and may also require extensive discussion to change laws in over 30 other countries. Competition policy is another difficult area because of the need to standardize approaches regulating domestic economic activity, although it may prove more easily reconcilable than IPR disagreements.

Labor and Environment Provisions. Another contentious issue is language covering labor and environment provisions. Developing countries resist these provisions, arguing that they: 1) should be left to domestic governing authorities or the relevant international organization; 2) may be difficult for developing countries to meet; and, 3) can be used for protectionist purposes. Concern from the developed world, on the other hand, is that different standards among trading countries may provide competitive advantages or disadvantages (lower or higher costs to produce). Specifically, the concern goes to ensuring that lower environmental or labor standards in developing countries not become a basis for exploitive, lower-cost exporting, or serve to attract foreign capital investment, and that higher standards, as in the United States, not be challenged as disguised barriers to trade. Environmental advocates also point to the social impact of failure to enforce pollution abatement and resource management laws.

NAFTA set a precedent for including labor and environment provisions in trade side agreements. Since then, the debate has intensified and has turned on where the language should be placed in the agreement, the specificity of the provisions, and how dispute resolution will be handled. A key reference point is the U.S.-Jordan FTA, which incorporated labor and environment provisions into the text of the agreement and provided for a single dispute resolution mechanism for both commercial and social issues. The wording emphasizes that each country will be held accountable for enforcing its own laws, will reaffirm its commitments to basic United Nations International Labor Organization (ILO) labor standards, and not diminish its standards as a way to pursue trade and investment opportunities. Trade sanctions, although not expressly called for, are also not excluded as a possible remedy for noncompliance.

Many in the United States and Latin America found these provisions too strict and resistance arose over the possible use of trade sanctions. The U.S.-Chile FTA calls for limited “monetary assessments” to address noncompliance, with a recourse to loss of trade benefits to collect unpaid fines, if needed. Labor advocates, however, argue that the U.S.-Chile FTA steps back from the U.S.-Jordan commitments because dispute resolution expressly applies only to upholding domestic labor laws, not reaffirmation of ILO standards nor “non-derogation” from domestic standards.⁷ This issue, however, hinges on one’s interpretation of congressional intent of negotiating objectives, as written in the TPA, which the USTR argues it has met in the Chile agreement. The monetary

⁷ Report of the Labor Advisory Committee for Trade Negotiations and Trade Policy (LAC). *The U.S.-Chile and U.S.-Singapore Free Trade Agreements*. February 28, 2003. pp. 5-9 and USTR Response to the Labor Advisory Committee (LAC) report on the proposed FTAs with Singapore and Chile. Undated. See: [<http://www.USTR.gov>].

assessment is also questioned as a “meaningful deterrent” for various reasons, which is also disputed by the USTR. Given the continuing debate over labor and environment language, the issue appears to remain open with respect to the FTAA.

Outlook: A U.S.-Brazil Compromise?

The eighth FTAA ministerial takes place November 17-21, 2003 in Miami, at which time the prospect of meeting the January 2005 deadline will become clearer. To meet this deadline, Brazil and the United States, the TNC co-chairs and the two countries with the most divergent perspectives on the FTAA, must resolve disagreements over how to proceed. Although both countries reiterated their commitment to meeting this deadline in a mini-ministerial held on June 13, 2003, and at a meeting between Presidents Bush and Lula a week later, an impasse developed on agricultural and other issues at two September 2003 meetings, the WTO ministerial at Cancún, Mexico and the FTAA TNC meeting in Trinidad and Tobago. In response, sixteen countries held a “mini-ministerial” on November 7-8, 2003 in Washington, D.C. to explore options for the FTAA.

The current tension heated up in May 2003 when Brazil responded to U.S. FTAA offers. Brazil challenged three U.S. policy initiatives. First, U.S. pursuit of subregional trade arrangements such as NAFTA, the Andean Trade Promotion Act (ATPA), and Caribbean Basin Initiative (CBI), as well as, bilateral deals with Chile and Central America, which it views as isolating the Mercosur countries, and especially Brazil, in the context of the FTAA negotiations. Second, U.S. refusal to address agricultural subsidies and antidumping issues in the FTAA, which Brazil considers as effectively formalizing barriers to Brazil’s key export sectors and to be in conflict with the FTAA’s single undertaking provision. Third, the U.S. offer of “differentiated” market access, which Brazil objects to because it would receive the least favorable treatment (although not by a great deal) compared to smaller and lesser developed countries.

Brazil responded with its own approach, referred to as the “Three Track Proposal.” The Brazilian offer would: 1) have the United States conduct market access discussions with the Mercosur countries, known at the “4+1” arrangement; 2) jettison investment, government procurement, services, and IPR issues along with agricultural subsidies and antidumping (per U.S. wishes) to the Doha WTO round; and 3) include the remaining rules-based issues in the FTAA discussions. This might include rules of origin, some disciplines on investment, competition policy, and other issues not dealt with elsewhere. The United States rejected this so-called “FTAA lite” proposal and argued for a comprehensive FTAA.

Brazil’s stand reflects both offensive and defensive postures, depending on the issue involved. A key issue is agriculture. By ruling out discussion of domestic agricultural subsidies in the FTAA, which most economists acknowledge as price and production distorting, the United States became vulnerable to Brazil’s hard line critics, despite these critics being chastised by some members of the Brazilian press and business groups. The hardline position reflects first Brazil’s support for its strong agribusiness, which is viewed as the sector most likely to lead the country toward greater growth and development, while also providing needed exports and public revenues to help keep its external balance in line and reduce its large public debt. The development of Brazil’s interior also hinges on the “New Agricultural Frontier,” which is a matter of both economics and national pride. Given that some 70% of Brazil’s agricultural exports go to Europe and Asia, and

less than 5% to the United States, Brazil has aggressively pursued improving its agricultural position vis-a-vis the United States as a negotiating objective..

Equally important to understanding Brazil's trade stand is its defensive position toward opening certain sectors of the economy where it feels less prepared to compete internationally. Brazil's hard stand against U.S. antidumping and subsidy laws has played out as a way to restrict access to its own sensitive sectors. Each of the four issues that Brazil would like to opt out of have either protectionist interests or structural economic problems that form the basis for supporting an "FTAA lite." In services, Brazil wants more time before taking on the United States in such areas as insurance and technology consulting, among others. IPR presents a problem because the United States dominates in ownership of intellectual property and Brazil is renown for its piracy. Government procurement is another area where Brazil prefers to support its own firms for as long as possible. As an example of a structural issue, Brazil's history of inflation and high interest rates has led to the development of credit markets and a banking system that technically relies on the subsidization of long-term lending rates through the federal development bank, while private banks tend to hold high-yield federal bonds that are low risk compared to investing in capital projects. This situation presents questions for both financial services and investment chapters and will not be changed quickly.

The Miami ministerial will have to find a compromise between the comprehensive approach of the United States and Brazil's less ambitious counterproposal. At the November 2003 mini-ministerial in Washington, D.C., apparently a "more flexible" proposal was discussed in which a two-tier FTAA would involve a minimum commitment for all countries to adopt chapters on such issues as market access, rules of origin, and customs administration, for example. Countries would then have a option to enter into other chapters on a reciprocal basis such as IPR, investment, services, and government procurement, among others. The United States would not have to address antidumping and subsidies issues.

The details of such a proposal will not emerge until the Miami meeting. For the United States, perhaps the critical factor is being able to move ahead with an agreement that is as comprehensive in scope, but limited in terms of being operational all at once. In such a case, even if the time line to eliminate barriers to trade or to open markets is very long, it may at least be defined in terms of a finite number of years in many cases and provide a framework that would be in place to encourage deeper integration at some future date with countries reluctant to do so at first. For Brazil, it seems to have accepted that domestic agricultural subsidies may be dealt with in the WTO and so an FTAA that provides sufficiently generous phase-out period for reducing protection of its sensitive sectors may be acceptable.

It is by no means assured that such a compromise will emerge, or that it will appeal to all FTAA negotiating countries. Should talks in Miami fail, however, the alternative is not the status quo, but rather living with the growing array of bilateral agreements that complicate and introduce inefficiencies into regional trade patterns. The United States appears poised to pursue this option even more aggressively than it already has should the Miami ministerial prove disappointing. Perhaps it is this prospect combined with the promise that many see in a full regional agreement that may ultimately sway opinions in all 34 countries.