

OAS TRADE UNIT STUDIES

Analyses on trade and integration in the Americas

**Mechanisms and Measures to Facilitate
the Participation of Smaller Economies
in the Free Trade Area of the Americas:
An Update**

**Mecanismos y Medidas para Facilitar la
Participación de las Economías más Pequeñas
en el Area de Libre Comercio de las Américas:
Actualización**

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MECHANISMS AND MEASURES TO FACILITATE THE PARTICIPATION OF SMALLER ECONOMIES IN THE FREE TRADE AREA OF THE AMERICAS: AN UPDATE

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INTRODUCTION

This report constitutes an update of a previous report, by the same name, prepared by the Trade Unit and presented for the consideration of the Working Group on Smaller Economies at its fourth and fifth meetings. This update was prepared at the request of the Chairman of the Working Group on Smaller Economies. It deals with the same set of issues examined in the previous version. The intention of the report is to contribute to the deliberations of the Working Group on Smaller Economies following the request made at the FTAA Belo Horizonte Ministerial that the Working Group on Smaller Economies "make specific suggestions to the Vice Ministers as to measures that would allow their effective participation in the FTAA process."

As in the previous version of the report, the suggestions included in this paper to deal with the issue of smaller economies in the context of the FTAA negotiations are of a broad and preliminary nature, as many of the critical decisions regarding the objectives, approaches, structure and venue of the FTAA negotiations have yet to be decided. The paper identifies some measures that could be considered in the FTAA negotiations to take into account the particular needs of the smaller economies with regard to the areas which will eventually be included in a FTAA agreement. These measures could, if the FTAA participants so decide, be further considered in the course of the negotiations. The measures can be grouped according to the following categories:

- ?? differentiated schedules for compliance with commitments, such as the ones that would be applied in the case of the elimination of tariff barriers;
- ?? quantitative thresholds to allow recourse to trade remedy instruments, as in the case of safeguards and in the use of de minimis requirements for triggering antidumping actions against imports from smaller countries;
- ?? provisions allowing for more flexibility in the treatment of goods originating in smaller economies, such as those that refer to regional content requirements for the determination of origin;
- ?? provisions allowing smaller economies to implement certain commitments at the subregional level in order to pool resources and technical expertise, such as those suggested in the case of FTAA commitments in intellectual property rights; and
- ?? technical assistance and cooperation measures to support national efforts for the development of the necessary laws and regulations, administrative infrastructure, human resource capacity and adequate enforcement agencies to implement FTAA commitments in various fields. This is an approach suggested in almost all areas to be included in the FTAA, given the great need of smaller economies to strengthen their capacity in the areas of trade policy formulation, negotiation and institutional adaptation in order to participate effectively in, and benefit fully from, hemispheric free trade.

PRINCIPLES

One significant challenge posed by Western Hemispheric free trade is how to design rules that apply both to large and highly developed economies and to the smaller developing countries in the region. The Heads of State and Government attending the Summit of the Americas acknowledged this problem when they stated that the economic integration and the creation of free trade will be complex endeavors, particularly in view of the wide differences in the levels of development and size of economies in our Hemisphere, and that they would remain cognizant of these differences as [they] work toward economic integration in the Hemisphere.

Also, as reiterated in the various FTAA Ministerial Declarations, the FTAA would represent a single undertaking of mutual rights and obligations which means that its adherents will have to agree to all or none of the provisions of the negotiated text. It also means that any specific treatment of the smaller economies would have to be implemented not by permitting these economies to pursue less demanding obligations than their larger counterparts but by allowing them more flexibility for the implementation of the FTAA general rules and disciplines, and by providing them with the necessary assistance, including technical assistance and material support, to meet their commitments.

This is commensurate with the evolving environment in which trade relations between larger and more developed countries and smaller developing nations has been taking place and the changing attitude of both developed and developing countries towards special and differential treatment in international trade. Although preferential treatment still continues to be an important feature of international trade relations, it is now being applied not so much as an exemption to general rules and disciplines, but through specific, transitory and negotiated provisions to allow beneficiary countries more flexibility and time for the implementation of trade commitments to be undertaken by all countries in the context of plurilateral and multilateral trade liberalization efforts. This trend has manifested itself both in the Uruguay Round and in the newer and recently reformed trade and integration arrangements in the Western Hemisphere.

In the FTAA negotiations, measures to facilitate the participation of the smaller economies should not necessarily be approached as a de facto right ingrained in an a priori manner at the inception of the negotiating process, but should result from specific negotiations among the participating countries. This would allow the FTAA participants to take into account the particular concerns of individual countries or groups of countries, including the specific sensitivities that may affect particular sectors or products. To that end, the FTAA should allow for differentiated treatment measures that would be negotiated in accordance with the particular concerns of the smaller economies.

Consideration could also be given in the FTAA negotiations to the possibility of applying certain differentiated treatment provisions on a group basis to the smallest countries and, in addition, allowing these countries to implement certain commitments on a subregional level in order to pool resources and technical expertise. The basic thrust would be that flexibility be introduced in the system so as to enable smaller countries to face the dual challenge of having to develop the necessary legislative, administrative and human resource capacity for implementing the FTAA, while at the same time maximizing the opportunities offered by hemispheric free trade.

SPECIFIC MEASURES

As pointed out above, the specific measures presented in this report cover the same issues as the previous report. Most of these issues have been the subject of the various FTAA working groups. The exception is the issue of safeguards which has not yet been considered in the FTAA process, but is likely to be a part of the negotiations, as it is difficult to envisage a trade agreement without safeguard clauses. This paper added a section on dispute settlement, which is the subject of a newly created working group.

1. Tariff Elimination

A main purpose of the FTAA is the progressive reduction and eventual elimination of tariffs and import duties to trade in goods among the members. To be consistent with the Uruguay Round Understanding on Article XXIV, a FTAA would have to provide for the elimination within ten years of "substantially all" duties on goods traded among its members. Should the members of such an agreement believe that "10 years would be insufficient they shall provide a full explanation to the Council for Trade in Goods of the need for a longer period.

While the approach to tariff elimination in the FTAA remains to be defined (i.e., formula or offer and request) certain instruments that could facilitate the participation of the smaller economies might be considered, i.e. longer timeframes for phasing out tariffs. A case for smaller economies to eliminate "substantially all" tariffs over a period in excess of 10 years could be made on the basis of, at least, two factors: the need for additional time to adjust their economies to greater competition within the FTAA, and the reduction in government revenue resulting from lowering border taxes which may require fiscal restructuring.

Regarding the time allowed for tariff elimination, smaller economies might negotiate non-linear schedules. Different formulas might be applied to whatever time period is agreed so that the majority of tariff cuts are "back-end loaded". As an example, tariff cuts on a particular product or products not take effect in each of the first six years and be reduced by 33% in each of the seventh, eighth and ninth years. Alternatively, the reduction of tariffs by smaller economies may be phased in over a period of time which is longer than the 10-year period prescribed by the WTO.

Finally, as FTAA participants have accepted the commitment to show "concrete progress by the end of the century" and are also heavily engaged in defining measures that might be considered an "early harvest", they might consider implementing unilateral tariff reduction and/or elimination measures favouring the smaller economies that could take place at the start of the negotiations. FTAA participants could, for example, notify such measures to the WTO as an "interim" agreement wherein the Article XXIV "rights" of other WTO members (i.e., non FTAA participants) would be fully reserved.

2. Non-Tariff Barriers

This is an area in which the FTAA could benefit from agreements already reached at the multilateral level. The Uruguay Round has succeeded in eliminating, or scheduling the reduction and elimination of, many traditional non-tariff barriers. Such barriers normally take the form of quotas or import licenses. To the degree that such measures continue to impede the exports of smaller economies, special attention might be given to at least two areas in particular: textiles and agriculture.

The WTO Agreement on Textiles and Clothing provided "quota issuing" countries with flexibility in reduction and eventual elimination of restrictive measures (i.e., "back-end loading"). In the FTAA, the smaller economies might negotiate, and importing countries should be prepared to accept, a "front-end loading" of such measures. In this sector, negotiations should also ensure that conservative rules of origin and marking requirements do not have the effect of nullifying other market access opening measures.

The WTO Agreement on Agriculture also poses a number of obstacles for the smaller economies. While many non-tariff barriers were subject to tariffication, the result often did little to enhance the ability of smaller economies to access larger markets. Tariffs on products of particular importance to the smaller economies (i.e., sugar, dairy, poultry, beans and some tree fruits) could be dealt with early in the negotiations by the larger economies and could be included in the "interim" agreement referred to above.

3. Rules of Origin

Rules of origin are an essential part of any free trade agreement, and the FTAA would be no exception. To the extent that the FTAA would confer a tariff preference only to the products of its members, rules would be required to determine what products are entitled to this preferential treatment. When goods are produced entirely within the territory of a member of the free trade area, the determination of origin is clear and relatively straightforward. But when materials imported from various countries outside the free trade area are incorporated in an article produced within the area, difficult questions can and do arise. These questions have become increasingly complex in the wake of the desegregation of production among many countries brought about by globalization, as well as the worldwide proliferation of free trade agreements with varying rules of origin.

FTAA negotiations on rules of origin should lead to an efficient and transparent system. The negotiations will also have to address nomenclature and certificates of origin issues. The rules should provide for: (a) the common interpretation of the rules; (b) the wide dissemination of such rules so as to make them available to users, and (c) the optimal use of administrative resources aimed at facilitating their use by external operators while stimulating trade within the Hemisphere itself.

In this context, FTAA negotiations should keep open the possibility to allow several producers from smaller economies to cumulate their processing activities for purposes of determining origin. In addition, consideration could be given to including de minimis provisions (i.e., if the value of non-originating materials is less than a certain percentage the good will nonetheless be considered as originating) in favor of smaller economies.

4. Safeguards

While safeguards are not yet a topic of discussion in the FTAA process, they will undoubtedly be an element in the FTAA Agreement. The FTAA approach to safeguards may be designed on the basis of the Uruguay Round Agreement on Safeguards, which contains detailed rules to ensure that WTO members make proper use of Article XIX safeguard actions.

The FTAA agreement on safeguards could set out criteria to be met in the case of bilateral emergency actions (i.e., within the FTAA) applied to goods originating from smaller economies. The agreement could also specify the conditions under which imports from the smaller economies would be excluded from safeguard actions pursued by FTAA members under WTO rules. FTAA provisions on safeguards could accommodate the interests of smaller economies through various types of measures:

- a)** enabling smaller economies to extend the application of a safeguard measure for a particular length of time beyond the maximum period allowed to other FTAA members;
- b)** prohibiting the application of safeguard measures against products from smaller economies whose share of imports of the product concerned does not exceed a certain percentage;
- c)** allowing smaller economies to apply, according to specific criteria, a safeguard measure against an imported product previously subject to such a measure;
- d)** allowing smaller economies to apply a MFN bound rate, as opposed to a previously applied MFN applied rate.

5. Subsidies, antidumping and countervailing measures

The use of antidumping (AD) and countervailing duties (CVDs) to prevent or remedy unfair trade practices has accelerated during the past years. In the Western Hemisphere unfair trade legislation is in force in approximately 19 countries. The smaller economies of the region have not traditionally been the target of AD/CVD actions. Nevertheless, the FTAA might "lock in" the current situation vis-à-vis the smaller economies by the negotiation of a broad based "exemption".

On the antidumping side, market penetration by the smaller economies is unlikely to reach such a scale that their exports (even if "dumped") would be on an order to "threaten" or cause "serious injury" to producers in the larger economies. On the subsidy/countervail side, an analysis of WTO subsidy notifications shows that there are few subsidy practices in the smaller economies that would be of serious concern to the larger economies. Thus, a possible approach in this area could be worked out by incorporating de minimis provisions in the future Agreement.

6. Investment

One of the main objectives of the FTAA is the progressive elimination of barriers to investment in the region. Provisions of the FTAA in this area will have to be built upon the investment framework put in place in the Hemisphere during the last few years. Since the beginning of the 1990s, new laws have been enacted in most countries, bilateral treaties have been signed and subregional instruments have been negotiated. These instruments promote investment liberalization and embody high standards of protection of foreign investment. They also share important commonalities, albeit different approaches are used with regard to some issues -such as admission of investments (i.e. the entry of investments of investors of one country into the territory of the other country).

The interests of the smaller economies would be well advanced if their abilities to attract foreign investment were strengthened. Such an end would be achieved by the regionalization in a FTAA agreement of the commitments that most countries -including smaller economies- have entered into at the national, bilateral, and subregional levels. Countries generally acknowledge the positive impact that foreign investment has on economic growth, productivity and the promotion of exports through intra firm trade. The smaller economies would not wish to risk their capacity to compete for those resources by seeking a lower level of commitment in this area. The smaller economies might even consider implementing such measures on either a unilateral or "interim" basis early in the negotiations, or as a demonstration of "concrete progress by the end of the century".

7. Services

In many countries, both developed and developing, services now account for the largest share of employment and gross domestic product. Technological and managerial innovations have also created and increased both the demand for and the supply of new services, while many types of services are becoming tradable internationally. In addition, the availability of efficient producer (e.g. professional), distributive (e.g. transport and telecommunications) and financial (e.g. banking and insurance) services has become an important pre-condition for an outward-oriented economy, be it based on manufacturing, primary production or services.

In order to be compatible with Article V of GATS (Economic Integration), the FTAA would have to provide for "substantial sectoral coverage" and for the "absence or elimination of substantially all discrimination among members". Paragraph 3 of this Article provides for developing countries to have flexibility with respect to the conditions to be fulfilled for such agreements to be acceptable under the provisions of GATS.

Given the competitive advantage many of the smaller economies have developed or are developing in this sector, the smaller economies would be well-served if the FTAA contains a

strong legal framework for the liberalization of trade in services which provide for the broad elimination of restrictions and for meaningful negotiations on a sector-by-sector basis. This would advance the modernization of policies and regulations in this area of particular interest to the smaller economies.

8. Intellectual Property Rights

In the Uruguay Round, participants sought to consolidate most of the provisions of existing international agreements into a single instrument. Implementation of intellectual property provisions will entail the adoption of new or adaptation of existing legislative instruments and, more important, the development of an effective infrastructure. In this context, countries will need to incorporate the relevant provisions of the WTO Agreement in their laws and regulations, substantially improve and enlarge the judicial, administrative and enforcement framework, including the setting up of the necessary customs and border control machinery, and mobilize and develop the requisite human resources.

The TRIPS Agreement contains transition provisions which enable developing countries to bring their intellectual property regimes into conformity with the new standards as late as January 1, 2000, with further delays allowed under defined circumstances as in the case of extension of protection for chemicals and pharmaceutical products. At minimum, virtually all countries in the Hemisphere will have to comply with the TRIPS Agreement within, roughly, a year and a half of the Santiago Summit launch of the FTAA negotiations.

Given the complexity of this issue and the resources which will be necessary to develop adequate infrastructure and effective enforcement mechanisms, smaller economies should consider pooling their scarce resources at the subregional level. Larger economies, in turn, should be prepared to assist the smaller economies in this endeavour, for example by providing technical assistance and expertise to enable these countries to apply their WTO commitments as well as any agreements which may be reached in the FTAA negotiations.

9. Competition Policy

In spite of the far reaching trade reforms undertaken by Latin American and Caribbean countries in the 1980s and 1990s, reforms in competition policy legislation are yet to be fully addressed. Unlike the trade area, there are few international agreements on competition policy. With the exception of the competition rules of the European Union, there are no international competition rules and no agreed international procedures for resolving international disputes over national anti-trust actions that have international ramifications. Although some limited provisions regarding competition issues have been incorporated in some of the agreements that emanated from the Uruguay Round, such as in the case of safeguards and services, the WTO itself has only recently established a Working Group on this issue.

Given the incipient nature of competition policy in most countries of the Western Hemisphere, a crucial issue with regard to the facilitation of small economy participation in the FTAA in this field would be the implementation of technical assistance and cooperation programs. These could be designed to support national efforts in the sphere of competition policy, including the design of national legislation and the establishment of adequate enforcement agencies.

10. Government Procurement

Government procurement involves the purchase of goods and services by federal, provincial and local governments for their own use. To the extent that governments are significant consumers of these goods and services, discriminatory government practices can be an effective barrier to trade. The aim of the FTAA negotiations in this area will likely be the significant reduction and eventual elimination of barriers in this area.

Government Procurement is not currently covered by WTO rules, but is a plurilateral agreement to which, of the countries of the Western Hemisphere, only Canada and the United States are signatories. FTAA negotiations on government procurement would, in principle, involve the granting of most favored nation and national treatment to trading partners regarding the purchase of goods and services by governments and government controlled entities. The negotiations would cover issues such as public notification of public tenders, transparency in the bidding and selection process and specialized dispute settlement procedures, and would center on the determination of the list of government entities, the portion of government procurement activities, and the threshold value of procurement of products or services to be covered.

Among the measures which could be adopted in the field of government procurement in order to facilitate the participation of smaller economies are the following:

- a)** negotiate mutually acceptable exclusions from the rules on national treatment with respect to certain entities, products or services, or specified percentages of the total value of procurement contracts of goods and services procured by government entities. In addition, allow smaller economies, after the entry into force of FTAA commitments in this field, to modify their coverage lists of entities, products or services subject to FTAA government procurement commitments;
- b)** exclude from FTAA government procurement commitments smaller economy procurement contracts financed by loans from regional and multilateral financial institutions;
- c)** provide technical assistance and cooperation to enable enterprises from smaller economies to participate in tendering procedures; and
- d)** larger countries that are subject to government procurement obligations in sub-regional agreements could "regionalize" in the FTAA the access on a non-reciprocal basis at the outset of the FTAA negotiations in favour of the smaller economies.

11. Standards and technical barriers to trade

Discussions, so far, in the FTAA Working Group on Standards and Technical Barriers to Trade have centered on the need to ensure that the development of standards, technical regulations and conformity assessment procedures is done in a transparent and non-discriminatory manner. FTAA participants will have the option of going beyond the WTO agreement in some areas, particularly with regard to the promotion of compatibility, equivalence and mutual recognition. Progress might also be achieved in the establishment of more detailed hemispheric procedures on accreditation, mutual acceptance of test data and certification procedures, information exchanges and notification.

The problems faced by the smaller economies, are mainly institutional and infrastructural. Given their physical and resource limitations, smaller countries may have difficulties with the preparation and application of technical regulations, standards and conformity assessment procedures. Given the diversity in levels of economic development, participation in Mutual Recognition Agreements at the subregional and regional level could be voluntary and could expand along with the development of infrastructure and human resource development on the part of member states.

Direct technical assistance for the smaller economies could focus on:

- (a)** the preparation of technical regulations;

(b) the establishment of national standardizing bodies and participation in international standardizing bodies;

(c) the establishment of regulatory bodies or bodies for the assessment of conformity with technical regulations;

(d) steps to be taken by Small Economy producers in order to have access to systems for conformity assessment operated by governmental or non-governmental bodies within other FTAA participants;

(e) the training of personnel; and

(f) the steps to enable the relevant bodies within the smaller economies to fulfill the obligations of membership or participation in international bodies.

12. Sanitary and Phytosanitary Measures

The modalities to facilitate the participation of smaller economies in the FTAA that could be adopted with respect to this issue could be similar to the ones contemplated in the Uruguay Round SPM Agreement itself. These modalities include, among others, the following:

a) allowing longer time-frames for compliance of provisions regarding the introduction of new SPMs on products of interest to smaller economies;

b) granting smaller economies, upon request, specified, time-limited exceptions in whole or in part from obligations;

c) facilitating the provision of technical assistance to smaller economies with a view to allowing such countries to adjust to, and comply with, FTAA/WTO sanitary and phytosanitary provisions;

d) facilitating a sub-regional (i.e., collective) approach to the fulfillment of obligations and disciplines.

13. Customs Procedures

Customs administration and procedures are indispensable for interpreting, administering and enforcing rules of origin and dealing with other important aspects of trade. In addition, the development of efficient customs procedures and institutions has become a key element in an era of open trade policies and advances in transport and communications. Problems of inefficiency in customs services was not such an important issue when trade was already restricted by tariffs, quotas and high taxes. But now that trade policy has become a more central element to countries development strategies, governments are increasingly more concerned about the effects which cumbersome and corrupt customs procedures can have on the conditions of access to their markets and, indirectly, on the flows of foreign direct investment.

The FTAA negotiations would probably cover issues such as certification of origin, administration and enforcement; advance rulings, review and appeal, physical inspection mechanisms, etc., with a view to simplifying, harmonizing and modernizing customs procedures, eliminating arbitrariness, increasing customs effectiveness, and reducing the possibilities for fraud, corruption, and tax evasion.

There are few national customs services in the Western Hemisphere that have fully automated

customs clearance procedures. Many services do not have the resources necessary to generate reliable and timely data. Thus, in this area, the challenge is less one of trade policy, and more one of identifying human and financial resources that would allow the smaller economies to effectively implement the Agreement, including those elements needed to determine whether goods qualify for preferential or non-preferential treatment.

14. Dispute Settlement

A predictable, transparent, non-discretionary, and timely dispute settlement mechanism is essential to the stability and success of an FTAA. It is in the interest of all the participating countries – especially the smaller economies – that an effective dispute settlement mechanism be created within the FTAA.

The shortcomings of GATT47, led to the reform of dispute settlement procedures at the multilateral level in the form of the Dispute Settlement Understanding (DSU). It is reasonable to conclude that a dispute settlement mechanism in the FTAA will incorporate many, if not all, elements of the DSU. The DSU itself is slated for review within the context of the WTO after three years of operation. Given the interlocking timelines of the FTAA and the WTO Review, it seems sensible that any further modifications and/or improvements that result from this Review could be incorporated into the FTAA. Already under the WTO, small and developing countries have become much more active participants than was the case under the GATT. As such cases show, a country's ability to protect its interests is more dependent upon legal and argumentation skills than on financial resources.

Smaller Economies will benefit most from a dispute settlement process that contains a well developed supporting structure. This might include:

- (a)** a well funded and staffed legal division in the eventual secretariat, capable of providing impartial advice and information purely in the character of legal research;
- (b)** access to accurate and timely information concerning the evolving trade policies of one's FTAA partners, thus providing the basis for Smaller Economies to determine whether policies and practices are undermining their negotiated benefits; and,
- (c)** some measure of enhanced legal, or other related, training for government officials from the Smaller Economies who are charged with the role of defending their country's interests in the dispute settlement procedures themselves.