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David M. Gilmore

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DAVID M. GILMORE*

* David M. Gilmore is currently an attorney with Preston Gate Ellis & Rouvelas Meeds LLP, the Washington, D.C. office of Preston Gates & Ellis LLP. The author gratefully acknowledges assistance from Mr. James R. Holbien, former U.S. Secretary of the North American Free Trade Agreement Secretariat, Ms. Karen O. Robinson and Ms. Taunya L. McLarty.

I. INTRODUCTION

The issue of the creation of a free trade area that will encompass the entire hemisphere stretching from the northernmost point in Canada to Tierra del Fuego has long been discussed in the United States and Latin America with little result. However, with the start of negotiations last month to create a Free Trade Area of the Americas (FTAA) there is hope that the vision will become a reality. Despite this optimism there are many obstacles that must be overcome before this goal will become a reality.

In December 1994, at the Summit of the Americas, President Clinton signed a declaration with thirty-three other leaders from the hemisphere which established the parameters and objectives of the negotiations for an ambitious project that not only includes the FTAA initiative, but also negotiations addressing the preservation of democracy in the hemisphere, the eradication poverty and discrimination throughout the region, and the promotion and improvement of education in the Americas.[1] The hope is that through these four 'pillars' Latin America and the Caribbean can break out of their long history of slow economic growth and guarantee the necessary level of sustainable development that will change the face of the region in the next century.

With the creation of the North American Free Trade Agreement (NAFTA)[2] in 1994 many saw a renewed opportunity

1. Summit of the Americas: Declaration of Principles and Plan of Action, Dec. 11, 1994, 34 I.L.M. 808, 810-815 (1995).

2. North American Free Trade Agreement, Dec. 17,1992, U.S.-Can.-Mex., 32 I.L.M. 289 (1993)[hereinafter NAFTA].

for the long promised hemispheric free trade area based on that agreement.[3] The advocates of this 'hub and spoke' approach saw Mexico as simply the first Latin American country to join the agreement with other hemispheric states individually negotiating to join NAFTA as they were determined to be able to integrate themselves into the agreement economically.[4] In fact, when Chile began negotiations with the NAFTA partners in 1994 it was believed that it would be the first of many 'spokes' to be attached to the NAFTA hub.[5] However, this approach did not survive long as Chile suspended its negotiations in 1995 pending approval of 'fast track' negotiating authority in the United States.[6] The eventual result of United States inaction was the signing of bilateral free trade agreements between Canada and Chile, Mexico and Chile, and MERCOSUR[7] and Chile.

Today, there is little doubt that all hope in achieving a hemispheric free trade area rests not with countries joining NAFTA, but with the FTAA negotiations which encompass all the countries in the hemisphere, save Cuba, negotiating together for the creation of a comprehensive agreement that overlays all of the existing regional and subregional agreements. While this is not to say that many of the provisions found in NAFTA will not be included in the FTAA, it is almost a certainty that the United States position is considerably weaker in this format than under the 'hub and spoke' approach as it will face the growing economic power of Brazil and MERCOSUR in achieving many of its trade

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3. *See* David Gilmore, Note, *Expanding NAFTA to Include all of the Western Hemisphere: Making Chile the Next Member,* 3 J. INT'L L. & PRAC. 413(1994)(For further discussion on Chilean ascension to NAFTA). *See also* Raymond J. Ahearn, *supra* note 11, Congressional Research Service, Issue Brief, *Trade in the Americas, supra* note 43 at 2. *See also* Mark, B. Baker, *Integration of the Americas: A Latin Renaissance or a Prescription for Disaster?* 11 TEMP. INT'L & COMP. L.J. 309, 324, n.142 (1997) and Dr. Richard L. Bernal, *Regional Trade Arrangements and the Establishment of a Free Trade Area of the Americas,* 27 LAW & POL'Y INT'L BUS. 945, 950, n.45 (1996)(Even before President Bush proposed a hemispheric free trade agreement in his 1990 Enterprise for the Americas, President Johnson forwarded a similar agreement at a 1967 conference of regional leaders.)

4. *See* Thomas Andrew O'Keefe, *Potential Conflict Areas in any Future Negotiations Between MERCOSUR and the NAFTA to Create a Free Trade Area of the Americas,* 14 ARIZ. J. INT'L & COMP L. 305 (1997).

5. *See id.*

6. *See id.* (The most recent legislation allowing for "fast track" approval of trade legislation expired in 1994 and attempts to revive it have failed as of this writing.)

7. Treaty of Asuncion, March 26, 1991, Arg. Rep.- Fed. Rep. of Brazil- Rep. of Para.- Eastern Rep. of Uru., 30 I.L.M. 1041 (1991), Establishing a Southern Common Market – Mercado Comun del Sur [hereinafter MERCOSUR].

objectives. This is especially true since United States negotiators are currently without the added negotiating power that comes with fast track authority.[8]

Since the creation of MERCOSUR and NAFTA there has been much debate on both sides of the free trade issue as to whether the removal of trade barriers is achieving increased trade and development or whether it is simply diverting trade and resources from one source to another. The recent opening of formal negotiations on the FTAA has done little to cool that debate, especially in the United States. It is within this context that this paper will attempt to address whether the FTAA is advisable and whether there is reason to hope that there will be the type of changes that many in the United States and Latin America hope will come about as a result of it by focusing on the following issues: 1) the current structure of NAFTA and its impact on trade between its partners; 2) the current structure of MERCOSUR and the affect it has had on intramember trade; and 3) the format of the FTAA negotiations, its goals, and the projected impact that it will have on the hemisphere based on hemispheric trade by NAFTA and MERCOSUR.

II. NAFTA

A. *Overview*

The North American Free Trade Agreement was signed by the presidents of the United States, Mexico, and Canada on December 17, 1992, and entered into force on January 1, 1994.[9] These three founding members are still the only participants in the agreement to date.[10] Chile was invited to enter into negotiations with the parties in 1994, but there has been no progress in the negotiations.[11] It is the only country that has opened discussions as of this writing.[12]

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8. *See* David A. Gantz, *The United States and the Expansion of Western Hemisphere Free Trade: Participant or Observer?*, 14 ARIZ. J. INT'L & COMP. L. 381, 382 (1997).

9. North American Free Trade Agreement, *supra* note 2.

10. *Id.*

11. *See* Raymond J. Ahearn, Congressional Research Service, Issue Brief, *Trade in the Americas*, February 27, 1998, at 5-6.

12. *See id.*

Unlike the MERCOSUR structure discussed below, NAFTA is governed by a single comprehensive agreement with implementation legislation.[13] This document, with its 22 chapters and ten annexes, incorporates all the dispute settlement procedures, institutional structures, objectives and comprehensive rules that govern trade between all three partners.[14] It is very broad in its scope that provides for the removal of most intra-regional tariffs and nontariff barriers within fifteen years.[15]

B. Selected Governing Clauses[16]

The stated objectives of the NAFTA are found in Article 102 and include the following: 1) elimination of both tariff and non-tariff barriers between the parties; 2) simplification of the cross-border movement of goods and services between the parties; 3) promotion of fair competition; 4) increased investment opportunities; and 5) provide adequate and effective protection and enforcement of intellectual property rights.[17]

Chapter 4 of NAFTA governs the rules of origin requirements for duty free treatment. Article 401 requires that to qualify for a zero tariff rate you must establish that the good is one of the following: 1) a product which is wholly obtained or a good which is produced with materials exclusively from within the territories of the parties; 2) non-originating material which as the result of production undergoes a tariff reclassification; or 3) a product which is produced from one or more non-originating materials and does not undergo a tariff reclassification, but contains sufficient minimum regional content, based on either the transaction value method of calculation or the net cost

13. *See* Gantz, *supra* note 8, at 382 (Some provisions vary as to the treatment of the parties because of the incorporation of the U.S.-Canada Free Trade Agreement into NAFTA, however, except where it is otherwise noted in NAFTA, this is limited to the tariff elimination schedule which reduced tariffs between the U.S. and Canada to zero on January 1, 1998.)

14. *See id.*

15. *See id.*

16. This section is merely an overview of some of the sections that this author believes to be important to the discussion of this paper. For a more detailed discussion of the NAFTA *see* O'Keefe, *supra* note 4, and JAMES R. HOLBEIN and DONALD J. MUSCH eds., NAFTA, The Practitioner's Deskbook Series, 1994.

17. JAMES R. HOLBEIN and DONALD J. MUSCH eds., NAFTA, The Practitioner's Deskbook Series, 1994.

method of calculation.[18] The exceptions to these rules are very limited and only apply to goods related to a product which has been deemed to be an originating good.[19] Exceptions to the requirements would include things such as diagnostic equipment, spare parts or tools customarily included with the good, and retail packaging.[20]

Safeguard measures are controlled by Chapter 8. Under Article 801, a member state may suspend a NAFTA tariff preference or increase the tariff to the MFN rate, after serving written notice to the state, if imports of the product "constitute a substantial cause of serious injury, or threat thereof, to a domestic industry producing a like or directly competitive good."[21] The action must be taken within one year of the increase in quantity of the imported product and cannot exceed three years except in exceptional circumstances.[22] Finally, after the ten year transitional period such an action may only be taken with the consent of the member exporting the good.[23]

Foreign investment from another member of NAFTA is governed by Chapter 11(A). Article 1102 provides that each member shall afford investors from another member state national treatment. Furthermore, a member may not require a minimum level of equity to invest or that an investment must be liquidated based on nationality of the investor. Under Article 1109, an investor may not be prevented from repatriating capital from an investment by a member state. An investor is also protected from discriminatory expropriations and entitled to fair market value of the investment if there is any type of governmental taking under Article 1110.

Under Chapter 11(B) an individual investor may submit a claim for arbitration against a state if it is within three years of the date of the loss. If there already has been an attempt to resolve the dispute through consultation or negotiation, whether

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18. North American Free Trade Agreement, *supra* note 2, art. 401(a)(b)(c)(d)(Under Article 401(d), a product is required to have at least 60 percent region content under the transactional value method requirement or at least 50 percent regional content if the net cost method requirement is used. Article 402 establishes the formulae for the determining regional content for both methods.)

19. *Id.* at art. 401(d).

20. *Id.* at art. 407, 408, & 409.

21. North American Free Trade Agreement, *supra* note 2, art. 801(1)-(2).

22. *Id.* at art. 801(2)(b)-(c)(i).

23. *Id.* at art. 801(2)(c)(ii) and art. 805.

a claim is submitted to arbitration is entirely at the discretion of the investor under Article 1121, as each member consents to arbitration under Article 1122(1). For any arbitral proceedings Article 1120 provides the investor with a choice of three different sets of governing procedures. Finally, any award is binding upon the parties under Article 1136(2) and if a member state should fail to abide by award, action may be taken against it by the member state of the investor under Article 1136(5).

Chapter 12 addresses trade in services. Article 1201 includes within its scope, all measures relating to cross-border services from one member country to another except measures relating to financial services, air transport, and government procurement.[24] Article 1202 requires that any service measures afford national treatment to any service providers from another member of NAFTA. Under Article 1210 all members were required to eliminate all residency or citizenship requirements for the licensing of professional services by January 1, 1996, and any additional requirements for certification or licensing must be transparent, as least burdensome as possible, and not a disguised barrier to service.

The rules governing competition are located in Chapter 15. Under Article 1501 each member state is obligated to adopt and maintain measures which promote a competitive environment for business. Articles 1502 and 1503 allow for the creation of monopolies and state enterprises so long as they act in accordance with the requirements of Chapter 15 and do not engage in any discriminatory or anticompetitive behavior.

Chapter 17 controls the rules for all forms of intellectual property protection. The protections provided by this chapter are very comprehensive, ranging from traditional areas of protection such as copyright,[25] patent,[26] and trademark,[27] to modern technologies such as protection of encrypted satellite signals[28] and semiconductor circuit designs.[29] Article 1701(1) requires that each member country afford nationals of another party "adequate

24. Financial services and government procurement are governed by Chapters 14 and 10, respectively.

25. North American Free Trade Agreement, *Supra* note 2, at art. 1705.

26. *Id.* at art. 1709.

27. *Id.* at art. 1708.

28. *Id.* at art. 1707.

29. *Id.* at art. 1710.

and effective protection and enforcement of intellectual property rights, while ensuring that measures to enforce intellectual property rights do not themselves become barriers to legitimate trade." In addition to the requirements of Article 1701(1), Article 1701(2) states the members should accede to and establish as the minimum protections, with the requirements of Chapter 17, the following treaties:

1) 1971 *Geneva Convention for the Protection of Producers of Phonograms Against Unauthorized Duplication of their Phonograms*;

2) 1971 *Berne Convention for the Protection of Literary and Artistic Works*;

3) 1967 *Paris Convention for the Protection of Industrial Property*; and

4) 1978 *International Convention for the Protection of New Varieties of Plants* or the 1991 *International Convention for the Protection of New Varieties of Plants*.[30]

Chapter 19 governs the review and dispute settlement in anti-dumping and countervailing duty matters. Under Article 1902 each member is allowed to apply its own national laws for assessing anti-dumping and countervailing duties against the imports of another member country. Interestingly, despite preserving this authority for member states, Article 1904 replaces judicial review of anti-dumping and countervailing duty determination with a binational panel whose decisions cannot be reviewed by a court of the importing party. Said panel must be requested by a member and the member is obligated to make such a request at the behest of a person who would otherwise be able to challenge the duty through a court action.[31] Although states may apply their own national laws, if they intend to amend their legislation they must notify other affected members in writing under Article 1903. Furthermore, under that same provision a state may request that such amendment be reviewed by a binational panel to ensure that it is in conformance with Article 1902(2)(d)(i) or (ii).

Chapter 20(A) controls the institutional framework and establishes two organs as the heart of the structure for NAFTA.

30. North American Free Trade Agreement, *supra* note 2, at art. 1701(2).
31. *Id.* at art. 1904.

Article 2001 creates the Free Trade Commission (FTC) and Article 2002 addresses the Secretariat. The FTC is responsible for supervising the implementation[32] and further development of the agreement.[33] It is also tasked to resolve any interpretive disputes regarding interpretation or application of the agreement[34] and consider any matter affecting the operation of the agreement.[35] If it is unable to resolve any matter affecting the agreement to the satisfaction of a member it may establish an arbitral panel to decide the matter under Article 2008. The Secretariat is subservient to the FTC and is actually three different offices, one created by each member state.[36] The function of the Secretariat is to assist the FTC, support the work of any committees created by the NAFTA, and assist any panels created for review of anti-dumping and countervailing duty matters.[37]

Chapter 20(B) establishes the institutional dispute settlement mechanism for NAFTA. Pursuant to Article 2004 these rules are applied to any request for arbitration relating to a NAFTA dispute unless the area of dispute has its own special provisions.[38] Article 2005 gives a member the option using the WTO or the NAFTA dispute settlement procedures. Articles 2006 and 2007 require that the members engage in consultation and ask the FTC for assistance in resolving a dispute before an arbitral panel can be convened under Article 2008. Under Article 2018(1), the member states must agree on a final resolution of the dispute after receiving the panel's final report. Article 2018(2) requires that wherever possible the dispute resolution should involve removal of the offending measure and only if that is not possible is compensation acceptable. If the members are unable to come to an agreement for resolution of the dispute, Article 2019 allows the aggrieved member to suspend benefits of equivalent effect to the member complained against.

While this section of the comment is only a limited discussion of the whole North American Free Trade Agreement,

32. *Id.* at art. 2001(2)(a).

33. *Id.* at art. 2001(2)(b).

34. *Id.* at art. 2001(2)(c).

35. *Id.* at art. 2001(2)(e).

36. North American Free Trade Agreement, *supra* note 2, at art. 2002(1)-(2).

37. *Id.* at art. 2002(3).

38. *E.g.*., both anti-dumping/countervailing duty and foreign investment dispute matters have their own procedures so they are specifically excluded.

it is illustrative of the very detailed and comprehensive approach that negotiations took in an effort to ensure protection of the parties through a single agreement, covering a broad range of areas beyond tariff elimination, including: nontariff barriers, security commitments, and investment liberalization.[39] This theme is also illustrated by the authority of the FTC and inclusion of non-binding arbitration as a dispute resolution mechanism.[40] As an example, while NAFTA is a fully integrated treaty, which contains its governing structure in Part Seven of the Treaty, the institutional structure of MERCOSUR is found in the Protocol of Ouro Preto (an agreement adopted by MERCOSUR countries three years after the Treaty of Asuncion which establishes the framework of MERCOSUR.)[41] However, despite being so comprehensive in most areas, NAFTA does not attempt to encompass some of the goals set by MERCOSUR, such as coordination of economic and monetary policies, establishment of a common external tariff, or address free intra-NAFTA movement of labor.[42]

C. Impact of the Agreement on Member Trade

The creation of NAFTA established North America as the world's largest free trade bloc, for a brief period of time, until the most recent expansion of the European Union. In 1997, it had more than 395 million people and a gross domestic product of $7.5 trillion.[43] In 1997, intra-NAFTA trade accounted for 49 percent of all trade by its members,[44] an increase of almost 11 percent a year on average since 1990.[45] At the same time, NAFTA trade to third countries was only growing at 7 percent.[46]

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39. *E.g.*, Not included in the discussion were the chapters governing government procurement, telecommunications, standards related measures, and agricultural measures to name but a few.

40. North American Free Trade Agreement, *supra* note 2, at art. 2006 & 2007.

41. Protocol of Ouro Preto, December 17, 1994, 34 I.L.M. 1244. (Additional Protocol to the Treaty of Asuncion on the Institutional Structure of MERCOSUR.) *See also,* Gantz, *supra* note 8, at 403.

42. *E.g.*, Compare goals of Article I of Treaty of Asuncion and goals of Article 102 of NAFTA. *See also,* Gantz, *supra* note 8, at 402.

43. *See Integration and Trade in the Americas, A Preliminary Estimate of 1997 Trade*, Periodic Note, Int.-Am. Dev. Bank, Dec. 1997, at 2.

44. *See id.*

45. *See id.* at 11. (Extra-NAFTA trade has increased an average of only 7 percent a year during that period.) *Id.*

46. *See* Enrique V. Iglesias, *The New Face of Regional Integration in Latin America*

1. Economic Effects

By almost all accounts NAFTA has been a windfall for Mexico. Despite the serious economic downturn that it endured in late 1994 and early 1995 during the peso crisis, Mexico has seen substantial growth in its trade with its NAFTA partners and a blossoming of foreign direct investment.

From 1994 to 1996 Mexico received $25 billion of foreign direct investment in plants and equipment.[47] This was the second largest amount of direct investment of that type to a developing country ever recorded.[48] Seven billion dollars in investment was projected for 1997, increased from only $4.3 billion in 1993, before NAFTA.[49] As part of the impact from this influx of capital, Mexico saw the employment in the maquila industry increase by 20.3 percent in 1996 over the previous year.[50] The value added by parts and components from these plants increased 63 percent between 1995 and 1996.[51]

In 1996, Mexican imports from the United States grew by 24 percent, exceeding the pre-peso-crisis levels of 1994.[52] During that same year, United States suppliers accounted for 75.5 percent of all Mexican imports, up from 69.3 percent in 1993.[53] Between 1990 and 1996, Mexico increased its exports to the United States by 142 percent, climbing from $30.3 billion to $73 billion.[54] Between 1990 and 1996, Mexico's imports from the United States doubled from $28 billion to $57 billion.[55]

The effects of NAFTA trade on the United States has been

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and the Caribbean, Presentation at the annual World Bank Conference on Development in Latin America and the Caribbean, "Trade Towards Open Regionalism," Montevideo, Uruguay, (June 29, 1997).

47. *See* Luis Fernando de la Calle , *Mexico's View on the NAFTA,* 14 ARIZ. J. INT'L & COMP. L. 295, 296 (1997).

48. *See id.*

49. *See id.*

50. *See* Gantz, *supra* note 8, at 391. Mexico's maquiladora program was a duty drawback system that resulted in the establishment of over 2,000 factories, mainly along the U.S.-Mexico border. It was required to be eliminated by NAFTA. *Id.*

51. *See id.* at 392.

52. *See Integration and Trade in the Americas, supra* note 43, at 11.

53. *See* WILLIAM J. CLINTON, STUDY ON THE OPERATION AND EFFECTS OF THE NORTH AMERICAN FREE TRADE AGREEMENT, iv. (Exec. Off. of the Pres. of the U.S. 1997)[hereinafter President's Report].

54. *See* Ahearn, *supra* note 11, at 12.

55. *See id.*

decidedly more subdued, despite statistics showing that there has been a significant increase in U.S. trade with Mexico. In mid-1997, the United States International Trade Commission (USITC) released a report that concluded while trade between the United States and Mexico has increased significantly, there was little impact on trade with Canada.[56] It also found that it was unable to quantify a discernible effect by NAFTA on United States GDP or investment.[57] Despite the less than glowing report by USITC, it is notable that since January 1, 1994, United States total trade (imports and exports combined) with Canada and Mexico has increased from an annual average of $269 billion in 1991 to 1993 to an annual average of $384 billion in 1994 to 1996.[58] Bilateral trade between the U.S. and Mexico was $156 billion dollars in 1997, accounting for twenty percent of U.S. total trade, up from $81 billion in 1993.[59] Furthermore, while Canada has been the largest trade partner to the U.S. even before NAFTA, the agreement has increased trade with Mexico so substantially that it passed Japan to become the second largest export market for the United States in 1997.[60] United States exports to Mexico are increasing on average at 34 percent a year and increased five percent more than exports to the rest of the world in 1996.[61] That same year, Mexico's share of United States exports rose to 9.3 percent from 6.9 percent in 1993.[62] In 1997, the President's Study on the Operation and Effects of the NAFTA estimated that the United States had increased exports to Mexico by $12 billion, imports from Mexico by $5 billion.[63]

On the negative side, the United States total trade deficit with Canada and Mexico ballooned from $8.6 billion to $34

56. *See* JayEtta Z. Hecker, Associate Director, International Relations and Trade Issues, National Security and International Affairs Division, United States General Accounting Office; Testimony before the Subcommittee on Trade, Committee on Ways and Means, House of Representatives 6 (September 11, 1997) *in Impact Report, See infra* note 83.

57. *See id.* at 6.

58. *See id.* at 5.

59. *See* Congressional Research Service, *U.S.-Mex. and U.S.-Can. Trade Statistics*, Nov. 1997. (Data is based on compilation of U.S. Dept of Commerce Official Statistics. 1997 statistics are annualized from Jan-Aug 1997 statistics.)

60. *See* Fernando de la Calle, *supra* note 47, at 297; *See also* Congressional Research Service, *supra* note 59, compiled from official statistics of the U.S. Dept. of Commerce.

61. *See* Fernando de la Calle, *supra* note 47, at 297. U.S. exports to the world increased 31 percent while exports to Mexico alone increased by 36 percent. *Id.*

62. *See* President's Report, *supra* note 53.

63. *See id.* at iii.

billion.[64] Importantly, bilateral trade between the United States and Canada was over $208 billion in 1997, accounting for 41 percent of U.S. total trade, down slightly from just over $211 billion in 1993.[65]

It is obvious from the increases in Mexican trade they have received a substantial benefit from NAFTA, it is difficult to quantify what benefits NAFTA has bestowed on the United States based on the statistics. While it is true that exports to Mexico have increased substantially, since they are now the third largest trading partner of the United States, they only account for a small share of total U.S. exports.[66] This is especially the case when you consider the size of United States-Canada trade.[67] At the same time the amount of goods being imported has grown quite substantially.[68] While some of the figures may be distorted by the Mexican peso crisis, in the end analysis, any evaluation of the positive or negative impact of NAFTA on the United States at this time is difficult to ascertain without a long-term evaluation of the benefits of the agreement. This lack of available data is especially troubling considering the potential trade distorting effects of NAFTA discussed below and even broader impact that the FTAA could have on the United States.

2. Trade Distortion

Many argue that although there are benefits to regional trade arrangements, such as NAFTA, because they increase intra-regional trade, they also tend to discriminate against nonmembers potentially resulting in trade diversion.[69] While it is also generally held that this diversion is only present where there are high tariffs governing nonmember trade, there is evidence of diversion in the NAFTA context.[70] Most of the concern about diversion centers around Central America and the Caribbean because a significant portion of their trade is directed

64. *See* Hecker, *supra* note 56, at 5.

65. *See* Congressional Research Service, *supra* note 59.

66. *See* Ahearn, *supra* note 11, at 15.

67. *See id.* (In 1996, U.S. exports to Mexico accounted for only $57 billion, while exports to Canada were almost $133 billion.) *Id.*

68. *See id.* at 12, Table 1.

69. *See* Dr. Richard L. Bernal, *Regional Trade Arrangements and the Establishment of a Free Trade Area of the Americas*, 27 LAW & POL'Y INT'L BUS. 945, 949 (1996).

70. *See id.*

at the United States and analysis has shown that their economic growth has been negatively affected.[71] In fact, the World Bank has estimated that up to 36 percent of the Caribbean Basin Economic Recovery Act (CBERA) country exports to the United States could be displaced with countries such as St. Lucia facing displacement of 79 percent.[72] Most of these exports are being lost from these countries as a result of suppliers shifting production to Mexico because the requirements NAFTA rules of origin necessitate such action so that the suppliers may take advantage of the lower tariffs into the United States.[73]

As the United States is their most significant trading partner, many Central American and Caribbean nations have experienced significant economic downturns recently because of their inability to compete with Mexico.[74] The Caribbean Basin Economic Recovery Act (CBERA) that took effect on January 1, 1984, grants trade preferences to Central American and Caribbean nations to a limited number of exports considered vital to the region.[75] "NAFTA Parity" legislation that would grant Mexico-like trade treatment to CBERA nations has failed to pass in Congress twice.[76] An analysis that included 80 percent of the U.S. imports from the region showed that between 1993 and 1996 there was a shift in the products away from CBERA and toward Mexico.[77] Apparel is the fastest growing category of U.S. imports from CBERA countries. However, most products are ineligible for CBERA tariff preferences, and they may only get reduced tariffs if they are assembled with "fabric wholly formed and cut in the United States."[78] CBERA countries and Mexico are similarly priced in labor operations and both offer

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71. *See* Bernal, *supra* note 69.

72. *See id.* at 949-50.

73. *See* Gantz, *supra* note 8, at 392 n.5. *See also* Bernal, *supra* note 69, at 949 n.45.

74. *See* Gantz, *supra* note 8, at 409.

75. *See* Magda Kornis, *Is NAFTA Affecting U.S. Imports from the Caribbean Basin?*, INT'L ECON. REV., Sept./Oct. 1997, at 3, *available at*, ftp://ftp.usitc.gov/pub/reports/ier/PUB3065.PDF [hereinafter USITC report]. (The preferences do not cover items such as apparel and petroleum-related products which account for over half of U.S. imports from the region. Apparel alone was 40% of U.S. imports from the region in 1996.) *Id.*

76. *See id.* at 3-4.

77. *See id.* at 4-5. Between 1993 and 1996 the CBERA share of U.S. imports of 35 leading commodities shrank 2.55 percent while Mexico's share increased 5.5 percent. *Id.* at 5-6.

78. *See id. at* 7. From 1987 to 1996 apparel imports increased at 21 percent a year on average. *Id.*

lower transportation costs and close proximity to the U.S.[79] Despite this, CBERA countries have to compete with Mexico on unequal terms. This is because of the 16.7 percent tariff that is applied to the value added to the garments by assembling them in CBERA nations, while none is applied to Mexican garments and they enter duty free.[80] Since the implementation of NAFTA, CBERA countries share of the United States market has grown at a very slow rate, while Mexico's share has more than doubled.[81] While most of Mexico's market share increase has come at the expense of non-CBERA countries to this point, I find it notable that until the implementation of NAFTA, CBERA imports were increasing steadily and significantly. Now it appears that their growth is stagnating.

Production shifts because NAFTA rules of origin are not limited to CBERA countries. Some Asian suppliers also have been forced to shift their production to Mexico. The Korean television manufacturing industry has invested $500 million in Mexico since 1991, shifting picture tube manufacturing and television assembly jobs away from Asia because duty free status is only available if the picture tube is of North American origin.[82] While the investment in and of itself is not conclusive that there is distortion, this is an example of the possible trade distorting effects of NAFTA if it is shown that the televisions could be produced cheaper in Asia and but for the rules of origin would not be manufactured in Mexico.

Despite the focus above, the impact of NAFTA in trade distortion has not been limited to the United States. Because of the 1994-95 peso crisis, Mexico increased its MFN bound tariff on 502 consumer goods to 35 percent from the previous level of 20 percent.[83] As a result, U.S. goods meeting the rules of origin requirements, as well as Mexico's other FTA partners, are now

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79. *See* Kornis, *supra* note 75, at 7.

80. *See id.* (Mexican goods enter duty free if they are assembled using fabric wholly formed and cut in the U.S.) *Id.* at 7-8.

81. *See id.* at 8. (Most of Mexico's increased import share has come at the expense of non-CBERA countries which saw their share drop from 80.93% (1993) to 71.39% (1996).) *Id.*

82. *See* Gantz, *supra* note 8, at 392.

83. *See* Kyle Johnson et al., *Investigation No. 332-381: Impact of the North American Free Trade Agreement on the US Economy and Industries: A Three-Year Review*, Apr. 29, 1997, at 2-31, *available at*, http://www.usitc.gov/wais/reports/arc/w3045.htm. [hereinafter Impact Report] (U.S. exports on the goods affected amounted to $1.9 billion in 1996.) *Id.* at n.37.

enjoying a wider margin of preference over other foreign suppliers to the Mexican market.[84]

III. MERCOSUR[85]

A. Overview

The common market of the southern cone or MERCOSUR, the Spanish acronym it is more commonly known by, was created with the signing of the Treaty of Asuncion on March 26, 1991, by the presidents of Brazil, Argentina, Uruguay, and Paraguay.[86] The treaty entered into force in November 1991.[87] These four founding members are still the only full participants to date.[88] However, both Chile and Bolivia have signed agreements of association with MERCOSUR.[89]

The MERCOSUR structure is governed by three agreements: the Treaty of Asuncion,[90] the Protocol of Ouro Preto,[91] and the Protocol of Brasilia.[92] Although the Treaty of Asuncion is the founding document for the common market, it is a very simple document and stands apart from NAFTA because of its skeletal approach of mainly annunciating purposes, principles, and goals. With only 24 articles and 5 annexes, it was deliberately drafted to limit the amount of regulation that would take place during the "transition" period and allow for easy adaptation as circumstances presented themselves.[93]

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84. *See id.* at 2-31.

85. *See* MERCOSUR, *supra* note 7.

86. *See id.*

87. *See id.*

88. *See id.*

89. *See* Agreement of Economic Complementation between Chile and MERCOSUR, June 25, 1996, Article 2. (Chile agreed to establish a free trade area with MERCOSUR in June 1996. Under the agreement the tariffs on all goods, except for some sensitive goods which will have a longer phase in, will be reduced to zero by 2006. Bolivia signed a substantially similar agreement with MERCOSUR in December 1996.) *See also Integration and Trade in the Americas*, *supra* note 43, at 16 n.22 (With the addition of these two countries the free trade area of MERCOSUR includes half the population and 60 percent of the GDP of Latin America and the Caribbean.)

90. MERCOSUR, *supra* note 7.

91. Protocol of Ouro Preto, *supra* note 41.

92. Protocol of Brasilia, Dec. 17, 1991, 36 I.L.M. 691, *available at* http://www.brasilemb.org/economy/ProtBrasilia.htm.

93. *See* MARTIN AROCENA, COMMON MARKET OF THE SOUTHERN CONE: MERCOSUR, 10 (1995) (This transition period was marked from the signing of the treaty,

The Protocol of Ouro Preto, however, was negotiated to expand and formalize the process by creating an institutional structure to bind the parties.[94] The institutional structure, which is discussed below, was only one of the accomplishments of the protocol. In addition, it established MERCOSUR as a legal person in international law for the purpose of negotiating with third party countries, reaffirmed the principles and objectives of the Treaty of Asuncion, and confirmed the Decisions and Resolutions that the MERCOSUR institutions dictated during the transition period.[95] This was necessary because the organs created under the Treaty of Asuncion to administer and implement the agreement had no legal status and decisions between the four member countries were made by consensus.

The final major agreement, the Protocol of Brasilia, was created to govern dispute resolution and the interpretation of MERCOSUR's rules during the transition period. The Protocol of Ouro Preto preserves its validity and continues it under the current institutional structure.[96] Its role in MERCOSUR will be discussed in the next section.

B. *Selected Governing Clauses*[97]

Article 1 of the Treaty of Asuncion, the founding treaty for MERCOSUR, states that the objective of the agreement is to create a common market by December 31, 1994.[98] It calls for the free movement of goods, services, and factors of production through the elimination of customs duties and non-tariff restrictions on the movement of goods; the establishment of a common external tariff; maintenance of a common trade policy; the coordination of positions in international and economic forums; and the coordination of macroeconomic policies regarding

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March 1991, until the establishment of a common market by December 31, 1994).

94. *See* Dr. Paul Granillo Ocampo, *Policy Commentary: Lawyering in the Americas: Reflections on MERCOSUR and the Future of the Americas*, 3 SW. J. L. & TRADE AM. 373, 380 (1996).

95. *See* Ana Maria De Aguinis, *Can MERCOSUR Accede to NAFTA? A Legal Perspective*, 10 CONN. J. INT'L L. 597, 608 (1995).

96. Protocol of Ouro Preto, *supra* note 41, ch. VI.

97. This section is merely an overview of some of the sections that this author believes to be important to the discussion of this paper. For a more detailed discussion of the governing agreements of MERCOSUR, *See* Thomas Andrew O'Keefe, *supra* note 4, and the website of the Organization of American States at http://sice.oas.org.

98. MERCOSUR, *supra* note 7.

foreign trade, agriculture, industry, fiscal and monetary matters, foreign exchange, capital services, customs, transport, and communications matters.

Annex II governs the rules of origin requirements. These rules, which are much more limited and simplified than the NAFTA rules, are found in Article 1 of the Annex, as modified by Decisions 6/94 and 23/94,[99] and fall into four general categories: 1) products raised, extracted or harvested in the territory of one of the members of MERCOSUR such as mineral, plant, or animal products; 2) products that are manufactured exclusively using materials originating in territories of the members of MERCOSUR; 3) products in which the manufacturer does not use materials originating within MERCOSUR, but in which the process transforms the product in such a manner as to result in a tariff reclassification; or 4) the value of the MERCOSUR materials used in assembly is not less than 60 percent of the freight on board export value of the final product.[100] However, there are exceptions to these rules. If a good is unavailable within a reasonable time, is too expensive to obtain within the region, or a regional product does not meet the necessary technical specifications, a waiver may be obtained under Article 5 of the Annex.[101]

Annex IV governed the rules for safeguard measures, but it is no longer effective as Article 1 limited the application of such measures to the transitional period, up to December 31, 1994. It limited the quotas to no less than the average physical volume of the previous three years[102] and could only be applied for a one-year period with a renewal for an additional year.[103] Interestingly, Article 3 of the annex specifically excluded the use of technological advance or shift in consumer preference toward a similar competitive product as determining factors in evaluating the existence of or threat of serious damage to a product.

Intra-MERCOSUR foreign investment is governed by the Protocol of Colonia.[104] Articles 2 and 3 of the protocol provide

99. *See* THOMAS ANDREW O'KEEFE, LATIN AMERICAN TRADE AGREEMENTS, ch. 14-4, Transnational Publishers, Irvington, New York (1997).

100. MERCOSUR, *supra* note 7 at Annex II, art. 1.

101. *Id.* at art. 5.

102. *Id.* at art. 4.

103. *Id.* at art. 5.

104. Protocol of Colonia for the Promotion and Reciprocal Protection of Investments

with certain exceptions that national treatment will be provided for foreign investment from other MERCOSUR members. They also allow for the restriction or prohibition of investment in certain sectors.[105] Article 4 provides assurances against nationalization or expropriation. Article 5 guarantees the right to repatriate capital. Article 9 guarantees the investor a right to binding, international arbitration after six months of nonresolution of a dispute. The arbitration does not require the exhaustion of local remedies and is mandatory for the host country. Non-member country investment is controlled by the Protocol on Foreign Investment.[106] It operates in substantially the same manner as the Protocol of Colonia.

The organizational structure of the post-transitional period is governed by the Protocol of Ouro Preto.[107] As noted above, it established MERCOSUR as a legal entity under international law with six institutional organs at its core. Article 1 of the protocol calls for a Council of the Common Market (CCM), a Common Market Group (CMG), a MERCOSUR Trade Commission (MTC), a Joint Parliamentary Commission (JPC), a Economic-Social Consultative Forum (ESCF), and MERCOSUR Administrative Secretariat (MAS). Article 1 also allows for the creation of any auxiliary organs as may be necessary to assist in the integration process.

The CCM, originally created under the Treaty of Asuncion, is the highest organ in MERCOSUR.[108] It mainly functions to formulate policy and promote measures that assist in building the common market, but it is also responsible for negotiating agreements on behalf of MERCOSUR and ruling on proposals presented to it by the CMG.[109] The CMG, also established under the Treaty of Asuncion, mainly functions to submit draft Decisions to the CCM, to implement any measures necessary to

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Within MERCOSUR, January 17, 1994. [hereinafter Protocol of Colonia].

105. *See* O'Keefe, *supra* note 99, at ch. 14-9 (for example, under this provision Brazil, Uruguay, and Paraguay have reserved the right to limit foreign investment in their telecommunications sectors).

106. *See* Protocol on the Promotion and Protection of Investments Originated in Non-MERCOSUR Countries, August 5, 1994, [hereinafter Foreign Investment Protocol]. *See also* Horacio A. Grigera Naon, *Free Trade Areas: The Challenge and Promise of Fair vs. Free Trade; Panel V: Regionalism and the Transfer of Sovereignty; Sovereignty and Regionalism*, 27 LAW & POL'Y INT'L BUS. 1073, 1104 (1996).

107. Protocol of Ouro Preto, *supra* note 41.

108. MERCOSUR, *supra* note 7.

109. Protocol of Ouro Preto, *supra* note 41, at art. 8.

enforce CCM Decision, and to carry out any duties delegated to it by the CCM.[110] The MTC primarily functions to monitor and report on the development of a common trade policy, propose to the CMG any new regulations or changes to regulations relating to trade or customs policy, and propose revisions to tariff rates on specific items.[111] The JPC exists to help speed the integration process by "ensur[ing] the prompt entry into force of the decisions taken by the MERCOSUR organs."[112] ESCF serves as a consultative forum for the nongovernmental entities in the economic and social sectors.[113] The MAS is the operational support body that is responsible for publication and archiving the regulations and decisions of the other organs, as well as, handling organizational matters for the other organs through its base of operations in Montevideo, Uruguay.[114]

As noted previously, the Protocol of Brasilia governs any dispute resolution in MERCOSUR. In contrast to the approach taken by NAFTA which allows individuals to bring claims, all dispute matters in MERCOSUR must be handled on a governmental level.[115] The claims procedure begins with direct government-to-government negotiations; if they fail, the executive body of MERCOSUR makes a recommendation; if no agreement is forthcoming, the process ends with a binding decision from an ad hoc arbitration tribunal.[116] Although it did not create a supranational court some have argued that under the Vienna Convention on Treaties, to which all MERCOSUR members are party, the MERCOSUR rules are superior to the national rules of its members.[117]

Anti-dumping and countervailing duties were not addressed in any of the main protocols or the Treaty of Asuncion. Instead, it was agreed between parties that they would apply their own national legislation and coordinate their policies through an exchange of information until a MERCOSUR wide policy could be

110. *Id.* at art. 15.

111. *Id.* at art. 19.

112. *Id.* at art. 25.

113. *Id.* at art. 29.

114. Protocol of Ouro Preto, *supra* note 41, at art. 32.

115. MERCOSUR, *supra* note 7 at Annex III, par.1. (MERCOSUR and the Treaty of Brasilia both only contemplate resolution of disputes between "State Parties.")

116. *See* De Aguinis, *supra* note 95, at 606; *See also* Arocena, *supra* note 93, at 12.

117. *See* De Aguinis, *supra* note 95, at 613.

implemented.[118] CMC Decision 18/96 from December 1996 establishes a Protocol for the Defense of Competition that shifts the competition policy away from national legislation and to its procedural control after December 31, 2000 for intra-MERCOSUR disputes.[119] Currently there are no procedures for investigating third country trade practices affecting MERCOSUR, but they are expected by the time that the Protocol for the Defense of Competition becomes controlling.[120]

A trade in services protocol is contemplated within the framework of the MERCOSUR agreement; however, it is still in the process of negotiation. It is expected to be similar to the General Agreement on Trade in Services (GATS) that was recently negotiated within the framework of the World Trade Organization.[121] There has been some agreement on issues such as mutual recognition of high school and technical degrees.[122] However, Brazil, unlike Argentina, has been reluctant to enter into a commitment in GATS, so any progress in this area will be slow.[123]

Finally, as is illustrated by the preceding paragraph relating to a trade in services protocol, and unlike the NAFTA discussed in the previous section, many areas of harmonization are still in a state of development and have little or no supranational regulation to promote a single market policy. Some of these areas include standards related measures, government procurement, telecommunications, financial services, and protection of intellectual property.

C. *Impact of the Agreement on Member Trade*

The creation of MERCOSUR is the most significant and ambitious attempt by a group of developing countries to form a trading bloc to date. In 1997, its population reached over 207 million people and it had a gross domestic product of $758 billion

118. *See* O'Keefe, *supra* note 99, at ch. 14-13,14; *See also* Arocena, *supra* note 93, at 12-13.

119. *See* O'Keefe, *supra* note 99, at ch. 14-14.

120. *See id.*

121. *See* Shirley Coffield, Lecture on MERCOSUR structure, NAFTA and other regional trade agreements, Georgetown University, (April 1, 1998).

122. *See* O'Keefe, *supra* note 99, at ch. 14-18.

123. *See* Ocampo, *supra* note 94, at 382.

dollars.[124] Intra-MERCOSUR trade accounted for almost 25 percent of all member trade and over half of its total exports were destined for countries in the Western Hemisphere.[125] If one were to include Chile and Bolivia, the MERCOSUR free trade area accounts for almost 30 percent of member trade.[126] Despite the many detractors and critics who argued that MERCOSUR would fail to be implemented as many free trade agreements between developing countries have, in October 1996 the World Trade Organization reported that "intra-regional trade between [the] MERCOSUR partners has been duty free since 1 January 1995 except for 29 tariff line items" out of 9,107, which amounts to 95 percent of all intra-MERCOSUR trade being at the zero tariff level.[127]

1. Economic Effects

Until the recent shift toward trade liberalization, most countries in Latin America focused their development on the policy of import substitution.[128] With this policy, the countries maintained very high tariff rates to encourage development of domestic industry at the expense of imports.[129] This was implemented in spite of any inefficiencies or increased expense of the product that resulted from domestic production. As a result of these high tariffs there was very minimal intra-regional trade between Latin American countries even for products from particular countries which had a comparative advantage. Furthermore, what export trade Latin American countries did engage in was directed outside Latin America, primarily toward the United States and Europe.[130] MERCOSUR is attempting to change that by generating greater regional trade.[131]

From 1990 to 1994, intra-MERCOSUR imports by Argentina

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124. *See Integration and Trade in the Americas*, *supra* note 43, at 4.

125. *See id.* at 2 (If one were to include Chile and Bolivia, intra-MERCOSUR trade increases another five percent). *Id.*

126. *See id.*

127. *See* Alexander Yeats, World Bank Working Paper, *Does MERCOSUR's Trade Performance Raise Concerns about the Effects of Regional Trade Arrangements?*, February 1997, p. 24.

128. *See* Arocena, *supra* note 93, at 6.

129. *See* Iglesias, *supra note 46, at 5.*

130. *See* Arocena, *supra* note 93, at 39-40.

131. *See* Arocena, *supra* note 93, at 39-40.

increased almost six fold with its imports from outside MERCOSUR also increasing more than five fold, Brazilian imports from MERCOSUR members climbed 100 percent and by 38 percent from non-MERCOSUR members, intra–MERCOSUR imports by Paraguay rose by 85 percent with no change in its imports from extra-MERCOSUR countries, and Uruguayan imports from MERCOSUR and non-MERCOSUR countries were up by two and one half times and 74 percent respectively.[132]

Between 1990 and 1994 Argentina's exports to MERCOSUR members increased two and a half times with only a 4.5 percent increase in exports to the rest of the world during the same time frame, Brazil's intra-MERCOSUR exports increased 4.5 tines while extra-MERCOSUR exports only increased 25 percent, Uruguay showed a 52 percent increase in intra-MERCOSUR exports as opposed to an 8 percent increase for extra-MERCOSUR exports, and Paraguyan exports to all countries declined.[133]

The above numbers indicate that the intra-regional trade is increasing at a much greater rate for most MERCOSUR members than non-member trade, the fact remains that imports and exports have increased across the board. This trend of increased trade indicates that all of the trading partners of MERCOSUR members should be benefiting from trade creation whether they are part of MERCOSUR or not.[134]

2. Trade Distortion

As noted in the NAFTA section, many argue that although there are benefits to regional trade arrangements, such as MERCOSUR, because they increase intra-regional trade, they also tend to discriminate against nonmembers potentially resulting in trade diversion.[135] It is also generally held that this diversion is only present where there are high tariffs governing non-member trade and many point to MERCOSUR to support that reasoning. While it is true that the MERCOSUR external tariff rates have been reduced, they are still considered high. In

132. *See id* at 39-40.
133. *See id.*
134. *See* Iglesias, *supra* note 46, at 11.
135. *See* Bernal, *supra* note 69, at 949.

fact, MERCOSUR tariffs for non-members are above average for industrial countries at approximately 3.9 percent.[136]

While a 1996 Inter-American Development Bank analysis of MERCOSUR trade showed that there was distortion in only one sector as a whole, petroleum, and about fifteen percent of the overall product categories.[137] Analysis of trade statistics shows that the MERCOSUR agreement has created a major reorientation toward intra-member trade which has not occurred in agreements like NAFTA.[138] On average about 63 percent of intra-MERCOSUR trade is manufactured products, about 15 percent above the extra-MERCOSUR export level.[139] The intra-MERCOSUR trade of food and animal feeds is approximately 11 percent lower than the trade of those products to nonmember markets with transport and machinery goods becoming increasingly important.[140] Finally, over 81 percent of Brazil's intra-MERCOSUR exports are manufactured goods.[141] Based on these figures one must ask whether this shift in trade orientation is genuinely justified based on comparative advantage rather than other distorting factors.

As was previously discussed, there has been a shift in labor intensive production, under NAFTA, to Mexico, where the low cost labor makes the labor intensive products cost effective, while capital intensive products have remained in the United States and Canada. However, with MERCOSUR members, there seems to be a shift away from imports of capital intensive products from extra-MERCOSUR suppliers and toward intra-MERCOSUR suppliers. From 1989 to 1994 intra-MERCOSUR vehicle exports increased from $207 million to $2.1 billion, an increase of over 900 percent, domestic electrical appliances exports increased from $12.5 million to $97.3 million, a 675 percent increase, special industrial machinery exports increased from $10.7 million to $120 million, an increase of over 1000 percent.[142] A World Bank report tracking these and 27 other separate product categories showed that most of the products in which intra-

136. *See* Yeats, *supra* note 126, at 2.

137. *See* Iglesias, supra note 46, at 11, *quoting* IDB period note December 1996, Annex 1.

138. *See* Yeats, *supra* note 126, at 8.

139. *See id.* at 5.

140. *See id.* at 7.

141. *See id.* at 5.

142. *See id.* at 13.

MERCOSUR trade was increasing were being traded at a significantly and disproportionately higher level within MERCOSUR than they were in non-member markets.[143] Additionally, these same products required a higher than average capital intensity, in opposition to the comparative advantage that MERCOSUR countries have in labor intensive production.[144]

An analysis of regional comparative advantage showed that MERCOSUR is becoming less competitive internationally in products that were the biggest part of the reorientation toward intra-member trade.[145] In point of fact, the top five products with the greatest shift toward intra-MERCOSUR trade, non-alcoholic beverages, lead, prepared dairy, non-wheat meal or flour, and perfumes/cosmetics, are among the least competitive internationally.[146] Three other product categories, transport equipment, non-electrical machinery, and electrical machinery, which accounted for over fifty percent of the increase in intra-MERCOSUR trade between 1988 and 1994 were also among the least competitive products made in MERCOSUR.[147] This indicates that the products with the biggest gains in intra-MERCOSUR trade are ones that cannot be exported to non-member countries because they are so uncompetitive and need the protective tariffs to thrive.

Not surprisingly, the same products which enjoyed the greatest shift toward intra-MERCOSUR trade also enjoyed the highest tariff levels on foreign imports.[148] On average, they were protected by a duty of approximately 18 percent, seven percent higher than the average duty on the other goods analyzed in the report.[149] In addition to the high tariff levels there is the application of non-tariff barriers to about 21 percent of all tariff line items.[150] A more extreme example of this protection is automobile production in MERCOSUR countries, one of the most heavily protected industries in the region, with even trade

143. *See id.* at 15.
144. *See* Yeats, *supra* note 126, at 15.
145. *See id.* at 18.
146. *See id.* at 17.
147. *See id.* at 18-20.
148. *See id.* at 23.
149. *See* Yeats, *supra* note 126, at 26.
150. *See id.* at 28.

between members subject to quotas.[151] In April 1995, Brazil raised its tariff on automobiles from non-MERCOSUR countries from 20 percent to 70 percent.[152] Shortly afterward, in June 1995, Brazil also reduced its tariff on capital goods, components, and raw materials to the sector from 18 percent to 2 percent.[153] These two actions created a preference for member manufactured cars and forced any other automobile manufacturers to manufacture their products in MERCOSUR countries or be shut out of a significant portion of the automobile market.

There appears to be a trend with MERCOSUR producers reorienting their products for intra-MERCOSUR trade based on the protection of higher tariffs and other trade barriers allowing them to continue being uncompetitive. This may be creating a situation where MERCOSUR consumers are paying higher prices for lower quality products. If not for the barriers, consumers would be paying less for better quality goods which were purchased from extra-MERCOSUR sources.

IV. THE FTAA

A. *Overview*

The proposed FTAA comprised 776 million potential consumers from countries that had a combined GDP of $8.5 trillion in 1997.[154] In 1996, total trade to the potential members of the FTAA totaled over $2.4 trillion or 22 percent of world trade.[155] If current trends continue the Western Hemisphere will be the world's largest market with more than 850 million consumers buying $13 trillion in goods and services within only a

151. *See* Arocena, *supra* note 93, at 17 (Despite the quota system there has been free trade in vehicles and parts between Brazil and Argentina since 1986). *Id.* at 31. (Although it currently is regulated by bilateral agreements the members of MERCOSUR have agreed that automobiles will be included in the common external tariff scheme and have a zero tariff on intra-member trade by January 1, 2000).

152. *See id. at* 17.

153. *See id. at* 30-31.

154. *See Integration and Trade in the Americas, supra* note 43, at 4.
(As noted earlier, the scope of the current negotiations includes every country in the Western Hemisphere except Cuba).

155. *See* Raymond J. Ahearn, Congressional Research Service, Hemispheric Trade: Status, Hurdles, and Opposition, Nov. 25, 1997, p. 1.

few years.[156]

B. *Negotiations and Proposed Structure*

As noted previously, the formal negotiations to establish the FTAA began in April 1998. The countries involved in the negotiations have agreed that the FTAA will be a hemisphere-wide, separate agreement negotiated by the parties that will coexist with all current regional agreements.[157] Furthermore, it will be consistent with all WTO obligations, and liberalization should be completed within ten years of signing.[158]

A tripartite committee, composed of the OAS, Inter-American Development Bank, and U.N. Economic Commission for Latin America and the Caribbean, will oversee the entire process, including the other three areas of negotiation aside from the FTAA.[159] The basic structure of the negotiations is centered around the following principles:

* consensus constitutes the fundamental principle of decision-making in the FTAA process;

* any eventual undertaking on a free trade area must take the form of a comprehensive single undertaking;

* the FTAA can co-exist with bilateral and subregional agreements to the extent that the rights and obligations under these agreements are not covered by or go beyond the rights and obligations of the FTAA;

* the FTAA must be fully consistent with WTO agreements, in particular with Article XXIV of the GATT 1994 and its Uruguay Round understanding and Article V of the GATT;

* special attention should be given to the needs, economic conditions and opportunities of the smaller economies to ensure their full participation in the process;

* a temporary administrative Secretariat should be established to support the negotiations;[160] and

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156. *See* Ahearn, *supra* note 11, at 3.

157. *See* Ahearn, *supra* note 161, at 3.

158. *See id.* at 3-4.

159. *See* James Holbein, Lecture on NAFTA and other regional trade agreements, Georgetown University, (April 22, 1998).

160. *See id.* (In spite of this goal, no site was agreed on at April 1998 meeting in

* 2005 is the target date for concluding negotiations, at the latest.[161]

Although it is only one member of the tripartite committee overseeing the entire negotiation, the Organization of American States plays such a very important role of the FTAA process that any discussion of the process must include it. The FTAA function in the process includes the Special Committee on Trade (SCT), Special Committee of the Permanent Council on Inter-American Summits Management (SCIASM), the Inter-American Juridical Committee (IAJC), the Trade Unit, and the Secretariat for Legal Affairs.[162]

The objective of the SCT is to promote trade liberalization and expansion among countries in the hemisphere. It achieves this goal by coordinating with the various regional and subregional trade organizations and non-governmental organizations in the hemisphere, studying and analyzing existing integration agreements, and preparing a compilation of data on the region.[163] The objective of the SCIASM is to coordinate all the activities of the OAS dealing with the four categories that comprise the process which includes the FTAA. The IAJC is an advisory body on legal matters relating to the integration and international trade issues including possible methods of dispute settlement under the FTAA.[164] The Trade Unit is part of the General Secretariat and functions as a source of technical support for the SCT by providing it with information on inter-country integration within the hemisphere and strengthening trade information systems.[165] The SLA is tasked with promoting legal and judicial cooperation between the countries involved in the process and providing advisory services for other parts of the OAS to assist in the drafting of uniform national laws.[166]

Twelve working groups are involved in the negotiations:

Santiago. Therefore, no permanent site for the FTAA secretariat has been decided as of the writing of this paper. For the near term, it is scheduled to revolve between three cities: Miami until 2001, Panama City from 2001 until 2003, and Mexico City from 2003-2004.)

161. *See Integration and Trade in the Americas*, *supra* note 43, at 18.

162. *See* Jeanette M.E. Tramhel, *Free Trade in the Americas: A Perspective from the Organization of American States*, 19 HOUS. J. INT'L L. 595, 597-603 (1997).

163. *See id.* at 598-99.

164. *See id.* at 600-03.

165. *See id.* at 602.

166. *See id.* at 602-03.

market access, customs procedures and rules of origin, investment, standards and technical barriers to trade, sanitary and phytosanitary measures, subsidies, anti-dumping and countervailing duties, small economies, intellectual property, services, competition policy, and dispute resolution.[167] Although there is no real structure to the FTAA at this writing, the separate negotiating groups are indicative of what will likely be the major components of the final agreement. These are substantially the same categories that were used during the NAFTA negotiations and are more than likely the core of the agreement that will be signed at the end of the negotiations, early in the twenty-first century. Furthermore, many of these working groups, whose subject matter is discussed in the previous sections on NAFTA and MERCOSUR, will be sources of conflict simply because of the interplay between the United States attempting to achieve language close to that of NAFTA and Brazil seeking language that closely tracks that of MERCOSUR.

The largest areas of potential conflict between the two trade blocs are 1) rule of origin requirements, 2) anti-dumping and countervailing duties 3) telecommunications, 4) financial services, and 5) intellectual property.[168] The reason for the conflict is the substantial difference that exists between MERCOSUR and NAFTA in these areas. For example, the NAFTA rules of origin are much more complex and have a higher local content requirement then either MERCOSUR or the recent Chile-Canada Free Trade Agreement.[169] In the area of anti-dumping and countervailing duties, there is serious resentment not only to the United States application of the duties, but to their use in general. In point of fact, the Chile-Canada Free Trade agreement has an anti-dumping phase-out and MERCOSUR prohibits their use internally after 1999.[170] Financial services are also an area of concern because the United States enjoys a substantial comparative advantage, and it has been traditionally considered closed to non-nationals in many developing countries, including Brazil and Uruguay.[171]

167. *See Integration and Trade in the Americas*, *supra* note 43, at 17-18.

168. *See* O'Keefe, *supra* note 4, at 307.

169. *See id.* at 306. (The Chile-Canada Agreement only requires 35 percent local content).

170. *See id.; See also* O'Keefe, *supra* note 99, at ch. 14-13,14.

171. *See* O'Keefe, *supra* note 99, at ch. 14-9,10.

Telecommunications is also another area that usually has restrictions on foreign investment in developing countries, including Brazil, Uruguay, and Paraguay, and one in which the United States and Canada also enjoy a substantial comparative advantage.[172] Finally, intellectual property protection has long been a source of contention because many Latin American countries consider it to be an obstacle to development and any United States attempt to adopt NAFTA-type protections will not be received well.[173]

One of the problems with the approach that is being taken with the FTAA negotiations is that the agreement will overlay the 23 trade pacts or agreements in the region. This is further complicating the current overlap of many regional and subregional agreements with yet another layer of rules and regulations governing trade transactions, creating more confusion.

Any hemispheric trade agreement is going to revolve around the two biggest trade entities in the Western Hemisphere, NAFTA and MERCOSUR. Together the two blocs constituted over 92 percent of all exports in the hemisphere in 1997.[174] Although the NAFTA partners are not negotiating as one, like MERCOSUR, they are as much of a force to be reckoned with as is MERCOSUR. As a result, any accord will be difficult to achieve in the areas that there is divergence of objectives and incompatibility between the two agreements.

C. Impact of the Proposed Agreement on the Hemisphere

The population of countries in the proposed FTAA was 776.3 million in 1997 with a gross domestic product of $8.54 trillion.[175] If one were to exclude NAFTA from the hemispheric calculations, it would mean United States access to a market of 380.4 million people with a combined GDP of $1.1 trillion growing at approximately 5 to 6 percent a year.[176] Analyzing the numbers from the Latin American perspective, it gives those countries

172. *See id. at* ch. 14-9.
173. *See id. at* ch. 14-11.
174. *See Integration and Trade in the Americas*, *supra* note 43, at 2.
175. *See id.* at 4.
176. *See id.* at 4-5.

duty free access to the 395.9 million person NAFTA market with a GDP of $7.45 trillion.[177] The economies of Argentina, Brazil, Chile, and Mexico comprise nearly 85 percent of the current economic output of Latin America.[178] At the other end of the prosperity spectrum, there are small economies which depend almost exclusively on a single commodity or product.[179]

Despite their size and share of the Latin American economy as a whole, the trade impact of the FTAA on MERCOSUR countries, at least initially, would be muted because a substantial portion of MERCOSUR trade will be within the customs union and already duty free or will be with Europe which is outside the FTAA.[180] A study by the Centro de Economia Internacional - Buenos Aires showed that Argentina would only gain approximately $100 million annually in increased trade, against a U.S. increase of $1.5 billion.[181] In 1997, only 16.3 percent of all MERCOSUR exports were directed toward NAFTA, of that a substantial portion was to Mexico.[182] Furthermore, the growth rate of MERCOSUR exports to NAFTA was substantially slower than the increase of exports to the rest of the hemisphere.[183] In this context it is notable that in 1994, for the first time, Brazil, with Latin America's largest industrial base, surpassed the United States in exports to Latin America.[184] In this context it is understandable that Brazil is reluctant to subject its substantial manufactured goods export base to unrestricted competition from U.S. sources.

One of the main concerns from MERCOSUR regarding the FTAA is that trade from cheaper sources outside of the Western Hemisphere will be diverted to the United States because of the purchasing power available and the lack of tariffs to protect their industry, thereby creating a dependence on the United States for

177. *See id.* at 4.

178. *See* Mark, B. Baker, *Integration of the Americas: A Latin Renaissance or a Prescription for Disaster?*, 11 TEMP. INT'L & COMP. L.J. 309, 318 (1997); *See also* De Aguinis, *supra* note 95, at 601.

179. Baker, *supra* note 183, at 318.

180. *See* Yeats, *supra* note 126, at 4 (Table 1).

181. *See* De Aguinis, *supra* note 95, at 629.

182. *See Integration and Trade in the Americas*, *supra* note 43, at 2.

183. *See id.* (NAFTA exports only increased at 3.6 percent whereas exports to Latin America increased 18.4 percent.) *Id.*

184. *See* Baker *supra* note 183, at 328 (Eighty percent of Brazil's exports to Latin America were in the form of manufactured goods).

capital goods and inputs.[185] At the same time, MERCOSUR argues that it would have little to gain for the increased costs of the diversion because of the low level of trade with the United States.[186] However, despite the concerns from MERCOSUR, it cannot be denied that the FTAA will secure access to one of the world's biggest markets and lock in an advantage in Latin America. While traditionally most U.S. hemispheric imports have been from Central America and northern South America, recently there has been a significant increase in trade with other countries in the hemisphere.. Between 1990 and 1996, exports to Brazil increased 149 percent, exports to Argentina grew 275 percent, and exports to Chile climbed 141 percent.[187] At the same time U.S. imports increased 11 percent from Brazil, 53 percent from Argentina, and 77 percent from Chile.[188] In 1997, 74 percent of Latin America's exports went to NAFTA.[189]

In considering the U.S. view of the benefits of the FTAA, an Institute for International Economics study shows that hemispheric integration would increase U.S. exports to Latin America by about $36 billion and U.S. imports by $28 billion above the levels that might be reached without further integration for the period between 1997 and 2002.[190] Hemispheric wide free trade would boost the economies of the region by 1.5 percent a year.[191] If the agreement were currently in place, the regional output would be increased to almost $300 billion a year by 2002 and foreign investment would rise by almost $10 billion a year.[192] Although Latin America is currently only 7 percent of U.S. trade, it holds the promise of faster, long-term growth and potential to be an important export market. It also would support long-term merchandise trade markets, open new trade in service markets and investment markets, and support continued stability in the hemisphere. Between 1990 and 1996 U.S. exports to Latin America, excluding Mexico,

185. *See* O'Keefe, *supra* note 99, at ch. 14-17 (Currently, most of MERCOSUR sourcing is done with Europe).

186. *See id.* at ch. 14-17,18.

187. *See* J.F. Hornbeck, Congressional Research Service, *A Free Trade Area of the Americas: Toward Integrating Regional Trade Policies,* Sept. 25, 1997, p. 7.

188. *See id.*

189. *See Integration and Trade in the Americas, supra* note 43, at 2.

190. *See* Ahearn, *supra* note 11, at 3.

191. *See id.* at 5.

192. *See id.*

increased by 103 percent.[193] While during that same time period, U.S. imports from Latin America, excluding Mexico, increased only 44 percent.[194]

Since 1989, U.S. exports to Latin America have increased at more than double the rate of exports to other parts of the world.[195] Most of these exports are high value, with imports concentrating on raw materials and complementary products.[196] If trends continue, by the turn of the century U.S. exports to Latin America will exceed combined exports to Europe and Japan.[197] Importantly, these increased exports are in technology enhanced industrial exports such as automobiles, computers, telecommunications equipment, and electrical and power generation equipment.[198] All of these products are produced efficiently by the United States and are subject to serious competition from Japan and East Asia in third markets outside of the Western Hemisphere.[199] In contrast U.S. imports from Latin America are mostly semi-manufactured goods, natural resource based products, and petroleum products.[200]

Finally, even if you were to exclude the NAFTA-MERCOSUR competition dynamic, the creation of an FTAA would benefit Latin America significantly because of the recent growth in intra-regional trade. In 1996, 54 percent of all Western Hemisphere exports were to destinations in the hemisphere.[201] Intra-hemisphere exports grew faster than extra-hemisphere exports by almost three percent.[202] In 1996, 74 percent of MERCOSUR exports and 55 percent of all NAFTA exports were for the Western Hemisphere.[203] Additionally, 35.1 percent of all MERCOSUR exports to the hemisphere were to Latin America, and while only 24 percent of NAFTA intra-hemispheric exports went to Latin America,[204] NAFTA exports to MERCOSUR alone

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193. *See* Hornbeck, *supra* note 191, at 6.
194. *See id.*
195. *See* Ocampo, *supra* note 94, at 377.
196. *See id.*
197. *See id.*
198. *See* Hornbeck, *supra* note 191, at 6.
199. *See id.*
200. *See id.*
201. *See Integration and Trade in the Americas*, *supra* note 43, at 2.
202. *See id.* (Intra-hemisphere exports increased by 12.9 percent as opposed to extra-hemisphere exports which only increased by 10.1 percent). *Id.*
203. *See id.*
204. *See id.*

grew at 13 percent from 1996 to 1997.[205]

V. CONCLUSION

In the final analysis, it is difficult to determine what results the FTAA would bring to both Latin America and the United States as far as trade benefits are concerned.

This paper has shown that even NAFTA, which is not supposed to create trade distortive effects because of the low U.S. and Canadian tariffs, does appear to do so and has not achieved the results that many had argued that it would. While it is possible that gains expected from free trade with Mexico need to be evaluated over the long term, I believe that Mexico is indicative of the results that the United States will see with free trade to Latin America as a whole. Like U.S.-Mexico trade, it is a small part of the U.S. trade picture today. It is dwarfed by U.S. trade to Asia, Europe, and Canada. However, an acknowledgment must be made of the recent, significant growth of U.S. trade to the region, albeit from a small base, and the fact that Latin America is projected to be an economic force in the near future at its present rate of growth. With this being so, can the United States sit by and pass up the opportunity to secure such a market for the future? I believe that the answer in this case is a definitive no; if the United States does let it pass, it will not only surrender the market, but possibly leadership in the region to MERCOSUR.

While it is true that the creation of a hemispheric free trade area would secure the lucrative market of the United States for Latin America, what benefit would it be to those countries with the largest economies in Latin America, Brazil and Argentina, when they have little to gain because only a small amount of their trade is with the United States? As was shown in the analysis above, MERCOSUR has a significant problem with trade distortion and this could be easily translated into a hemisphere-wide phenomenon with the creation of the FTAA. However, despite the risks of this effect, can Latin America, like the United States, pass on securing an access to a market that will provide the kind of sustained long-term growth that is needed to maintain the economic development that the region

205. *See id.*

seeks? I believe that the answer is no because as Mexico has shown with the significant increase in foreign direct investment, falling trade barriers means increased investment in the economy.