

Deputy Undersecretary (ILAB), Sandra Polaski

**Statement of Sandra Polaski, Deputy Undersecretary,
Bureau of International Labor Affairs (ILAB)
Testimony before the Subcommittee on Trade of the House Committee on Ways and
Means
November 17, 2009**

Introduction

Chairman Levin, Ranking Member Brady and distinguished members of the Subcommittee on Trade:

On behalf of the Department of Labor, thank you for the opportunity to discuss how to ensure that U.S. trade preference programs are achieving their goals.

As you know, U.S. trade preferences were created in order to spread economic growth and development through new trade opportunities for developing countries. Secretary Solis and I support this goal. The Secretary has made the overarching goal for the Department of Labor *Good Jobs for Everyone*. In the Department's Bureau of International Labor Affairs (ILAB), which I lead, we support this goal by working to ensure that workers and their households are able to share in the benefits of trade — both in developing countries and here at home. This goal is also an essential component of the President's broader vision for international growth and development that broadly benefits the people of the world.

Today I would like to focus on one essential aspect of preference programs — the labor component. I will discuss the role that labor provisions play in preference programs, and why they are indispensable in achieving the development objectives of preference programs. I will also share some observations on the functioning of the preference programs, particularly areas where Congress may want to consider whether the programs could be improved.

Trade, Labor and Economic Development

When Congress authorized the first U.S. trade preference program — the Generalized System of Preferences (GSP) — through the 1974 Trade Act, the goal was to provide greater access to the U.S. market for developing countries. The purpose was to create additional export opportunities which would attract investment, develop new industries, create jobs, and thereby foster growth and development. Since then, Congress has expanded U.S. trade preferences roughly each decade through the Caribbean Basin Initiative (CBI) in 1983, the Andean Trade Preference Act (ATPA) in 1991, the African Growth and Opportunity Act (AGOA) in 2000, and the Haitian Hemispheric Opportunity through Partnership Encouragement (HOPE) Act in 2006 and 2008. Each of these new programs modified the original GSP model to incorporate the knowledge and experience gained about how best to stimulate development using market access incentives.

One of the key ways in which the preference programs evolved over these last 35 years was through the program eligibility criteria that beneficiary countries must meet in order to receive

unilateral duty exemptions. Congress gradually included eligibility criteria in the programs — covering matters as diverse as treatment of investors and treatment of workers — that reflected the understanding that without a positive policy framework greater access to the U.S. market alone would not lead to broad-based and sustained development.

The labor requirements of preference programs first emerged in 1984, when Congress and then-President Reagan negotiated the addition of *internationally recognized worker rights* to the GSP eligibility criteria. This innovation reflected the understanding that fundamental labor rights were an essential component of broad-based economic development in low and middle income countries, just as they were an essential component in our own economic development. Labor markets in many developing countries are characterized by numerous shortcomings. Economic power is often highly consolidated and the institutions that would allow workers to claim their rights under law are often very weak. In some countries these problems are compounded by pervasive corruption. Under these conditions, the likelihood is low that trade preferences alone will easily translate into significant and sustained benefits for workers and their families. However, if workers share in the benefits of trade and have effective means of addressing their exclusion, then the economic growth that comes from expanding trade may help address existing inequalities. It should increase the incentives for employers and workers to upgrade productivity and skills, rather than encouraging cost-cutting through disregard of national labor laws and international labor standards. When labor is free from coercion, when children are kept in schools rather than factories, and when workers are able to freely organize and bargain for their interests, the economic opportunities that come through trade are more likely to create widespread prosperity and put the beneficiary country on a virtuous upward cycle.

By protecting the most basic human and workers' rights and ensuring a broader distribution of gains throughout an economy, the labor provisions of trade preference programs also spur global aggregate demand which is good for U.S. workers and firms. By helping to build a more level playing field in the global economy, they shore up support for free trade both at home and in recipient countries.

Improvements in Worker Rights

By adding the labor eligibility provisions on *internationally recognized worker rights* to the U.S. preference programs, Congress created both a requirement and an opportunity for developing countries to improve their labor standards. As we have utilized these provisions in the past, they have led to positive changes in workers' lives.

For example, in August 2005 the U.S. government accepted for review an AFL-CIO petition to remove Uganda's eligibility for GSP benefits. The petition alleged serious shortcomings in Ugandan labor law and enforcement, including a requirement that a minimum of 1,000 workers were needed to form a union. Following high-level U.S. government demands on the issues raised in the petition, Uganda committed to expedite passage of long-overdue labor legislation to improve the situation. The legislation, which the International Labor Organization (ILO) reviewed, addressed each of the main problems cited in the petition and was ultimately passed and enacted in May 2006. The government also undertook measures to fund and begin

operations of a new industrial court for labor issues, and posted labor inspectors in each district of the country.

On occasion benefits have actually been withdrawn when countries did not make progress addressing worker rights and other eligibility criteria. For example, Liberia's benefits were suspended in 1990 because of worker rights concerns. However, following two decades of war, Liberia's new President, Ellen Johnson Sirleaf, made improving worker rights a high priority. This included repealing a decree that prohibited strikes and inviting the ILO to assist Liberia in bringing its laws and practices into conformity with its ILO obligations. In 2006, Liberia's GSP eligibility was reinstated.

Trade preferences have also been used to provide additional incentives for countries to make concerted improvements in worker rights. In 1999, the U.S. negotiated a textile agreement with Cambodia that offered additional textile quota annually to Cambodia when worker rights criteria were met based on factory-level monitoring reports. I was closely involved in the creation and implementation of that agreement and believe that certain lessons from that experience continue to be instructive today.

First, the agreement aligned the market incentives facing the government, investors, international buyers, employers, and workers. Since improvements in working conditions were tied to a positive incentive — increased textile quota — both the private sector and the government benefited when workers benefited. Because the quota determinations were made annually, there was a close temporal relationship between improvements on the factory floor and greater market access. The result of the program was significant growth in trade, employment, and incomes for apparel workers in one of the world's poorest countries. From 80,000 apparel jobs in 1998¹ before the agreement took effect, employment increased to over 350,000 jobs by the end of 2008.² As the industry and employment were growing, the labor rights of Cambodian workers and their working conditions also improved. It is important to note that even after the Multi-Fiber Agreement ended at the end of 2004 — and with it the quota incentives that were used at the beginning of the program — the country continued its efforts to improve worker rights.

A second element of the Cambodia program that deserves close attention is the way the factory conditions were monitored and the information was transmitted. The program introduced an innovative design that combined transparency and integrity to overcome limited market information and lower costs for producers. The ILO was asked by the U.S. and Cambodian governments to carry out a monitoring program, known as the *Better Factories* project, that monitored factories and made the results public. This provided transparency about the conditions in all the export firms to international buyers, consumers and other factories, as well as to the governments and the labor force. This information helped buyers make better sourcing decisions and rewarded the factories that were improving, while channeling business away from factories with a record of labor abuses. Since the monitoring was conducted by a credible outside entity, buyers were able to reduce or eliminate their own inspections of their supplier factories. Since factories pay for these buyer-required inspections, the program reduced factory costs and eliminated redundant monitoring. Estimates show the Cambodia monitoring program cost factories about \$3 per worker per year, compared to third-party monitoring costs of up to \$50 per worker per year.

A third element in the success of the program was the decision by the Cambodian government that all firms benefiting from the market access should participate in the *Better Factories* project. This ensured that factories that complied with the national labor laws and internationally recognized worker rights were not at a disadvantage compared to factories not in the program. This sector-wide participation avoided creating perverse incentives in which factories joining the program would be subject to greater transparency than factories outside the program, which would free ride on the reputation of the industry and program benefits. It also avoided the risk that the reputation of Cambodia and its apparel industry could be damaged by media exposes of poor labor practices by non-compliant factories outside the program.

In sum, preference programs can be effective tools to both promote economic development and improve labor standards, so that economic development is broad-based and sustainable. Our preference programs work best when economic incentives are aligned in a way that produces optimal results for overall growth of exports, employment generation and improved respect for workers' rights. That is when we are most likely to see broad distribution of the benefits from preferential access to our market.

Observations on Existing Preference Programs

Since the original inclusion of internationally recognized worker rights in the GSP statute, the United States has included labor provisions in every subsequent preference program and virtually every free trade agreement. However, Congress created the preference programs over time, and our current system is made up of varying levels of benefits, eligibility criteria and eligibility reviews. These variations provide insight into how the incentives created by the programs work in practice.

Incentives

Congress has authorized the preference programs to provide benefits to countries that meet the eligibility criteria and to remove benefits when these criteria are not being met. The objective of the labor provisions of the programs is to align the incentives facing government, employers and workers. When we have been able to effectively operationalize this alignment, we have been able to make significant and lasting progress.

Regarding the incentives, I want to make an important point. The goal of reviewing a country's eligibility is not to remove benefits, but rather to encourage compliance. It may be helpful to think of the analogy to enforcement of U.S. labor laws. The goal of enforcement is not to impose penalties, but rather to create effective deterrents in order to elicit voluntary compliance. For the incentives in our preference programs to be effective, they must be credible, just as our domestic enforcement must be credible.

The purpose of eligibility reviews — whether for worker rights or other program criteria — is to examine whether a country is failing to meet the criteria, engage with them to help them come into compliance, and — failing that — determine whether eligibility should be revoked. Eligibility for U.S. preference programs has been removed in the past at least 12 times due to failure to address abuses of worker rights, but nearly all of the actions were taken in late 1980s

and 1990s. There have been several occasions when countries responded to U.S. engagement, through the petition and review process, to make positive changes to come into compliance with eligibility criteria. When this happens, this is a win-win situation: improvements are made, and benefits are retained.

There has also been one worker rights case under the GSP program, involving Pakistan, in which benefits were withdrawn for some, but not all, eligible tariff lines. Under the HOPE Act, benefits can be withdrawn for particular firms that fail to meet the programs' requirements, but benefits are maintained for rest of the country. As currently authorized, preference programs provide duty-free access for eligible goods; but, if eligibility is revoked, then rates revert to the normal trade relations duty rate.

Transparency

Transparency helps provide better information to all stakeholders and can lead to desirable outcomes with efficiency and speed. President Obama has called on the federal government to improve the transparency of decision making. In administering the preference programs, the interagency representatives regularly meet with petitioners, government officials and other stakeholders to discuss the process and specific allegations when they are raised in a petition. Public hearings are also held to gather information. At the conclusion of the review process, a decision is made public on whether to close the review, continue the review or remove benefits. However, additional consideration could be given to how the process can be made further transparent.

Standards

Over time, our definition of labor rights has evolved. The definition of *internationally recognized worker rights* found in the GSP statute in 1984 preceded the development of the ILO's 1998 Declaration *on Fundamental Principles and Rights at Work*, a consensus definition which the U.S. supports. U.S. preference programs include the following labor rights:

- freedom of association and the right to organize and bargain collectively;
- a minimum age with respect to children;
- the elimination of the worst forms of child labor,
- freedom from compulsory labor, and
- "acceptable conditions of work" with respect to minimum wages, hours of work and occupational safety and health.

The ILO's 1998 Declaration includes these labor rights except for acceptable conditions of work. The Declaration also includes freedom from discrimination in the workplace as an additional right, which is not included in U.S. preference programs. The most recent U.S. free trade agreements combined the Declaration labor rights with acceptable conditions of work.

Petitions versus Systematic Reviews

Another area where preference programs vary is on the trigger for eligibility reviews of beneficiary countries. For example, the GSP and ATPA programs have a petition-driven process, while AGOA has an annual, self-initiated review. It should be noted that both systems have advantages and are not mutually exclusive. Petitions can serve to highlight, in a timely way, where significant labor abuses are occurring. These petitions are usually filed by stakeholders and organizations "on the ground" that have real-time knowledge and also may bring the capacity to collaborate on solutions to the problems identified.

However, there are also cases in which third-party petitions are not received simply because such stakeholder groups do not exist or because information is strictly controlled by the government, and organizations that typically would file petitions are constrained from doing so. In these cases, regular, systematic reviews by the U.S. may better identify countries that are failing to meet the eligibility criteria of the preference programs. For example, the AGOA annual, eligibility review examines every beneficiary country against each criterion every year and makes a recommendation to the President on eligibility. This has the benefit of applying the criteria universally and regularly each year. The review is completed at a certain date, and decisions on individual countries are rarely extended. In contrast, some GSP petition reviews remain open for several years. While this allows for greater discretion and engagement with the beneficiary country to address the concerns raised in the petition, it may also lessen the incentive for countries to act expeditiously. As a practical matter, though, I should mention that the GSP program has approximately 140 eligible countries, and a full, annual review process would be resource intensive. It may be preferable to effectively target resources at the most significant or strategic cases.

Conclusion

Thank you again for inviting me to participate in this hearing, Chairman Levin, Ranking Member Brady, and distinguished members of the Subcommittee. I believe we share the common goal of making preference programs more effective tools for development and poverty alleviation. Secretary Solis and I believe that the labor provisions of the preference programs are an essential component in meeting these goals. The Bureau of International Labor Affairs and the Department of Labor stand ready to provide any assistance or support to you and your staff as you continue in your deliberations.

Footnotes

¹Independent Final Evaluation Report (covering the period February 2003 — December 2005), *Ensuring that Working Conditions in the Textile and Apparel Sector in Cambodia Comply with Internationally-Recognized Core Labour Standards and the Cambodian Labour Law*, Luis Reguera & Christopher Land-Kazlauskas, P.7, Oct. 2007.

²*Twenty-Second Synthesis Report on Working Conditions in Cambodia's Garment Sector*, Better Factories Cambodia, International Labor Organization, April 30, 2009, p.5 (graph 3).