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WTO AND REGIONAL TRADE AGREEMENTS MONTHLY REPORT

September 2003

Due to the general nature of its contents, this newsletter is not and should not be regarded as legal advice.

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WTO Talks Collapse in Cancun: A Splash of Cold Water, or Dead in the Water?

WTO Members on Sunday afternoon, September 14, 2003 failed to agree on a Ministerial Declaration that would have given much needed momentum to the Doha Development Agenda (or "Round"). Discussions at the Cancun Ministerial collapsed due to numerous factors, including:

- ***Complications created by shifting agricultural alliances*** – The emergence of the "G-21+" group of developing country exporters (and declining relevance of the Cairns Group) created a new North-South dimension to agriculture negotiations. Coupled with African countries' demands on the reduction of cotton subsidies (an emotional issue which received a clumsy response), agriculture polarized the atmosphere for negotiations on a broader scale.

- ***ACP's rejection of EC concession on Singapore issues*** – The EC offered to remove investment and competition (the two more controversial Singapore issues) from the agenda on the last day, but perhaps too late. Despite the EC's major concession, the African Caribbean Pacific (ACP) group, angered by the cotton issue and spurred by anti-trade non-governmental groups ("NGOs"), refused negotiations on any of the four issues. Many countries have criticized the motive behind the ACP's resistance, which did not materialize until Cancun.

- ***Chairman's questionable decision to end talks*** – Chairman Derbez of Mexico called off talks early on Sunday, to the surprise and disappointment of many participants. The EC and others have questioned the Chair's decision and tried to revive talks, but it was too late.

- ***Conspiracy theories?*** – Some observers speculate that the talks were called off early due to developed countries' unwillingness to negotiate on agriculture. Some believe that certain NGOs exploited the ACP's anger over cotton and persuaded the group to scuttle talks.

Most participants were surprised by the sudden collapse of talks, which happened during the "Green Room" meeting among 30 countries. The US warned throughout the week that certain Members' demands were based on rhetoric and not the willingness to negotiate. USTR Robert Zoellick expressed frustration at the breakdown and warned that the US would pursue more aggressively bilateral and regional free trade initiatives. The EU criticized the WTO's decision-making process, and what it described as unreasonable positions of certain Members. Many of the G-21+ countries tried to distance themselves from the breakdown, and asserted that they intended to negotiate constructively.

WTO Members agreed to reconvene in Geneva at the Senior Officials level before December 15, in order to salvage the talks. It remains unclear whether the draft texts prepared at Cancun will be preserved to some extent, and serve as the basis for eventual agreements on modalities for outstanding issues such as agriculture, non-agricultural market access ("NAMA") and the Singapore issues.

It is now more obvious than ever that the December 2004 deadline for the Round is unattainable. History will tell if Cancun was a needed dose of cold water (and a wake up call to the developing country dimensions of trade), or a setback on the magnitude of the disastrous Seattle Ministerial.

Industrial Market Access Negotiations: Developing a Double Standard?

Negotiating modalities on non-agricultural market access ("NAMA" or industrial goods), is one of the critical areas of the Doha Development Agenda where WTO Members have not yet reached agreement (initial deadline of May 2003). On August 22, 2003, Members failed to endorse a draft text prepared by the Chair of the Negotiating Group on NAMA, Ambassador Pierre Louis Girard that intended to set out a framework for reaching a future agreement on modalities for market access talks.

The major differences among Members exist in the following areas:

- ***Nature of tariff cutting formula***: Developed countries seek a higher level of ambition in tariff reduction, while developing countries propose relatively moderate cuts, especially in regard to their own tariffs. Developing countries would be subject to much deeper tariff reductions in this Round since developed countries' tariffs are mostly at a low level.

- ***Sectoral tariff elimination/harmonization***: Ambassador Girard's draft text on modalities[1] proposes duty reduction on seven product groups of export interest to developing countries Developed countries seek participation in the sectoral initiatives by all Members. Developing countries however, argue that they should participate on a voluntary basis.

General Council Chairman Carlos Perez del Castillo has incorporated much of Girard's draft text into the draft Ministerial Declaration[2], by reference in Annex B. Unlike in agriculture negotiations, Castillo did not attempt to offer many compromise positions. Castillo did, however incorporate several issues to reflect developing country concerns, including flexibility on sectoral negotiations. Members in Cancun will attempt adopt a "framework" for establishing the modalities in order to conclude modalities by early next year. Members will also try to take account of developing countries' needs while avoiding the creation of a two-track WTO process and a double standard in the world trading system.

[1] "Draft Elements of Modalities for Negotiations on Non-Agricultural Products" (TN/MA/W/35/Rev.1), dated August 19.

[2] JOB (03)/150/Rev.1, dated August 24, 2003.

Navigating the Singapore Issues: Rough Seas Ahead

The four "Singapore Issues," Investment, Competition Policy, Trade Facilitation and Transparency in Government Procurement, have until now been treated together at the insistence of the EU and Japan, the main demandeurs for negotiations on investment and competition. The EU and Japan have not wanted to separate investment and competition from the less controversial issues of trade facilitation and government procurement since this would probably doom any hope of a negotiation on investment and competition. At the Doha Ministerial, this insistence coupled with resistance to investment and competition by some developing countries, resulted in the four being bundled together.

Investment in particular is strongly opposed by some developing countries, notably by India, and certain African states, which have said that under no circumstances would they agree to launch negotiations on the subject in Cancun. The United States, while not a demandeur for either investment or competition, has until now given quiet support to the EU – as for example at the Doha Ministerial in 2001. The United States recently broke ranks, indicating that it does not wish to see negotiations on trade facilitation and government procurement held up by disagreements on the other two. One issue at Cancun will be whether to decouple the negotiations on the four issues.

The draft Ministerial text contains virtually identical language on each of the four issues, presenting two stark alternatives – to commence negotiations on the basis of "modalities" annexed to the Declaration, or to remit the subject to officials for further clarification. The draft modalities are in each case short: each stresses the need of developing countries for technical assistance and capacity building, and for flexibility in the application of any agreements to them. The draft on investment contains more details on the elements to be contained in an agreement.

It is believed by most Geneva delegates that there is little possibility of an agreement at Cancun to launch negotiations on investment. An agreement to launch negotiations on competition policy will also be difficult. Whether the Members let trade facilitation and procurement go forward at Cancun will depend on the tactics of the EU and Japan. If the EU and Japan continue to insist on keeping the four issues together, Members may have to relegate all four issues to further study, despite a considerable amount of preparatory work since 1996. In any case, navigation of the Singapore Issues will be difficult, and unpredictable as the weather patterns in Cancun during the current hurricane season.

Competing Proposals on Agriculture Have Transformed the Rural Landscape

WTO negotiations on "modalities" (approaches and targets) for agriculture reform have regained momentum in the final weeks before the Cancun Ministerial Meeting, but competing proposals from several major blocs of Members have complicated negotiations even further.

Since missing the March 2003 deadline, key WTO Members in the past month have tried to break the deadlock over Chairman Stuart Harbinson's draft modalities by submitting new proposals. The most significant ones are the joint US-EU proposal and a counter-proposal put forward by a group of twenty developing countries ("G-20"), led by Brazil, China and India. In

addition, the General Council Chairman, Carlos Perez del Castillo, released a revised ministerial declaration for the Cancun meeting that contains his own proposal on modalities for agriculture negotiations. The Chairman's text is intended as a compromise between the EU-US joint proposal and the G-20 counter-proposal. Reaction to this text has been mixed. In any event, it will serve as a basis for discussion at the Cancun.

The EU-US text has provoked a sudden and unexpected modification in the landscape of traditional alliances that play a role in agriculture negotiations. Key developing countries that belonged to different groupings such as the Cairns Group, the Like-minded countries and Net-food importer countries, have rallied together as a reaction against the conservative approach of the EU-US text. It is likely that the two driving forces at Cancun will be the US and EU, on the one hand, and the G-20, on the other side.

The present report highlights the recent events leading up to Cancun on agriculture and the key proposals in relation to the "three pillars" of the Agreement on Agriculture (market access, domestic support and export competition). In particular, the Chairman's draft text is contrasted with the EU-US and the G-20 texts.

It must be understood that the agriculture modalities are critically important. The negotiation on modalities includes, *inter alia*, agreements on phase-out or reduction formulas, implementation periods, and special and differential treatment for developing countries. An agreement on negotiating modalities will, to a considerable extent, decide the outcome of the negotiations.

Draft Ministerial Text Forwarded to Cancun: Surf's Up, or a Wipeout Ahead?

The World Trade Organization released on August 31, 2003 the text of a letter sent by the Chairman of the General Council, Ambassador Carlos Perez Del Castillo, and the Director General, Dr. Supachai, to the Foreign Minister of Mexico, Dr. Louis Derbez, who will Chair the Ministerial Conference of the WTO in Cancun on September 10-14. The purpose of the letter is to convey and comment on the "Draft Cancun Ministerial Text" issued on August 24, which will be the basis for the negotiations in Cancun and for the final declaration which will emerge from it.

The letter and the draft text are the product of intensive consultations among delegations that have taken place in Geneva throughout the month of August. The product of these negotiations demonstrate that time has not been wasted; one major issue has been resolved (*i.e*. TRIPS and Public Health) and the remaining problems facing Ministers at Cancun have been clarified, so that the danger of a manifest failure (or washout) at the Cancun Conference, which many feared, is now greatly reduced.

Nevertheless, it is also clear that all of the major elements of the Doha Development Agenda on which decisions will be required at Cancun remain unresolved, and that Ministers will face the greatest difficulty in reaching agreement on them in a five-day meeting. The outcome is unclear – perhaps the result will be neither success nor failure, but enough progress in some key areas to provide the basis for intensified negotiations in the next phase. This implies, in our view, that the official deadline of December 2004 for conclusion of this Round will become clearly unattainable (although Governments may find it impossible to say this explicitly at this stage). If

the 2004 deadline is missed, the most likely date for conclusion of the Round will be December 2006.

Averting an Unhealthy Outbreak at Cancun: WTO Members Conclude an Agreement on TRIPS and Public Health

On August 30, 2003, WTO Members reached agreement on an important and overdue Decision (original deadline was December 2002) setting out a system to assure the supply of cheaper drugs to least developed countries and other developing countries in situations of national health emergencies or extreme urgencies.

Since December 2002, the United States has been the lone holdout on reaching a final deal due to concerns of patent infringement arising from illegitimate use of compulsory licensing, among other reasons. Since WTO Members agreed to the Declaration on TRIPS and Public Health at the Doha Ministerial in 2001, they have sought to strike a balance between the interests of patent protection and the health needs of developing countries, especially in sub-Sahara Africa. Paragraph 6 of the Declaration required further guidance on implementation, in particular with respect to countries that have insufficient or no manufacturing capacity.

In addition to the latest Decision, Members agreed on a controversial General Council Chairman's Statement. The Statement contains several key shared understandings of Members regarding the Decision that was adopted and the way it will be interpreted and implemented. In particular, the Statement provides that Members will take "all reasonable measures" to prevent diversion of cheaper drugs produced under the new system, and sets forth some of the anti-diversion measures that are likely to be implemented.

Although the TRIPS and Public Health issue is not formally part of the Cancun agenda, a failure to conclude a deal prior to Cancun would have complicated negotiations on other issues.

UNITED STATES

Free Trade Agreements

Bush Administration Continues Push for Competitive Liberalization

The Bush Administration is forging ahead with its competitive liberalization strategy by negotiating Free Trade Agreements (FTAs) at the bilateral, regional and multilateral level. Since our last update, the following developments took place:

- President Bush signed the implementing bills for the FTAs with Singapore and Chile. The implementation of the FTAs will take effect starting January 1, 2004.

- The Administration continued negotiations with Morocco, Central America, the Southern African Customs Union (SACU), and Australia;

- The Administration formally notified Congress of its intention to initiate FTA negotiations with Bahrain and the Dominican Republic.

In this report, we highlight the different steps that the Administration had to take, under Trade Promotion Authority (TPA), for the negotiation of the Singapore and Chile FTAs, as well as for the ongoing and announced negotiations.

Panama Hopes U.S. Will Announce FTA Negotiations by the End of the Year; U.S.-Dominican Republic FTA Will Focus on Market Access Issues

On September 5, 2003, Panamanian Ambassador to the U.S. Roberto Alfaro Estripeaut stated at a meeting by the U.S. Chamber of Commerce that Panama hopes that the U.S. will formally announce the launch of negotiations on a U.S.-Panama FTA by the end of 2003.

At the same event, the Ambassador of the Dominican Republic to the U.S. Hugo Guiliani Cury indicated that the U.S. and the Dominican Republic will launch formal FTA negotiations in January 2004. The negotiations will focus on market access issues and will conclude by March or April 2004, after which the FTA will be integrated into CAFTA. The final agreement would then be submitted to Congress in late April or May 2004.

Senate Appropriations Bill Would Prohibit Negotiation of Trade Agreements with Temporary Entry Provisions

On September 4, 2003, the Senate Appropriations Committee unanimously approved the Commerce-Justice-State (CJS) Appropriations Bill (S.1585), which includes an amendment offered by Senator Dianne Feinstein (D-California) that would prohibit the Office of the US Trade Representative (USTR) from negotiating free trade agreements (FTAs) "contain[ing] provisions relating to the entry of foreign nationals into the United States."[3] Representative Steve King (R-Iowa) proposed a similar amendment (H.AMDT.290 to H.R.2799) in the House during consideration of the CJS Appropriations Bill in late July, however that amendment was withdrawn.

Some analysts worry that, if approved, the Feinstein amendment would set a precedent for Members of Congress to use restrictions on appropriations to "negotiate" FTAs. Members of Congress essentially could demand certain provisions are met by holding funds necessary to implement the agreement hostage to their individual concerns. These restrictions would hamper the ability of the USTR to negotiate.

ITC Report Concludes NAFTA and Other FTAs Contributed to U.S. Growth

The International Trade Commission (ITC) released a report in August 2003 entitled "The Impact of Trade Agreements on the U.S. Economy". The report concludes that trade agreements were only one of many factors that contributed to U.S. growth in the past twenty years. The five

[3] S. 1585, Title II, Section 214 (CJS Appropriations Bill)

trade agreements analyzed in the report, including NAFTA, have had a positive impact on the U.S. economy.

The report serves as a useful tool for Members of Congress to evaluate U.S. trade policy, especially given the TPA requirements for congressional consultations. The report provides further evidence that multilateral trade negotiations benefit the U.S. economy more than bilateral and regional negotiations.

The full report is available at www.usitc.gov.

Customs

FDA to Issue Final Rule on Registration of Food Facilities Under the Bioterrorism Act by October 2003

The U.S. Food and Drug Administration ("FDA") indicated recently that it intends to implement Section 305 of the Public Health Security and Bioterrorism Preparedness and Response Act of 2002 (hereinafter "Bioterrorism Act" or "Act") on schedule by October 10, 2003. Section 305 of the Act requires that domestic and foreign facilities that "manufacture, process, pack, or hold food for human or animal consumption" register with the FDA, and no later than December 12, 2003. Currently, the FDA is reviewing public comments on its proposed registration procedures, including on the Draft Food Facility Registration Form ("the Form") – the registration form that food facilities will be required to submit to the FDA.

Facilities that fail to register by December 12, 2003, can be subject to civil and criminal actions. For example, food from facilities that fail to register can be held at the port of entry. Moreover, if facilities and their agents provide false information, they can be subject to fines, imprisonment or both. The FDA estimates that about 400,000 domestic and foreign facilities must register by the deadline. Some U.S. trading partners, however, have argued that the process appears burdensome and might violate WTO disciplines on technical barriers.

Customs Publishes Final Rule of Definition of "Customs Business"

On August 11, 2003, the Bureau of Customs and Border Protection ("Customs") published its final rule amending Section 111.1 of the Customs Regulations as it pertains to the definition of "customs business." Section 111.1 implements Section 641 of the Tariff Act of 193, as amended, which provides that a person must hold a valid customs broker's license and permit in order to transact customs business on behalf of others.

The final rule becomes effective on September 10, 2003.

Customs Adopts Final Rule on Manufacturing Substitution Drawback; Updates List of International Organizations Eligible for Free Entry Privileges; Withdraws Proposal on Listing of Trademarks on Imported Merchandise

We want to alert you to the following customs developments:

- On August 22, 2003 the Bureau of Customs and Border Protection (CBP), Department of Homeland Security (DHS), adopted as a final rule an amendment on the Manufacturing Substitution Drawback: Duty Apportionment. The final rule is effective from August 22, 2003.

- On August 22, 2003 the CBP updated its list of international organizations eligible for visa-free entry. The final rule is effective from August 22, 2003.

- On August 22, 2003 the CBP published its decision to withdraw a proposed rule that would require importers to provide on their invoices a listing of all trademarks appearing on imported merchandise and its packaging. As of August 22, 2003, the proposed rule is withdrawn.

GSP

USTR Announces Review of 2001 and 2002 Country Practice Reviews; US Extends Duty-Free Treatment for Israeli Agricultural Products

On September 3, 2003, the Office of the United States Trade Representative (USTR) announced which of the 2001 and 2002 petitions it intends to review to determine whether applicant developing countries are in compliance with the eligibility criteria to receive benefits under the Generalized System of Preferences (GSP).

In a related event, President Bush on August 27, 2003 extended duty-free treatment for certain Israeli agricultural products to December 31, 2003. This duty-free treatment was previously scheduled to expire at the end of 2002.

US-EU

EU, US, and Acceding Countries to Agree on Amendments to the Acceding Countries-US Investment Treaties

At the beginning of September 2003 the European Commission authorized Commissioners Lamy and Verheugen to sign a Memorandum of Understanding (MOU) with the US and eight future Member States[4], which is expected to resolve the legal issues arising from the existing Bilateral Investment Treaties (BITs) between the US and those eight acceding countries. The EU has long warned that the BITs need to be amended or denounced, as some of their provisions are inconsistent with EU law. It now seems that the parties have reached a political agreement on most of the controversial issues. However, some matters, e.g. capital movements, still need to be negotiated. In addition to this, BITs that were concluded between the acceding countries and other countries such as Canada will also need to be revised.

US-LATIN AMERICA

[4] Bulgaria, Czech Republic, Estonia, Latvia, Lithuania, Poland, Romania and Slovakia.

Mexico and US Clash Over Trade Issues

US-Mexico trade disputes involving cement, oil tubing, steel sheeting, pork and high-fructose corn syrup (HFCS) and telecommunications have increased tension in the bilateral relationship.

On August 5, the Ministry of Economy filed formal panel requests at the World Trade Organization (WTO) protesting anti-dumping duties that the United States imposed on Mexican exports of cement, oil tubing and steel sheeting. The same day, the US Trade Representative (USTR) raised the possibility of raising a WTO complaint against Mexico for barriers to U.S. HFCS imports. Regarding the pork dispute, U.S. authorities believe that Mexico will delay until September the decision to accept or reject an antidumping petition filed by Mexican pork producers against U.S. imports, and will continue to monitor the situation closely. Moreover, a WTO panel will soon issue its findings in the U.S. complaint regarding access to Mexico's telecommunications market.

Meanwhile, Members of the U.S. Congress, including Senate Finance Committee Chairman Grassley (R-Iowa), have raised concerns in letters to both U.S. and Mexican officials criticizing Mexico's failure to implement its NAFTA commitments.

Colombia and Dominican Republic FTAs Could Add Momentum to FTAA Negotiations

On August 4, 2003 the United States Representative (USTR) sent a notice to the U.S. Congress announcing its intention to integrate the Dominican Republic into negotiations of the US-Central America Free Trade Agreement (US-CAFTA). Among the sectors that could benefit most from the US-CAFTA are: electrical power systems, refrigeration and telecommunications equipment.

On August 8, 2003, U.S. Trade Representative, Robert Zoellick met with the Colombian Minister of Trade Jorge H. Botero to discuss the possibility of negotiating an FTA. USTR sources reported that the Colombian Government is willing to eliminate all agricultural tariffs, which are a key concern of U.S. industries.

The Bush administration is using the bilaterals in the region to advance its "competitive liberalization" strategy, hoping that the bilaterals will provide momentum for the FTAA negotiations.

US-ASIA

Congress Takes Aim At Currency Manipulation; China Chief Target

Over the past ten days, three bills, H.R. 3058, S.1586, and S.1592, and one non-binding Senate resolution, S.Res 219, have been introduced in the US Congress to address alleged currency manipulation by the largest East Asian economies, notably China. While providing the President with a wide array of remedial action, all three bills contain language suggesting that "currency manipulation" has been an important factor in the loss of over 2.6 million American manufacturing jobs since early 2001. On a recent visit to Asia, Treasury Secretary Snow raised

the issue of exchange rates with officials in China, however he failed to win any promises on the floating of China's currency the renminbi (RMB).

The introduction of multiple bills signals growing concern among lawmakers about the link between China and the loss of manufacturing jobs in the US, particularly with elections just over a year away. Trade lobby groups have also been discussing possible action to confront China's undervalued currency, and momentum is building. However, some analysts have cautioned that a floating RMB would not automatically correct the US trade deficit with China; reported at US$11.3 billion for July 2003.

REPORTS IN DETAIL

SPECIAL REPORTS ON THE WTO CANCUN MINISTERIAL CONFERENCE

Special Report on WTO Cancun Ministerial Preparations, Number 6:

"WTO Talks Collapse in Cancun: A Splash of Cold Water, or Dead in the Water?"

SUMMARY

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ANALYSIS

I. Chairman Derbez Ends Talks Suddenly: Premature Decision, or a Good Call?

Mexico's foreign minister and Chair of the Ministerial Conference Luis Ernesto Derbez around 3pm on Sunday called an abrupt end to the Cancun talks, to the surprise of many including the EC, developing countries and ministers leading the five negotiating groups. Derbez was at the time chairing the "Green Room" meeting of about 30 countries, and discussion had dragged on beyond schedule over whether to launch negotiations on the Singapore issues. These issues were dealt with first on the agenda at the insistence of the EC, which did not expect negotiations to be so difficult (especially after the EC dropped its demands on investment and competition).

The negotiations collapsed even before ministers proceeded to discussion of agriculture – the most critical item on the agenda. Most delegations at that stage assumed negotiations would resume after the Green Room process, and would continue well into the night and into Monday. Until the release of the second draft Ministerial Declaration the day before[5] (Saturday afternoon around 1:30pm), many participants felt that serious negotiations had not yet taken place.

Some observers have commented that Derbez made a good call by ending negotiations before the situation became worse, especially due to the hardened positions of various country groupings like the ACP.

A. EC Concession: Not Too Little, But Too Late?

Derbez called for a short break at lunchtime, after some indication from EC Trade Commissioner Pascal Lamy that he might have additional flexibility on unbundling the four Singapore issues. Lamy then met briefly with Member States across the street in a 133 Committee, and returned to the Green Room to announce that the EC would be willing to remove investment and competition from the agenda – a major concession (despite resistance from France and Germany, and uncertainty over the lack of the 133 Committee's mandate on this

[5] JOB(03)/150/Rev. 2, dated 13 September 2003.

issue). Lamy interpreted the lack of explicit opposition from the 133 Committee as a mandate to move forward.

The EC's concession on investment and competition prompted a flurry of responses. Malaysia, a traditional opponent of the issues, made a tactical maneuver and suggested that it could agree to trade facilitation and competition (and not transparency in government procurement). Later, Malaysia took a harder line against negotiations on procurement. Sources indicate that India, Malaysia's ally on the Singapore issues, was ready to move forward on both trade facilitation and procurement, and was thrilled by the EC's sudden concession. Then Botswana, speaking on behalf of the ACP, said the group would reject all four issues including trade facilitation because "not enough was on the table." The Chair called for a short break, but positions did not change. In reaction, Korea, a traditional supporter of the EC on these issues, stated its continuing support for negotiations on all four issues. It is debatable, however, if Korea (and Japan) would have continued to stake out a hard line without the EC's backing.

B. ACP Rejects EC Concession; Cheers the Collapse of Talks

The ACP grouping[6], surprisingly, refused to accept the EC's concession and insisted that all four issues must be rejected – even the least controversial issue of trade facilitation. The strong stand by the ACP grouping prompted Chairman Derbez to call a sudden halt to talks and announce that a closing ceremony would follow. The announcement caught many by surprise, especially since a large majority of the WTO's Members were not present in the Green Room meeting. Upon this announcement, the ACP ministers in the Green Room started cheering the apparent collapse of talks. The Kenyan minister proceeded downstairs to the common area and made the announcement, to the surprise of many including other ministers. As a result, confusion ensued while anti-trade NGO groups began to celebrate loudly over the collapse of the talks. Within an hour, an announcement was posted that Derbez would convene a heads of delegation meeting (for all 148 Members), followed by the closing ceremony.

C. G-21+, EU and US React with Dismay

The G-21+ was the first group of countries to react, and held a press briefing by the ministers of Argentina, Brazil, Ecuador, Egypt and South Africa. The G-21+ countries, which had taken a hard line on negotiations much of the week, did not celebrate the collapse of talks, but emphasized that the group was a negotiating force that must be dealt with seriously.[7] The group insisted that WTO discussions must move forward in order to achieve agriculture reform. The underlying message was that the group should not be blamed for the collapse of negotiations,

[6] The African Caribbean Pacific ("ACP") grouping consists of over 70 countries that are a beneficiary of the European Union's preferential market-access programs, as originally provided by the Lome Convention and later renewed by the Contonou agreement.

[7] The G-21+, led by Brazil, China and India, also includes Argentina, Bolivia, Chile, Colombia, Costa Rica, Ecuador, El Salvador (later withdrew), Guatemala, Mexico, Pakistan, Paraguay, Peru, Philippines, South Africa, Thailand and Venezuela. At the start of the Cancun Ministerial, Egypt, Senegal and Turkey joined. Indonesia and Nigeria joined towards the close of Ministerial.

even though it made a strong stand on agriculture throughout the week (and month prior). Our sources among the G-21+ countries indicate that many of its members were upset at the ACP grouping in particular and believed that its members obstructed talks, starting at the heads of delegations meeting on Saturday evening. Many G-21+ countries felt that talks on agriculture were progressing constructively despite significant differences after the release of the second draft Ministerial text, and that intense negotiations could have produced a deal at Cancun.

USTR Zoellick and Agriculture Secretary Veneman were the next to hold a briefing, and expressed their frustration towards what they described as a lack of cooperation from certain Members. Zoellick stated bluntly that the "can do" was overwhelmed by the "won't do," but did not mention any countries in particular.[8] The US throughout the week directed its anger at Brazil, the leader of the G-21+ and argued that the group was basing its demands on rhetoric and was unwilling to engage in constructive talks. Zoellick stated repeatedly that the US would continue bilateral and regional trade initiatives with countries that were ready to negotiate (and implicitly, dismiss countries that are not).

EC Commissioner Lamy and Agriculture Commissioner Franz Fischler held the next briefing, and directed most of their criticism towards the WTO's "medieval structure." Lamy questioned the Chair's judgment to end the talks early, and suggested the need to review the organization's decision making. Fischler stated that the EC's concession on Singapore issues should have allowed for progress on agriculture, and also believed that negotiations had ended too abruptly.

D. Conspiracy Theory: Intentional Delay of Agriculture Liberalization?

Many participants including from the G-21+ countries and others privately expressed outrage at the Chair's decision to end talks early. Many participants had changed their travel plans to remain in Cancun until Tuesday, and expected talks to extend well past the scheduled deadline of Sunday at 6pm. Due to the sudden turn of events, some have suggested that the motives of the Chairman were driven by other factors, and possibly developed country efforts to thwart agricultural reform. Although their theories are not based on any apparent facts, speculation has persisted since the collapse of talks.

II. Singapore Issues: No Longer Two Problems, But the Major Stumbling Block

The four Singapore issues – Investment, Competition Policy, Trade Facilitation and Transparency in Government Procurement – proved to be the stumbling blocks that caused the collapse of talks at Cancun. Canada's trade minister Pierre Pettigrew facilitated the discussions on the Singapore issues at Cancun and proposed a compromise that would have allowed the two less controversial issues to proceed, along with eventual negotiations on investment, but not competition.

[8] At an address in Washington shortly after the Cancun Ministerial, Zoellick stated that talks broke down after African and Caribbean countries walked out on efforts to launch negotiations on trade facilitation – which he described as a necessary modernization of agreements to facilitate customs and other procedures reached back in 1947 with the creation of the GATT.

The EU and Japan have been the main *demandeurs* for negotiations on investment and competition since discussion on these issues was launched at the Singapore Ministerial in 1996. The two less controversial issues of trade facilitation and transparency in government procurement had been ready for negotiations since the Seattle Ministerial in 1999 (where talks also collapsed), and were delayed again at the Doha Ministerial in 2001 when the EC and Japan insisted on bundling the four (presumably to gain leverage in order to resist reform of their agricultural regimes). Investment in particular provoked the most criticism from other WTO Members, and especially developing countries.

A. Draft Proposes Eventual Negotiations on Investment, Not Competition

The second draft Ministerial Declaration released on September 13 favored the EC/Japan position on investment. The text stated that "modalities that will allow negotiations on a multilateral investment framework to start shall be adopted"[9] no later than the decisions on modalities for agriculture and industrial/NAMA negotiations.[10] The draft, however, relegated competition policy to further study.[11]

The language of the second draft also left vague the completion date for investment negotiations and did not specify whether negotiations should be part of the single undertaking of the current Round, or should be completed at a later date.

Several developing country Members, chiefly India and Malaysia, criticized the language on investment as going too far, and not representing the sentiment of most Members. The US had also warned previously that the EC/Japan demands on these two issues did not reflect reality.

B. Draft Proposes Launch of Trade Facilitation and Transparency Negotiations

The second draft proposed that negotiations move forward on transparency in government procurement and trade facilitation.[12] Unlike the language on investment, the draft made explicit references to the Doha mandate for these two issues and stated that negotiations should conclude as part of the Round. These two issues have been far less controversial than investment and competition, and most Members were ready to proceed with negotiations.

The ACP and other groupings also criticized the Singapore issues, but their opposition to all four issues was not evident prior to Cancun. It appears that the poorly worded draft on the cotton initiative (discussed below) provoked their anger – especially since the EC and Japan gained a major concession on investment. Some participants, including among the G-21+ countries, noted that the ACP opposition to trade facilitation in particular is baffling, and not

[9] JOB(03)/150/Rev. 2, at paragraph 14.

[10] JOB(03)/150/Rev. 2, at footnote 1.

[11] JOB(03)/150/Rev. 2, at paragraph 15.

[12] JOB(03)/150/Rev. 2, at paragraphs 16-17.

representative of their interests (*e.g.*, trade facilitation would provide more technical assistance to the lesser developing countries than any others, and they would have been granted longer implementation periods).

The failure to launch modalities on all four Singapore issues does not mean that they have been removed from the current Round. WTO Members can make decisions on any or all these issues in a General Council meeting in Geneva, or at the next Ministerial (to be hosted by Hong Kong, China at the end of 2004, or later.) The issues of investment and competition, however, are probably off the agenda as the EC has withdrawn its support and will find it hard to insist on them again.

III. Cotton Subsidies Initiative: An Emotional Debate Spirals Out of Control

Prior to Cancun, four West African producers of cotton – Burkina Faso, Benin, Chad and Mali, had pleaded for the consideration of a sectoral initiative to reduce and eliminate cotton subsidies. The first draft Ministerial text reflected this concern with some general language on cotton issues. The initiative by itself was outside the context of agriculture negotiations and therefore perhaps unrealistic, but nevertheless drew attention to the plight of some of the WTO's poorest Members. The US, EU and China are heavy subsidizers of cotton, with the U.S. paying cotton growers an estimated $2.5 to $3 billion a year and the EU an estimated $700 million.[13]

The cotton initiative was placed on the Cancun agenda at the urging of the four West African countries. The US previously had resisted inclusion of the cotton initiative in the draft Ministerial Declaration, arguing that the Doha agenda did not make specific mention of it, and that the initiative would be more appropriate to address as part of agricultural negotiations.

The second Ministerial draft reflects much of the language of the U.S. proposal. The text suggested that cotton was part of a more complex range of issues and that several WTO bodies should "address the impact of distortions that exist in the trade of cotton, man-made fibres, textiles and clothing to ensure comprehensive consideration of the entirety of the sector.[14] The text's most inflammatory language suggested that international bodies "direct existing programmes and resources toward diversification of the economies where cotton accounts for the major share of their GDP."[15] African countries perceived the message as saying they should stop growing cotton.

The angered West African countries, prodded by anti-trade NGOs, sought support for their initiative from the ACP countries. Afterwards, the enlarged group demanded an end to all export subsidies in three years, the end to production subsidies in four years starting in 2005, and in the interim period, payments of up to $300 million a year to African countries affected by subsidies. Some Members like the EU provided an initial response, pledging to reduce subsidies.

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[13] Figures cited by the Wall Street Journal, "Trade Talks Fail Amid Big Divide Over Farm Issues", 15 September 2003 and the Financial Times, "Talks Unravel Over Cotton," 16 September 2003.

[14] JOB(03)/150/Rev. 2, at paragraph 27.

[15] *Id.*

Others saw the demands for compensation as extortion, and coming from countries where transparency was lacking. But, the situation appeared to have spiraled out of control and turned into an emotional debate.

At the "heads of delegations" meeting on Saturday evening (among all 148 WTO Members), African and Caribbean countries one after another made statements emphasizing political and development issues, rather than practical approaches to their trade concerns. Canada's minister Pierre Pettigrew commented that, "I felt like I was at a U.N. parliamentary session." It appears that many of these statements were drafted after consultation with NGO advisors who were keen for the WTO talks to fail. Sources report that these countries' positions hardened after they left the room, presumably to consult with NGO advisors.

IV. Emergence of the "G-21+" Complicates Agriculture and Other Negotiations

In the month leading up to the Cancun Ministerial, the traditional alliances of agricultural producers were transformed in reaction to the US-EU proposal of August 13, and the counterproposal from developing countries later known as the G-21+ countries, dated August 20. The traditional alliance of agricultural exporters, the Cairns Group (including developing and developed countries), found that its influence was greatly diminished in the run-up to Cancun.

A. Emergence of G-21+ Polarized Negotiations at Cancun

The emergence of the G-21+ group complicated negotiations at Cancun by polarizing the debate into a North-South struggle, led by Brazil. The US, EU and other countries directed strong criticism towards the G-21+ countries throughout the week, asserting that Brazil and other countries made demands based on rhetoric and were not willing to negotiate constructively. Reports abounded at Cancun that the US and EU were attempting to weaken the group since some in the group were more protectionist or liberal than others. The group, however, did not weaken at Cancun and instead presented an unexpected show of force – which complicated the prospects for serious negotiations at Cancun (thereby encouraging the ACP to demonstrate similar resistance towards developed countries).

B. Draft on Agriculture Favors US-EU; Criticized by G-21+

The facilitator for agriculture negotiations at Cancun, minister George Yeo of Singapore, presented in Annex A of the draft Ministerial text, a compromise text which seemed to favor more the US-EU positions than some of the G-21+ positions.[16] For example, Annex A contained few specific targets but proposed some caps for reductions of domestic support and export subsidies, and proposed the extension of the "peace clause" – the moratorium on disputes applicable to certain subsidy programs set to expire at the end of 2003. The target for reducing

[16] Senator Charles Grassley, Chairman of the Senate Finance Committee issued a statement on September 14, indicating that although the US would have preferred more ambitious reform, he believed the administration was prepared to accept the agricultural reforms proposed in Annex A as a "constructive text" in which to move forward.

"blue box" subsidies was up to 5 percent of total agricultural production in 2000-2002, which would have allowed the US to maintain the level of subsidies provided by the Farm Bill, but too low for the EU to avoid changes to its subsidy regime.[17]

Some G-21+ members including Brazil and India criticized several elements of the draft, but did not dismiss it as a basis for reaching a deal. The group gathered on Saturday the 13th to draft a paper proposing significant revisions to the text in Annex A. Among their major objectives, they sought: (i) further reduction of "blue box" domestic support from the proposed 5 percent to 2.5 percent; (ii) reduction of export subsidies by including export credit programs in the proposed reductions; and (iii) elimination of the extension of the peace clause.

Several G-21+ country participants informed us that the group believed a deal was within reach despite the significant gaps on agriculture. The group had intended to engage in serious negotiations in the Green Room meeting on Sunday, and beyond if necessary. These participants were greatly disappointed by the collapse of talks in the Green Room, and even before discussion on agriculture took place. We understand that the facilitator for agriculture suggested before the abrupt end of the Ministerial that the Chair declare a recess in order to proceed on discussion of agriculture (since Members went well beyond the time scheduled on Singapore issues). In any event, the opportunity to move agriculture negotiations forward at Cancun was lost. With the upcoming expiration of the "peace clause" next year – the provision in the Agriculture Agreement that exempts many subsidy programs from dispute settlement – a proliferation of disputes will probably result.

V. No More Fun in the Cancun Sun – A Long Cold Spell Ahead?

Developing countries as a whole can claim some degree of success at their growing prominence in the global trading system. Major trading powers must take groups like the G-21+ and ACP seriously; otherwise, decisions at the WTO in Cancun and elsewhere cannot be made. But, the question now arises on whether the WTO will be considered the most effective forum to achieve meaningful trade liberalization. Many signs indicate that serious WTO negotiations will be on hold for some time ahead. The sunny window of opportunity in Cancun was ideal for a deal, but that window is closing fast with the coming cold spell. If so, the touted victory at Cancun will be bittersweet as less developed countries become increasingly marginalized by the lack of trade liberalization.

For major players like the US and EU, WTO negotiations would require making major concessions on agricultural reform and other sensitive areas. In the US, protectionism is growing due to increasing competition from imports and the lack of major economic recovery. Political sensitivities attributed to the economy and trade policy will be heightened in a presidential election year. The EU, which would be forced to make the deepest concessions in WTO talks, will also experience a turnover in leadership next year. Moreover, the EU will expand by ten new members and thereby come under enormous pressure to reallocate existing subsidies to the new Member States, rather than to cut subsidies overall. The possible change in trade

[17] The EU's proposed reforms to the Common Agricultural Policy ("CAP") would have shifted subsidies from the more distorting amber box programs to the less distortive "blue box" programs. The proposed cap of even 5 percent of production could have posed a serious problem to the EU.

representatives in both the US and EU might also diminish US-EU leadership at the WTO. USTR Zoellick and Commissioner Lamy have managed to cooperate in difficult situations, including the deals reached on the bilateral bananas dispute, the launch of the Round at Doha, and a compromise text on agriculture. It is uncertain whether US-EU cooperation in the WTO will continue at this ambitious level.

After the collapse, WTO Members agreed in Cancun to convene a Senior Officials level meeting in Geneva no later than December 15, 2003. Members will attempt in Geneva to revive negotiations. It is uncertain, however, whether Members can achieve real progress on the Round. In past experiences, meetings of Senior Officials (usually deputy ministers) have rarely moved significant decisions forward, such as the ones required to revive the Round.

There is also much talk that the WTO as an institution has become unmanageable due to its consensus-based system that provides the smallest Member the same rights as larger trading powers. Unlike in the IMF and other multilateral institutions, there is no weighted voting. Although the WTO process if more democratic, it is prone to abuse, as was the case in Cancun.

OUTLOOK

The collapse of WTO talks at Cancun was an unfortunate setback that could have been averted. Warning signs abounded, including the growing frustration of the West African countries (and later the ACP group) towards the lack of a considered response on the cotton initiative. Although a US proposal prompted the hard-line response on the cotton initiative, the EC as the main granter of preferences to the ACP should have detected their frustration. None of the leaders of the Ministerial stepped in to defuse the volatile situation and the ACP's anger made them susceptible to exploitation by anti-trade NGOs, leading the ACP to reject all of the Singapore issues. At least, the anti-trade NGOs can call their efforts a "success" and are emboldened by the failure of talks.

The EC and the *demandeurs* of investment and competition probably made a tactical error on the Singapore issues by holding on to these bargaining chips for far too long. Even more sympathetic Members like the US criticized the EC and its supporters for not recognizing the political reality, *i.e.*, the overwhelming resistance towards launching negotiations on these two issues. Although the EC came around on the last day and dropped its demands on these two issues, it was too late given the hardened position by the ACP group against all Singapore issues.

The emergence of the G-21+ also complicated negotiations at Cancun by polarizing the North-South debate on the most sensitive issue in the Round – agriculture – and perhaps undermined overall negotiations. The collapse of talks at Cancun was indeed a "splash of cold water" and acknowledgment of the strength of developing countries in the global trade negotiations system. These complex new dynamics make the deadline of December 2004 more unattainable than ever.

More worrisome, the collapse at Cancun has sent the WTO into "intensive care" (as described by the EC's Lamy), a condition that might persist for quite some time. In the wake of the collapse, the US and other countries that are eager to open markets will engage more

intensively in bilateral and regional trade initiatives.[18] Unfortunately, the poorest countries will have much to lose as a result of the global trading system's critical state.

[18] USTR Zoellick in a speech after Cancun stated that many ministers approached him after the collapse to consider bilateral free trade agreements, and indicated that the US is open to any countries that are serious about trade liberalization.

Special Report on WTO Cancun Ministerial Preparations, Number 5:

"Industrial Market Access Negotiations: Developing a Double Standard?"

SUMMARY

Negotiating modalities on non-agricultural market access ("NAMA" or industrial goods), is one of the critical areas of the Doha Development Agenda where WTO Members have not yet reached agreement (initial deadline of May 2003). On August 22, 2003, Members failed to endorse a draft text prepared by the Chair of the Negotiating Group on NAMA, Ambassador Pierre Louis Girard that intended to set out a framework for reaching a future agreement on modalities for market access talks.

The major differences among Members exist in the following areas:

- ***Nature of tariff cutting formula***: Developed countries seek a higher level of ambition in tariff reduction, while developing countries propose relatively moderate cuts, especially in regard to their own tariffs. Developing countries would be subject to much deeper tariff reductions in this Round since developed countries' tariffs are mostly at a low level.

- ***Sectoral tariff elimination/harmonization***: Ambassador Girard's draft text on modalities[19] proposes duty reduction on seven product groups of export interest to developing countries Developed countries seek participation in the sectoral initiatives by all Members. Developing countries however, argue that they should participate on a voluntary basis.

General Council Chairman Carlos Perez del Castillo has incorporated much of Girard's draft text into the draft Ministerial Declaration[20], by reference in Annex B. Unlike in agriculture negotiations, Castillo did not attempt to offer many compromise positions. Castillo did, however incorporate several issues to reflect developing country concerns, including flexibility on sectoral negotiations. Members in Cancun will attempt adopt a "framework" for establishing the modalities in order to conclude modalities by early next year. Members will also try to take account of developing countries' needs while avoiding the creation of a two-track WTO process and a double standard in the world trading system.

ANALYSIS

I. Background

[19] "Draft Elements of Modalities for Negotiations on Non-Agricultural Products" (TN/MA/W/35/Rev.1), dated August 19.

[20] JOB (03)/150/Rev.1, dated August 24, 2003.

As provided in the Doha Ministerial Declaration, WTO Members agreed in November 2001, to launch negotiations on industrial market access that would aim, by modalities to be agreed, for a reduction or elimination, as appropriate, of tariff peaks, high tariffs and tariff escalation as well as non-tariff barriers, particularly for products of export interest to developing country. Members also agreed upon the following provisions:

- Comprehensive product coverage without *a priori* exclusions; and
- Special and differential treatment for developing and least developed countries, including through "less than full reciprocity" in reduction commitments.

WTO members were originally scheduled to reach a deal on modalities[21] for the non-agriculture talks by May 31, 2003 but failed to do so because of diverging positions. Members then agreed to try to secure an agreement on modalities at the Cancun Ministerial. The Chair of the negotiating group on NAMA, Ambassador Pierre-Louis Girard, issued towards that end a first and a revised version (TN/MA/W/35/Rev.1) of the "Draft Elements of Modalities for Negotiations on Non-Agricultural Products" in May and August 2003, respectively. Girard's draft texts presented a variety of tariff reduction formulas, seven sectors for expedited tariff elimination and other guidelines.

Members, however, were unable to reach agreement on the text in late August, and aim to do so at Cancun. Girard circulated on August 21 a draft framework for establishing modalities to be appended to the Cancun Ministerial text. The framework for establishing modalities that appears as "Annex B" in the Draft Cancun Ministerial Declaration issued on August 24, is closely based on Girard's August 21 draft framework and proposes that Girard's August 19 draft modalities text be used as a reference for future work. In Annex B, General Council Chairman Carlos Perez del Castillo did not attempt to offer many compromise positions, unlike his approach towards agriculture. He did however, factor the views of developing countries' into several areas, including sectoral tariff initiatives.

At a General Council meeting on August 25-26, the framework was received with criticism, with Members still unable to settle their differences on certain key issues. Discussion of these contentious issues will now be taken up at Cancun.

II. Girard Draft Texts on Modalities: Criticized, But a Basis for Compromise

Ambassador Girard's first draft text[22] on modalities issued in May proposed that Members adopt a single, non-linear formula for a line-by-line reduction in tariffs on industrial products. The formula uses a country's average base rate and the base rate of the product in question so as to impose bigger cuts in tariffs for goods where the tariff is above the average rate

[21] The modalities are intended to set out broad outlines for final commitments in the negotiations, such as the formula to be used for reducing tariffs and the extent to which tariffs should be cut. Modalities lay out the goals for the talks and procedures how to achieve them.

[22] TN/MA/W/35.

and lower cuts in tariffs falling below the average. The EU and US however, criticized the formula, arguing that it would reward those countries (mainly developing) that have higher rates and could result in some countries being allowed to maintain bound rates above current applied rates.

In response, Girard suggested as "possible options"[23], adjustments to certain parameters of the formula. He suggested for instance, capping the average base rate, or parameter "ta", at a certain level to be determined by the participants. Additionally, the calculation of "ta" could be disassociated from the calculation of the base rates. For example, one could consider calculating "ta" using a 50/50 weighting of the average of all bound rates (after full implementation of current concessions) and the average of all applied rates. The base rates ("to") used in the formula would remain unchanged.

Girard's revised version of his modalities draft, entitled "Draft Elements of Modalities" (TN/MA/W/35/Rev.1), dated August 19, sets out additional flexibilities in the application of the proposed tariff-reduction formula but does not incorporate the "possible options" outlined in JOB(03)/155. The framework paper in Annex B excludes details on the tariff reduction formula as provided in Girard's August 19 modalities text. Paragraph 2 of the framework paper, however proposes that Girard's modalities text be used as a reference for future work.

III. Chairman Castillo's Framework for Establishing Modalities ("Annex B"): Incorporates Girard's Texts; Some Additional Compromises

The "Draft Cancun Ministerial Text" circulated on August 24 by Ambassador Carlos Perez del Castillo, the Chairman of the WTO's General Council, contains the draft "framework" – known as "Annex B" for the negotiations on tariffs and non-tariff barriers, on the basis of which detailed modalities will be established. The framework for the non-agricultural talks was last considered at the General Council meeting on August 25-26 where disagreement among Members ensued due to differences particularly on the tariff reduction formula to be adopted and the extent of sectoral tariff elimination. Ambassador Castillo indicated that ambiguities in the framework were intentional, describing the text as having the "constructive ambiguity" of not prejudging issues on which Members have differences and leaving those issues open for negotiation.

Despite opposition from developing countries to the harmonization approach, which would impose bigger cuts on higher tariffs, the Annex B framework retains the language provided in Ambassador Girard's August 19 draft, proposing the use of a non-linear formula applied on a line-by-line basis *(See table on page 8).* Developing countries generally have higher applied and bound tariffs on manufactured imports than their developed country counterparts.

The US and the EC on the other hand, consider Annex B as lacking in ambition and clarity with regard to a definition of the tariff-reduction formula. The EC and the US have expressed their disappointment at what they consider a low level of ambition reflected in the

[23] JOB(03)/155.

draft framework. The framework paper does not, for example, contain any figures outlining the level of ambition for tariff cuts. It also does not mention the "single co-efficient" as proposed in the US-EC-Canada proposal of August 11 *(See table on page 8).*

Members also stand divided on the proposal that reductions on tariffs not subject to WTO bindings should use as the starting point the applied rate multiplied by two. The proposed starting point appears within brackets, indicating that Members will decide upon the final figure at Cancun.

We provide below an overview of the key elements of the framework in Annex B:

A. Parameters for Negotiations: The Basics

The framework in Annex B instructs the Negotiating Group to continue its work on a non-linear formula applied on a line-by-line basis. Additionally, the Annex B framework lists the following provisions:

- ***Product coverage*** – Coverage shall be comprehensive without *a priori* exclusions;

- ***Base rates*** – Tariff reductions or elimination shall commence from the bound rates after full implementation of current concessions; however, for unbound tariff lines, the basis for commencing the tariff concessions shall be [two] times the MFN applied rate in the base year.

- ***Base year*** – The base year for MFN applied tariff rates shall be 2001 (applicable rates on 14 November; date of Doha Ministerial).

- ***Ad valorem basis*** – All non *ad-valorem* duties shall be converted to *ad valorem* equivalents on the basis of a methodology to be determined and bound in *ad valorem* terms.

- ***Reference period*** – The reference period for import data shall be 1999-2001.

- ***HS 96 and 2002 standards*** – Negotiations shall commence on the basis of the HS96 or HS2002 nomenclature, with the results of the negotiations to be finalized in the HS2002 nomenclature

- ***Autonomous liberalization*** – Credit shall be given for autonomous liberalization provided that the tariff rates were bound on an MFN basis in the WTO since the conclusion of the Uruguay Round.

B. Special and Differential Treatment: Avoiding a Double Standard

The Annex B framework paper proposes that the tariff reduction formula take fully into account the special needs and interests of developing and least-developed countries, including through "less than full reciprocity in reduction commitments" as stated in the Doha Declaration.

The paper submitted jointly on August 11 by the EU, US and Canada proposes in contrast, that "less than full reciprocity" would be extended to developing countries through a system of credits, which would be accorded on the basis of certain stipulated eligibility criteria *(See table)*. Neither the Annex B framework nor Ambassador Girard's August 19 framework draft makes reference to any such eligibility criteria.

Several developing countries have opposed the idea that flexibility under this provision be made conditional on the system of credits proposed by the three Quad countries. The US-EU-Canada paper proposes that in addition to the system of credits, Members could agree to other elements of flexibility for developing countries such as longer staging of reduction commitments, less than formula cuts for a limited number of tariff lines not concentrated in any one sector but subject to a minimum required cut. Although the US-EC and Canada are receptive to allowing flexibility for developing countries, they insist that developing countries must commit to meaningful liberalization in this Round, so as not to create a two-track WTO process.[24]

C. Sectoral Tariff Reductions: Elimination, Harmonization or Both

The Annex B framework paper calls for discussions on a sectoral tariff component aiming at elimination or harmonization of tariffs, particularly on products of export interest to developing countries. It proposes participation by all Members. Notably, Ambassador Girard's August 19 framework provides for the more ambitious objective of sectoral tariff "elimination" in contrast to the "elimination or harmonization" wording in the Annex B framework. The adjustment in language evident in Annex B resulted due to resistance by developing countries that have argued that sectoral tariff elimination should apply to them on a voluntary, rather than mandatory basis.

In a letter[25] to Ambassador Girard circulated on September 1, a group of 15 Latin American countries[26] expressed their preference for a voluntary sectoral approach, arguing that the proposed tariff elimination would imply going beyond the tariff reduction resulting from the application of the formula. Moreover, it would be difficult to find sectors that are of interest to all developing countries (*e.g.* beyond the initial seven categories identified). They also argued that negotiations on product coverage could also delay the talks beyond the time limits set in the negotiating mandate.

Annex B does not specify the products that would be subject to elimination or harmonization. However, Ambassador Girard's August 19 draft modalities, proposes an initial seven product groups (*i.e.*, electronics and electrical goods; fish and fish products; footwear; leather goods; motor vehicle parts and components; stones, gems and precious metals; and

[24] The United States has cited, for example, that about 70 percent of the tariffs paid by developing countries are to each other.

[25] TN/M/W/45.

[26] Argentina, Bolivia, Brazil, Chile, Colombia, Costa Rica, Ecuador, El Salvador, Guatemala, Mexico, Panama, Paraguay, Peru, Uruguay and Venezuela.

textiles and clothing) for zero duties. Although Girard's product grouping does not find mention in Annex B, it is probable that these groupings are used as a reference for the future work of the Negotiating group.

Girard's draft mentions that Members will need to determine the product coverage applicable to these sectors. The draft sets out the implementation of the sectoral tariff elimination in three phases of equal length. The basis of elimination will be from the bound rates after full implementation of current concessions or for unbound items, the MFN applied rates in 2001. The tariff reductions will occur in equal annual stages, as follows:

- Developed participants and other participants who so decide, shall eliminate tariffs at the end of the first phase;

- Other participants shall achieve tariff reduction and elimination as follows:

  -- Tariff reduction to a proposed level of not more than 10 percent[27] at the end of the first phase;

  -- Maintain this level during the second phase; and

  -- Achieve elimination of tariffs at the end of the third phase.

Some other concerns have arisen with regard to the sectoral component. Neither the Annex nor Girard's draft mentions environmental goods as one of the product grouping eligible for sectoral tariff elimination, as proposed in the US-EC-Canada paper. The EC has expressed its disappointment in this regard. In addition, Japan is seeking the removal of leather and fish and fish products from the sectoral elimination initiative.

It is noteworthy that Annex B does not propose that the sectoral elimination initiative be an "integral part" of a future modalities deal, as set forth in Girard's August 19 framework as well as the US-EC-Canada paper. Developing countries (*e.g.*, Brazil and Mexico, in particular) have resisted the inclusion of this language in the framework paper.

D. Binding Coverage: Extent of Binding To Be Decided

The Annex B framework exempts Members with a binding coverage of industrial tariff lines of less than [35] percent from making tariff reductions through the formula. Instead, these countries would be expected to bind [100] percent of industrial tariff lines at an average level that does not exceed the overall average of bound tariffs for all developing countries after full implementation of current concessions. Members will decide upon the bracketed figures at Cancun.

[27] If the rate (bound or in the case of unbound items. The MFN applied rate in 2001) is less than 10 percent, this lower rate shall remain in place.

E. Other Provisions for Developing and Least Developed Countries: Long Implementation Periods and Unbound Tariffs

Annex B grants developing countries the following additional flexibilities:

- Longer implementation periods for tariff reductions; and
- Tariff lines will not be subject to binding or formula cuts, for up to [5] percent of tariff lines provided they do not exceed [5] percent of the total value of a Member's imports.

Least-developed countries (LDCs), while exempt from the application of the formula and participation in the sectorial approach, will be expected to increase substantially their level of binding commitments. Many LDCs did not bind a substantial part of their tariff schedules during the Uruguay Round.

Developed countries are called upon to grant autonomous duty-free and quota-free access for industrial products originating from LDCs by a date to be decided upon.

F. Newly Acceded Members: Possible Extension of Implementation Periods

Annex B grants newly acceded Members such as China recourse to special provisions for tariff reductions so as to account for market access commitments undertaken as part of their accession and on-going implementation of staged tariff reductions. China was one of the *demandeurs* for more lenient commitments for new Members, given the significant commitments China and others had undertaken as part of their accession.

A group of Latin American countries however, have taken issue with what they consider as inequity in the treatment proposed for different developing countries[28]. They point out that Girard's draft allows certain newly acceded Members differentiated coefficients for applying the tariff reduction formula while providing certain developing countries with the possibility of protecting their sensitive sectors by keeping up to 5 percent of their tariff lines unbound. They also assert that developing countries that are not recent Members and have bound 100 per cent of their tariffs do not have recourse to similar flexibility.

G. Supplementary Modalities: Additional Approaches Considered

Annex B keeps open the possibility of supplementary modalities such as zero-for-zero sector elimination; sectorial harmonization; and the request & offer approach. Annex B also calls for participants to consider the elimination of low duties (pending agreement on the "core" modalities).

H. Non-Tariff Barriers: Intensive Work to Begin this Autumn

[28] TN/MA/W/45

Under Annex B, non-tariff barriers ("NTBs") – which have not received much attention in the Round this far, are set out as an integral part of the negotiations. Members are encouraged to submit notifications on NTBs by 31 October 2003 and to proceed with identification, examination, categorization and ultimately negotiations on reducing NTBs. Modalities for addressing NTBs could include the request/offer approach, horizontal or vertical approaches and should account for special and differential treatment for developing countries.

I. Deadlines: No Target Dates

Annex B is already a less ambitious effort to establish a "framework" for negotiations, and does not attempt to set a deadline for an agreement on the modalities (the last deadline was May 2003). Ambassador Girard's August 19 framework text had suggested that WTO members fix January 31, 2004 as the next deadline for an agreement on the modalities. The deadline was removed due to resistance from a number of exporting countries such as Brazil, which opposed setting a deadline on the grounds that progress in the non-agricultural talks would depend on developments in the agriculture negotiations.

J. Other Issues to Consider: Preference Erosion, Capacity Building, Etc.

Annex B lists other issues for further consideration as including non-reciprocal preference erosion, high tariff revenue dependency, among others. The issue of preference erosion is of particular concern to developing countries who benefit greatly from developed countries' preference programs such as GSP, the ACP and others. The framework also states that appropriate studies and capacity building measures shall be an integral part of the modalities.

OUTLOOK

At Cancun, Ministers will take up the most contentious elements of the Annex B framework as contained in the Draft Ministerial Declaration. These issues include, *inter alia*, whether to adopt the tariff reduction formulas set out in Girard's draft texts, the level of participation in sectoral tariff reduction initiatives, among other issues. An agreement on the framework, and eventually on modalities sometime next year would be the pre-requisite to the next stage of substantive and binding negotiations. Progress in the NAMA negotiations at Cancun and beyond, as several Members have pointed out – will hinge upon developments in other areas of the Doha mandate and in particular, on the negotiations on agriculture.

Similar to agriculture negotiations, WTO Members are aiming for the less ambitious objective of concluding a "framework" in which to expedite agreement on negotiating modalities. Likewise, industrial market access negotiations are difficult, but more so for developing countries – many of which did not make substantial reduction commitments during the Uruguay Round. In fact, many have not bound most of their tariff schedules. At the Doha Ministerial, these countries insisted on inserting language on "less than full reciprocity", which should translate to some degree of additional flexibility. Developed countries, however, fear that developing countries are unwilling to agree to ambitious liberalization and risk creating a two-track WTO process whereby developing countries would retain many of their barriers. They assert that such a double standard, ironically, would be to the detriment of developing countries first and foremost.

ANNEX: NEGOTIATIONS ON NON-AGRICULTRUAL MARKET ACCESS

ISSUE	CHAIRMAN CASTILLO, DRAFT CANCUN MINISTERIAL DECLARTATION, ANNEX B *JOB(03)/150/Rev.1, August 24, 2003*	CHAIRMAN GIRARD's FRAMEWORK TEXT, *August 19, 2003*	JOINT PROPOSAL BY CANADA, EC AND US *August 11, 2003*
General Statements	We take note of the constructive dialogue on the Chair's Draft Elements of Modalities (TN/MA/W/35/Rev.1) and confirm our intention to use this document as a reference for future work of the Negotiating Group.	We also take note of the draft elements of modalities (TN/MA/W/35/Rev.1) and confirm out intention to use these draft elements as a basis for our work towards agreement on modalities.	
Tariff Reduction Formulas	The Negotiating Group should continue its work on a non-linear formula applied on a line-by-line basis, which shall take fully into account the special needs and interests of developing and least-developed country participants, including through less than full reciprocity in reduction commitments.	The Negotiating Group should continue its work on a single, non-linear formula applied on a line-by-line basis, which must adequately acknowledge the situation of developing countries and address the reduction or elimination of tariff peaks, high tariffs, and tariff escalation. We reaffirm the importance of special and differential treatment and "less than full reciprocity in reduction commitments" as an integral part of these negotiations, and in particular the special provisions for least-developed participants.	We agree that modalities should be finalized by [dd mm yyyy] and shall include a simple, ambitious, harmonizing formula applied on a line-by-line basis (e.g. Swiss Formula), with a single co-efficient [x]. The formula will incorporate special and differential treatment. Special and differential treatment could for example, be based on a system of credits to accommodate objective differences in the economic situation of these countries. i. Less than full reciprocity by developing countries will be achieved by reducing the formula cut applicable to their tariffs by a factor of [X] on the basis of credits. Credits could be given for instance for: -- bindings greater than 95%, which will reduce the overall obligation to reduce by y%; and -- narrowing the margins between bound and applied tariff levels. ii. In addition to this system of credits, members could agree to other elements of flexibility for developing countries:

			-- less than formula cuts for a limited number of tariff lines/value of trade, not to be concentrated in an one sector but subject to a minimum required cut [x%]; -- level at which unbound tariffs are bound (e.g. X times applied); and -- longer staging of reduction commitments
Sectoral Tariff Elimination	We recognize that a sectorial tariff component aiming at elimination or harmonization is another key element to achieving the objectives of paragraph 16 of the Doha Ministerial Declaration with regard to the reduction or elimination of tariffs, in particular of export interest to developing countries. We recognize that participation by all participants will be important to that effect. We therefore encourage the Negotiating group to pursue its discussions on such a component, which includes adequate provisions of flexibility for developing-country participants.	The Negotiating Group is encouraged to pursue its discussions on sectorial tariff elimination with adequate flexibilities in order for all participants to participate. We recognize that the sectorial elimination component is an integral part of the proposed modalities which should take into account the particular export interests of developing and least-developed countries.	As an integral part of modalities applying to all Members, sectoral initiatives, in particular for products of export interest to developing countries, for instance harmonization or elimination for textiles and apparel and elimination for environmental goods and other sectors to be defined. Product coverage of and participation in such initiatives will need to be defined.
Newly Acceded Members	We recognize that newly acceded members shall have recourse to special provisions for tariff reductions in order take into consideration their extensive market access commitments undertaken as part of their accession and that staged tariff reductions are still being implemented in many cases. We instruct the Negotiating Group to further elaborate on such provisions.	We recognize that newly acceded members shall have recourse to special provisions for tariff reductions in order take into consideration their extensive market access commitments undertaken as part of their accession and that staged tariff reductions are still being implemented in many cases. We instruct the Negotiating Group to further elaborate on such provisions.	Additional time for the implementation of the results of the round (normal period times [X])

Special Report on WTO Cancun Ministerial Preparations, Number 4:

"Navigating the Singapore Issues: Rough Seas Ahead"

SUMMARY

The four "Singapore Issues," Investment, Competition Policy, Trade Facilitation and Transparency in Government Procurement, have until now been treated together at the insistence of the EU and Japan, the main demandeurs for negotiations on investment and competition. The EU and Japan have not wanted to separate investment and competition from the less controversial issues of trade facilitation and government procurement since this would probably doom any hope of a negotiation on investment and competition. At the Doha Ministerial, this insistence coupled with resistance to investment and competition by some developing countries, resulted in the four being bundled together.

Investment in particular is strongly opposed by some developing countries, notably by India, and certain African states, which have said that under no circumstances would they agree to launch negotiations on the subject in Cancun. The United States, while not a demandeur for either investment or competition, has until now given quiet support to the EU – as for example at the Doha Ministerial in 2001. The United States recently broke ranks, indicating that it does not wish to see negotiations on trade facilitation and government procurement held up by disagreements on the other two. One issue at Cancun will be whether to decouple the negotiations on the four issues.

The draft Ministerial text contains virtually identical language on each of the four issues, presenting two stark alternatives – to commence negotiations on the basis of "modalities" annexed to the Declaration, or to remit the subject to officials for further clarification. The draft modalities are in each case short: each stresses the need of developing countries for technical assistance and capacity building, and for flexibility in the application of any agreements to them. The draft on investment contains more details on the elements to be contained in an agreement.

It is believed by most Geneva delegates that there is little possibility of an agreement at Cancun to launch negotiations on investment. An agreement to launch negotiations on competition policy will also be difficult. Whether the Members let trade facilitation and procurement go forward at Cancun will depend on the tactics of the EU and Japan. If the EU and Japan continue to insist on keeping the four issues together, Members may have to relegate all four issues to further study, despite a considerable amount of preparatory work since 1996. In any case, navigation of the Singapore Issues will be difficult, and unpredictable as the weather patterns in Cancun during the current hurricane season.

ANALYSIS

I. Political Background: EU and Japan Becoming More Isolated

Two stark alternatives are presented by the drafters in paragraphs 13 – 16 of the draft Cancun Ministerial Text for each of the Singapore Issues – either to start negotiations on Investment, Competition Policy, Trade Facilitation and Transparency in Government

Procurement pursuant to "modalities" annexed to the draft Declaration, or to seek "further clarification" in the Council on Trade in Goods, thereby delaying formal negotiations.

African countries, in particular, have been strong proponents of delaying negotiations on all four Singapore issues. Furthermore, the "modalities" have been subject to criticism by developing countries, led by India, and joined by Botswana, China, Cuba, Egypt, Indonesia, Kenya, Malaysia, Nigeria, Philippines, Venezuela, Zambia, and Zimbabwe, which complain generally that the modalities were formulated by small groups and not discussed by the Members. On August 27, these countries wrote the Chairman of the General Council identifying many issues for further clarification and recalling that the Members can only commence negotiations on the Singapore issues on the basis of an "explicit consensus" – the language in the Doha Declaration on these issues. By emphasizing the need to clarify important issues, these developing countries are seeking to prevent negotiations or to delay the commencement of negotiations.

Despite the either/or tenor of the debate, resulting in part from the draft Declaration and the European view that linking the modalities on all four issues preserves balance, the United States is coming under domestic pressure from its Democratic party critics, industry representatives and others to de-link trade facilitation and transparency from investment and competition, recognizing that the latter issues pose greater challenges. These same critics have warned that investment may not be "ripe" for negotiation and that a weak investment agreement could undermine existing U.S. investment treaties. In any case, the US has always given lukewarm support to investment and competition policy throughout the study phase.

Bangladesh, Thailand, Colombia and Pakistan are reported to have complained that the draft Declaration "lacks middle ground" on the Singapore issues. The intermediate options being mooted include negotiating a "soft agreement" for competition, and perhaps other Singapore issues, that would not be subject to the terms of the dispute settlement understanding. One variant of this soft option calls for creation of a peer review mechanism for the review of competition authority decisions. Another option would be to link clarification of the modalities with a firm agreement to begin negotiations once an agreement on the modalities is reached. The EU remains opposed to a soft approach.

II. Investment: Strongest Winds Ahead

The EU and Japan, backed by Korea, Switzerland and Taiwan, have already begun to lower expectations on investment even as they clarify their position in the run-up to Cancun. Their latest proposal identifies specific negotiating objectives, but suggests limiting the scope of the negotiation to foreign direct investment (excluding portfolio investment) and would not permit investor-state disputes to be heard by WTO panels. Among other issues, the proposal addresses transparency, non-discrimination, pre-establishment commitments and special and differential treatment. The proposal also calls for balance-of-payment safeguards and a clarification of the relationship between an investment agreement, the existing Agreement on Trade-Related Investment Measures ("TRIMS Agreement"), and bilateral and regional investment agreements, raising concern among some Members that the negotiations could undermine existing bilateral investment agreements.

Developing countries and non-governmental organizations ("NGOs") continue to be skeptical (if not hostile) about the investment negotiations, in part because any inclusion of portfolio investment could limit the ability of developing countries to impose capital controls and to take other steps in the event of a financial crisis. Many NGOs have opposed investment negotiations since the OECD attempted, and failed to conclude an agreement. These groups have also expressed concern that an investment agreement may have unintended negative consequences for public health, the environment, labor rights, etc.

III. Competition: Another Problematic Forecast

Competition is also proving to be among the most problematic of the four Singapore issues. Developing countries propose exempting possible disciplines away from the applicability of the Dispute Settlement Understanding to this issue. The United States is providing some backing for developing countries in this regard, indicating support for a peer review mechanism (a "soft option"), instead of the normal dispute settlement rules.

IV. Transparency in Government Procurement: A Better Outlook

The EU and Japan, backed by Korea, Switzerland and Taiwan, have also tabled a proposal on transparency in government procurement. The proposal is modest in nature, explicitly limiting the negotiations to transparency, and providing for special and differential treatment for developing countries, including transition periods and flexibility concerning the extent of commitments. The proposal also calls for capacity building and technical assistance during the negotiations. The United States has gone further, indicating support for a developing country proposal that an agreement on transparency only cover developing country procurement above a certain threshold. Most developing countries have not expressed strong resistance to launching negotiations on transparency, even though a large majority are not part of the plurilateral Agreement on Government Procurement.

V. Trade Facilitation: More Promising Conditions

Although WTO Members are closer to an agreement on trade facilitation than any other issue, India and other developing countries have criticized the modalities Annex on this issue, calling for clarification of many points. Importantly, they suggest that the costs of trade facilitation for developed countries be assessed, and they propose compensation for the costs of developing countries that implement new rules and procedures to facilitate trade. They also propose that developed countries make special and differential treatment and technical assistance available.

Many developed and developing countries, gathering together as the "Colorado Group" in Geneva have been proponents of an agreement on trade facilitation. These countries have insisted that the conclusion of this long-delayed agreement would enhance the efficiency of trade overall, including for developing countries.

OUTLOOK

If the EU and Japan drop their demand that all four Singapore issues be treated together, progress may be possible on trade facilitation and transparency. Competition and investment have attracted considerable developing country opposition and it would take major concessions by the developed countries in other areas of interest to developing countries (in particular on agriculture) for progress to be made on these two issues.

It is no coincidence that the most protectionist countries on agriculture are also the main demandeurs for launching negotiations on complex new agreements on investment and competition. The EU since the first Ministerial in Singapore, under the direction of Commissioner Leon Brittain, had sought to balance the agenda and EU interests by insisting on these new and ambitious negotiations. Since the Singapore Ministerial, these two issues have become far more contentious and perhaps too difficult to expect even the start of negotiations.

Nonetheless, it appears that the climate has improved since Members last met at the port of Doha. There appears to be growing support to separate the four issues and allow the less controversial (and commercially meaningful) issues of transparency and trade facilitation to chart their course towards land. In the meantime, rough seas are ahead as Members gather in Cancun.

Special Report on WTO Cancun Ministerial Preparations, Number 3:

"Draft Ministerial Text Forwarded to Cancun: Surf's Up, or a Wipeout Ahead?"

SUMMARY

The World Trade Organization released on August 31, 2003 the text of a letter sent by the Chairman of the General Council, Ambassador Carlos Perez Del Castillo, and the Director General, Dr. Supachai, to the Foreign Minister of Mexico, Dr. Louis Derbez, who will Chair the Ministerial Conference of the WTO in Cancun on September 10-14. The purpose of the letter is to convey and comment on the "Draft Cancun Ministerial Text" issued on August 24, which will be the basis for the negotiations in Cancun and for the final declaration which will emerge from it.

The letter and the draft text are the product of intensive consultations among delegations that have taken place in Geneva throughout the month of August. The product of these negotiations demonstrate that time has not been wasted; one major issue has been resolved (*i.e*. TRIPS and Public Health) and the remaining problems facing Ministers at Cancun have been clarified, so that the danger of a manifest failure (or washout) at the Cancun Conference, which many feared, is now greatly reduced.

Nevertheless, it is also clear that all of the major elements of the Doha Development Agenda on which decisions will be required at Cancun remain unresolved, and that Ministers will face the greatest difficulty in reaching agreement on them in a five-day meeting. The outcome is unclear – perhaps the result will be neither success nor failure, but enough progress in some key areas to provide the basis for intensified negotiations in the next phase. This implies, in our view, that the official deadline of December 2004 for conclusion of this Round will become clearly unattainable (although Governments may find it impossible to say this explicitly at this stage). If the 2004 deadline is missed, the most likely date for conclusion of the Round will be December 2006.

ANALYSIS

I. Draft Ministerial Text: A Basis for a Deal?

The draft declaration sent forward to Ministers covers 25 separate issues – that is, all of the issues contained in the Doha Development Agenda. Not all of them require decisions at Cancun. On TRIPS and Public Health, for example, Ministers will simply welcome the decision already taken, and on many other subjects (*e.g.* services, rules and dispute settlement negotiations, etc.) they will just take note of the progress made in negotiations so far.

However there are three areas of major importance and difficulty on which it is necessary for Ministers to agree on negotiating "modalities" in order for the phase of substantive and binding negotiations to begin. These are (i) Agriculture; (ii) Non-Agricultural Market Access, which means essentially tariffs and non-tariff barriers on industrial products; and the (iii) "Singapore Issues" – Investment, Competition Policy, Trade Facilitation and Transparency in Government Procurement.

The covering letter by Ambassador Castillo and Dr Supachai makes it clear that there is no agreement as yet on any of these issues. It was not possible during the final days of consultations in late August in Geneva to improve on the text of the draft declaration which had been circulated on August 24. Thus, delegations in Geneva have forwarded the text unchanged to Cancun. Ministers meeting from September 10-14 must now take up the issue.

II. TRIPS and Health: Done Deal a Boost to the Round's Recovery

The issue which preoccupied Members and dominated the consultations at the end of August was agreement on the conditions under which poor countries should be allowed to use compulsory licenses to import generic copies of patented medicines for which they have no production capacity. Agreement had been delayed since December 2002 (the original deadline) because of fears that drugs produced for this purpose would be diverted onto world markets, thus damaging the revenues and research capacities of the pharmaceutical companies which own the patents.

Members concluded a deal on August 30 after several failed attempts during the week. A deal between the United States and African countries which are likely to be the major beneficiaries of such an agreement was derailed at the last moment by objections from the Philippines and Argentina. Withdrawal of these objections following strong pressure from African countries eliminated what would have been a serious embarrassment at Cancun: though it is not a major commercial issue its symbolic importance. If it had appeared that the US or other developed countries were impeding access by the poorest countries to essential medicines, could have prejudiced the entire Ministerial Conference.

The Decision taken on 30 August (WT/L/540) is accompanied by an explanatory statement by the Chairman of the General Council which in effect interprets the decision. It was the wish of certain countries to insert their own interpretation which caused the final crisis. The success of this deal clearly depends to some extent on good-faith implementation: "all reasonable measures" should be taken by governments to prevent the diversion onto other markets of medicines produced under compulsory license for distribution in the poorest countries. *(Please see our first Special Report on Cancun.)*

III. Agriculture: Tackling the Three-Hundred Pound (Pillar) Gorilla

It is universally recognized that the critical issue is agriculture and that if there is no agreement on this there will be none on any other of the controversial subjects. For many countries reform and liberalization of agricultural policies is the major priority in this Round and therefore at Cancun. Members intended at Doha to have already agreed at Cancun to the modalities which will govern the final stage of bargaining, and some hoped that if they were sufficiently precise it would be possible to complete the deal by the end of 2004.

However, the draft modalities proposed in March 2003 by the Chairman of the agriculture negotiations, Stuart Harbinson, proved too detailed to be acceptable to any of the major interest groups. Leaving aside specific objections, of which there were many, their acceptance would in effect have determined the outcome of the entire negotiation but for relatively minor outstanding points. No participant, and particularly traditional protectionist

Members like the EU, Japan and others under heavy pressure from domestic farm lobbies, could have made such concessions at this half-way stage of the Round.

The objective for Cancun has therefore been modified. Recognizing that detailed modalities are not attainable, what is now proposed is a "framework" which will "direct the subsequent work towards establishment of full modalities." The objective, therefore, is clearly less ambitious but nonetheless important in order to add momentum to these difficult negotiations.

The draft submitted by Ambassador Castillo is based mainly on a joint proposal submitted by the US and the EU, but also takes into account a counter-proposal by a group of 20 developing countries ("G-20") led by Brazil, China and India. The Chairman's draft presents options in all "three pillars" of agricultural reform (*i.e.*, market access, domestic support and export competition) and other issues (*e.g.* non-trade concerns, extension of geographical indications, etc.), but leaves open a wide range of possible outcomes.

Members from both major groupings have criticized the Chairman's draft for not containing specific figures for the reduction of export subsidies, domestic support and tariffs – but leaving these up for negotiation after the framework is agreed. Also, the extent of special and differential treatment for developing countries, and the tariff reduction formula to be applied by them, are left open, as are the conditions and coverage of a special agriculture safeguard mechanism which is to be established for use by developing countries. *(Please see our second Special Report on Cancun.)*

Agreement on such a framework at Cancun would clearly leave a great deal to be decided, and there is much discussion in Geneva of the possible need for a further Ministerial meeting, perhaps in January 2004, at which detailed modalities would be agreed. Alternatively – and perhaps preferably, given the complexities of Ministerial conferences - such a meeting might be held at high official level. In either case, if the real decision on agricultural modalities were to be deferred in this way it seems unlikely that final decisions could be taken at Cancun on the modalities for tariff negotiations and the Singapore issues.

IV. Non-Agricultural Market Access: A Less Ambitious Framework

The draft Ministerial text also contains a "framework" for the negotiations on tariffs and non-tariff barriers, on the basis of which detailed modalities will be established. This also therefore represents a scaling-down of ambitions for Cancun. The framework is closely based on the draft modalities proposed by Ambassador Girard of Switzerland, the Chairman of the negotiating group, but again excludes much of the detail. There is disagreement on two key issues: (i) the nature of the tariff-cutting formula to be employed; and (ii) which sectoral negotiations will be covered.

Regarding the tariff cutting formulas, developing countries in general seek a fairly low level of ambition, especially where their own tariffs are concerned, while the developed countries look for more. On the sectoral component of the negotiations, it is accepted that there should be some sectors, particularly involving products of export interest to developing countries, on which tariffs should be eliminated. Girard had proposed seven product groups (*i.e.*,

electronics and electrical goods; fish and fish products; footwear; leather goods; motor vehicle parts and components; stones, gems and precious metals; and textiles and clothing) for zero duties. Though these were selected as being advantageous to developing countries, it is being argued, by developing countries, that the elimination of tariffs on them should be voluntary, not mandatory (which would seem to defeat the object of the exercise; any country can voluntarily eliminate tariffs at any time).

Developed countries, including the US seek a far more ambitious approach to tariff liberalization and attention to non-tariff barriers. Although they support flexibility for developing countries to some extent, they have warned that they will not support a double standard in which developing countries could take advantage of far less ambitious tariff reduction formulas.

It is clear that final agreement on, and the level of ambition of, the tariff modalities will depend on the outcome on agriculture, as will the results in negotiations in other areas, such as trade in services. Major developing countries like Brazil have made it explicit that their contribution in all other areas will depend on a satisfactory outcome in agriculture. *(Please see our fourth Special Report on Cancun.)*

V. Singapore Issues: To Launch or Not to Launch? – Those Are the Four Questions

The four "Singapore Issues" – Investment, Competition Policy, Trade Facilitation and Transparency in Government Procurement – have hitherto been treated alike at the insistence of the EU and Japan, which have been the main demandeurs for negotiations on investment and competition and have feared that to separate them from the less controversial issues of trade facilitation and government procurement would be to surrender any hope of agreement to negotiate on them.

Investment in particular is strongly opposed by some developing countries, notably by India, which has said that in no circumstances will it agree to launch negotiations on the subject in Cancun. The United States, while not a demandeur for either investment or competition, has until now given quiet support to the EU – as for example at the Doha Ministerial in 2001. The US has now broken ranks, indicating that it does not wish to see negotiations on trade facilitation and government procurement held up by disagreement on the other two. The first question regarding these subjects at Cancun will therefore be whether to unbundle them.

The draft Ministerial text contains virtually identical texts on each of the four issues, presenting two stark alternatives – to commence negotiations on the basis of modalities annexed to the declaration or to remit the subject to officials for further clarification. The draft modalities are in each case very short: all of them stress the needs of developing countries for technical assistance and capacity building and for flexibility in the application of any agreements to them. Only the draft on investment contains any detail on the elements to be contained in an agreement.

It is believed by most Geneva delegates that there is no possibility of agreement at Cancun to launch negotiations on investment. Competition policy will also be difficult. Much will depend on the tactics of the EU and Japan, as to whether trade facilitation and procurement

will be allowed to go forward while investment and probably competition are held back for further study. If the EU and Japan continue to insist on keeping the four issues together, them Members might be resigned to relegate all four issues to further study without any negotiating mandate. *(Please see our fifth Special Report on Cancun.)*

VI. Special and Differential Treatment: Not Special and Different Enough?

The draft Ministerial text contains 21 decisions for adoption by Ministers regarding the special and differential treatment of developing countries under various WTO Agreements. These are the product of intensive consultations carried out by Ambassador Perez Del Castillo. Although many of the issues and demands raised by developing countries over the past four years regarding the "implementation" of agreements remain open, the decisions to be taken at Cancun should suffice to prevent disagreement over the implementation agenda from becoming a major problem and a threat to the conference. Nevertheless, some developing countries and groupings are still reluctant to adopt the 21 issues on which consensus has been achieved, and seek additional flexibility on up to an additional 70 outstanding issues identified in the Doha Ministerial texts.

OUTLOOK

Although the level of ambition for this Cancun Ministerial Conference has been substantially reduced by the adoption of the "framework" approach to agriculture and industrial tariffs, there will still be intense difficulty in reaching agreement on these issues and the Singapore Issues in only five days.

Success at Cancun will depend on the handling of agriculture – by far the most critical and difficult issue next week, if not the Round as a whole. Early progress on agriculture negotiations, perhaps facilitated by movement on the part of the EU, would generate progress on the other difficult issues. However, if agriculture is allowed to drag until the final day in the normal manner of WTO Ministerial meetings – the issue could become impossible to resolve simply for lack of time.

Members intend to use at Cancun the technique at Doha (successfully), of inviting some Ministers to act as "Friends of the Chair" in leading consultations on key issues. This enables work to proceed simultaneously on several different fronts. Nevertheless, it will still be agriculture which sets the pace of all other negotiations.

At least, Members will succeed in welcoming Nepal and Cambodia as new Members – important developments, but not the same magnitude of publicity as China concluding its membership at Doha.

Ministers from 146 WTO Members will soon proceed to the sandy shores of Cancun to either make waves and give much needed momentum to the Round, or face an embarassing wipeout. If Cancun turns out to be a wipeout, Members might have to wait a long time to catch the next big wave.

Special Report on WTO Cancun Ministerial Preparations, Number 2:

"Competing Proposals on Agriculture Have Transformed the Rural Landscape"

SUMMARY

WTO negotiations on "modalities" (approaches and targets) for agriculture reform have regained momentum in the final weeks before the Cancun Ministerial Meeting, but competing proposals from several major blocs of Members have complicated negotiations even further.

Since missing the March 2003 deadline, key WTO Members in the past month have tried to break the deadlock over Chairman Stuart Harbinson's draft modalities by submitting new proposals. The most significant ones are the joint US-EU proposal and a counter-proposal put forward by a group of twenty developing countries ("G-20"), led by Brazil, China and India. In addition, the General Council Chairman, Carlos Perez del Castillo, released a revised ministerial declaration for the Cancun meeting that contains his own proposal on modalities for agriculture negotiations. The Chairman's text is intended as a compromise between the EU-US joint proposal and the G-20 counter-proposal. Reaction to this text has been mixed. In any event, it will serve as a basis for discussion at the Cancun.

The EU-US text has provoked a sudden and unexpected modification in the landscape of traditional alliances that play a role in agriculture negotiations. Key developing countries that belonged to different groupings such as the Cairns Group, the Like-minded countries and Net-food importer countries, have rallied together as a reaction against the conservative approach of the EU-US text. It is likely that the two driving forces at Cancun will be the US and EU, on the one hand, and the G-20, on the other side.

The present report highlights the recent events leading up to Cancun on agriculture and the key proposals in relation to the "three pillars" of the Agreement on Agriculture (market access, domestic support and export competition). In particular, the Chairman's draft text is contrasted with the EU-US and the G-20 texts.

It must be understood that the agriculture modalities are critically important. The negotiation on modalities includes, *inter alia*, agreements on phase-out or reduction formulas, implementation periods, and special and differential treatment for developing countries. An agreement on negotiating modalities will, to a considerable extent, decide the outcome of the negotiations.

ANALYSIS

I. Recent Events in the Road to Cancun on Agriculture Negotiations

The recent events in the road to Cancun could be divided into two stages:

A. First Stage: Negotiations Dominated by the Harbinson Draft

- March 18, 2003: Chairman of the Negotiating Group on Agriculture Stuart Harbinson circulated his revised version of draft on agriculture modalities. The first version had been circulated on February 12, 2003.[29] As compared to Ambassador Pierre-Louis Girard's draft on negotiating modalities for non-agriculture products, Harbinson's draft is a very comprehensive and detailed one. This degree of detail could have proved counter-productive since it implied an early agreement on many substantive issues. The draft was immediately criticized heavily by all sides -by Japan and the EU as being unbalanced and neglectful of "non-trade concerns", and by the Cairns Group and the US as lacking ambition on subsidy and tariff reductions.

- July 7, 2003: Chairman Harbinson submitted his report to the Trade Negotiating Committee (TNC) on the state of play of agriculture negotiations, highlighting in a non-exhaustive manner key issues and questions which, in his view, participants needed urgently to address.[30]

B. Second Stage: Efforts to Break the Deadlock

- August 13, 2003: the EU and the US released a joint proposal to break the deadlock on negotiations on agriculture modalities.[31] This new proposal is less detailed than Harbinson's draft. It is just a "framework" agreement on the most relevant issues. The EU and the US have been keen to emphasize that their joint proposal was not exclusive and that additional issues such as special and differential treatment for developing countries needed to be inserted in the proposed text.

- August 20, 2003: Brazil, India, China and a group of developing countries, most of them Cairns Group members (the so-called G-20),[32] released a counter-proposal to the EU-US joint text, following the same structure.[33]

- In addition to these two propodsals, other Members such as Switzerland, a group of six newly acceded Members; Japan; Norway[34] and Kenya have also submitted their own proposals.

[29] TN/AG/W/1/Rev.1, dated March 18, 2003.

[30] TN/AG/10, dated July 7, 2003.

[31] JOB (03)/157, dated August 13, 2003.

[32] The G-20 comprises: Argentina, Brazil, Bolivia, Chile, China, Colombia, Costa Rica, Cuba, Ecuador, El Salvador, Guatemala, India, Mexico, Pakistan, Paraguay, Peru, Philippines, South Africa, Thailand, and Venezuela.

[33] JOB (03)/162, dated August 20, 2003.

[34] JOB (03)/169, dated August 21, 2003.

- August 24, 2003: WTO General Council Chairman Carlos Perez del Castillo released a revised Ministerial Declaration draft text for the Cancun meeting.[35] Paragraph 4 of the draft declaration reaffirms the mandate on agriculture as set out in paragraph 13 of the Doha Ministerial Declaration. In addition, paragraph 4:

  a) provides for a "framework" containing a basic agreement on key negotiating modalities for the major issues under negotiation (Annex A to this document). This proposal is intended to be a compromise text between the EU-US' joint proposal and the G-20's counter-proposal.

  b) directs the Special Session of the Committee on Agriculture to conclude its work on establishing modalities on pending issues for the further commitments, including provisions for special and differential treatment, within a specific timeframe to be agreed at Cancun.

  c) provides for a deadline (to be agreed at Cancun) to submit Members' draft Schedules based on the negotiating modalities.

II. New Alliances in Agriculture Negotiations

The release of the EU-US text has provoked a sudden and unexpected modification in the landscape of alliances that play a role in agriculture negotiations. As a reaction to that paper, Members broke traditional alliances. The most significant one is the establishment of the G-20 Group, led by Brazil, China and India, that comprises developing countries from the Cairns Group, net-food importers developing countries and some Like-minded countries. These countries may have decided to forget their differences, in particular, on market access, in order to put forward a proposal that could be sufficiently strong to counter-act the EU-US move. This could be understood as a reaction against the conservative approach on domestic support and export subsidies adopted by the two leading powers.

In addition to these two major contenders, the landscape seems to be completed by key isolated players who may side with one group or the other, depending on the issues. Such key players are: Norway, Japan, Switzerland, Australia, New Zealand, Canada, Kenya along with the rest of the Like-minded developing countries and some newly acceded countries.

III. Key Proposals on the "Three Pillars" of Agriculture

A. First Pillar: Domestic Support

- Formula for reduction of the Amber Box[36]: both the Chairman's and the UE-US texts call for the reduction of trade-distorting domestic support. Reductions would

[35] JOB (03)/150/Rev.1, dated August 24, 2003.

[36] The Amber Box mainly covers domestic support subsidies that are considered trade distorting. The Agreement establishes a ceiling on the total domestic support (calculated as the "Aggregate Measurement of Support," AMS) that governments may provide to domestic producers. In addition, it requires that AMS should be reduced by agreed percentages.

be made in an aggregated (non-product specific) manner following the Uruguay Round approach, and would not be harmonized. There would not be any distinction between products exported and those supplied to the domestic market. These proposals highly contrast with the G-20 text, which calls for i) a reduction on product specific basis; ii) steeper cuts on products which benefited from levels of domestic support, above the average, during a certain time period, bringing the final levels closer together (to harmonize the levels of support); and iii) deeper cuts, with a view to elimination, for products benefiting from domestic support which are exported.

In addition, the text also provides a further capping of domestic support: the sum of allowed support under the Amber Box and *de minimis* must be reduced so that it is significantly less than the sum of *de minimis*, payments under the Blue Box, and the final bound Amber box level in 2000.

- Proposal with regard to the Blue Box (Art. 6. 5 AA):[37] the Chairman's text introduces a cap on Blue Box measures of 5 percent of the total value of agriculture production in the 2000-2002 period, and subsequently applies on them an annual linear reduction (reduction percentage and time period to be agreed). While the EU-US proposal does not refer to the Blue Box, the G-20 paper calls for the complete elimination of Blue Box measures. Opponents of the Blue Box contend that these measures are trade distorting, since production is still required in order to receive the payments (although payments are not directly related to the current quantity of production).[38]

- Proposal with regard to the Green Box (Annex 2, AA):[39] the Chairman's proposal calls for the continuation of negotiations of "Green Box criteria." While the EU-US proposal does not refer to the Green Box, the G-20 proposal calls for i) capping and/or reducing green box direct payments in the case of developed countries and ii) for the elaboration of additional disciplines. The G-20 text reflects the great concern of developing countries about the abuse by developed countries of the Green Box. It should be recalled that the recent agreement on the reform of the EC Common Agriculture Policy (CAP) would shift around 60 percent domestic Amber Box existing subsidies to the Green Box.

[37] The Blue Box covers direct payments under production limiting programs, which are exempted from commitments if such payments comply with certain criteria.

[38] According to contenders, the EU-US text seeks to maintain the possibility of granting 10,000 millions euros and USD 9,500 millions in Blue Box domestic support, respectively for the EU and the US. It is worth noting that unlike the Fair Act of 1996, the Farm Bill of 2002, allows the introduction of Blue Box support.

[39] The Green Box covers all subsidies that have "no, or at most minimal, trade distorting effects or effects on production" and that do not have the "effect of providing price support to producers." Green box subsidies are exempt from reduction commitments.

- Proposal with regard to *de minimis* subsidies (Art. 6.4 AA):[40] the Chairman's text calls for the reduction of *de minimis* subsidies for developed countries. The Chairman has followed the G-20 on this point and contrasts sharply with the EU-US proposal which does not provide for special and differential treatment. However, the G-20 text makes it more explicit: it provides that developing countries will be able to maintain *de minimis* subsidies at the existing levels.

- Special & Differential Treatment: the Chairman's draft also includes a list with some S&D provisions for developing countries, "[…] *having regard to their development, food security and/or livelihood security needs* […]," The list includes: i) lower reductions of trade-distorting domestic support; ii) longer implementation periods; iii) retaining the so-called "developmental measures" (Art. 6.2 AA);[41] iv) and new S&D provisions under the Green Box. The G-20 has proposed to expand the scope of Art. 6.2 (development measures) so as to include focused and targeted programs.

B. Second Pillar: Market Access

- Formula for tariff reduction for developed countries: the Chairman adopted the EU-US approach which provides for:

  i) a "three-part blended formula" (Uruguay Round/Swiss formula/zero duty treatment) [42] for three categories of tariff lines, depending on their sensitiveness. In the case of "import-sensitive tariff lines" (1st category), the UR formula will be *combined with tariff-rate quotas.*

  ii) a "capping" for those tariff lines that exceed a maximum to be established, with the following options for developed countries: reduction to that maximum or granting of effective additional market access in these or other areas through a request-offer process that could include TRQ.

  This proposal contrasts sharply with the G-20's one, which i) does not provide for the application of tariff-rate quotas in case of sensitive products (1st category), ii) addresses the issue of tariff escalation in the case of products subject to the UR formula; iii) and calls for a capping of tariff lines that a exceed a maximum to be established and the for the commitment to reduce them to that maximum.

[40] *De minimis* subsidies are trade distorting domestic support (normally subject to reduction commitments) which are exempted from reduction when they do not exceed certain thresholds.

[41] Article 6.2 of the AA provides for the so-called "developmental measures:" measures of assistance, whether direct or indirect, designed to encourage agricultural and rural development and that are an integral part of the development programs of developing countries.

[42] According to the Uruguay formula, all *ad valorem* tariffs are reduced by a simple average (except in-quota) subject to a minimum reduction per tariff line. The Swiss formula entitles a greater reduction to the higher tariffs (tariff peaks) rather than an average cut.

- Formula for tariff reduction for developing countries: the Chairman proposes a choice between: i) the application of the UR formula to three different categories of tariff lines, depending on their sensitiveness; and ii) a blend of the UR and Swiss formulas, without a zero duty category. In both cases, the Chairman proposes for the first category (sensitive tariff lines):

  - a combination of tariff cuts and TRQs (as for developed countries);

  - additional flexibility under conditions to be determined to designate "Special Products" ("SP") which would only be subject to a linear cut of a minimum percentage and no new commitments regarding TRQs.

  By providing for the possibility of designating SP, the Chairman has tried to avoid the same critics to the EU-US's proposal which does not mention the concept of SP as introduced in the Harbinson modalities.[43] The G-20's proposal also calls for the establishment of SP "under conditions to be determined in the negotiations." This cautious language reflects the internal discrepancies of the G-20 members on this point and the need to show a basic degree of consensus.[44]

- Duty-free access for imports from developing countries. Following the EU-US proposal, the Chairman's text provides that "*all developed countries will seek to provide duty-free access for at least […]% of imports from developing countries through a combination of MFN and preferential access*." The G-20 proposes, instead, a more explicit commitment from developed countries to provide duty-free access to all tropical agricultural products, products of particular importance to the diversification of production from the growing of illicit narcotic crops, and other agricultural products representing a percentage to be agreed on of imports from developing countries.

- Issues to be addressed through further negotiations. In sharp contrast with the G-20 text, the Chairman's text follows the EU-US approach and calls for further negotiations on:

  - Expansion/Opening of [existing]TRQs and in-quota tariff rates. The G-20 proposes that TRQs "be expanded by [ ] % of domestic consumption and in quota tariff rates [be] reduced to zero. […] Larger expansion or creation of TRQs could be the result of a request and offer process." In addition, the G-20 calls for the exemption of developing countries from making commitments regarding TRQ expansion and reduction of in-quota tariff rates.

[43] The Harbinson draft text introduced the concept of "Special/Strategic products" that would allow developing countries to undertake lower tariff reductions on a number of sensitive products related to food security, rural development and/or livelihood security concerns.

[44] India and other developing countries, supporters of the so-called "development box," have put forward this proposal, which was resisted by the Cairns Group and the US. Opponents have expressed concern that the modality could provide developing countries with a tool to opt out from multilateral liberalization on a permanent basis.

- ***Special Agricultural Safeguard (SSG).*** This proposal contrasts sharply with the G-20's proposal which calls for the elimination of the SSG for developed countries.

- ***Special Agricultural Safeguard (SSM):*** the text calls for the establishment of a SSM for use by developing countries subject to conditions and for products to be determined.

C. Third Pillar: Export Competition

- Elimination/reduction formula: the Chairman proposed a two-tier approach, following the EU-US text. The proposal calls for:

  i) the elimination within a certain time period of export subsidies for products [to be designated] of special interest to developing countries;

  ii) the reduction, "with a view to phasing out," of export subsidies for the remaining products. Unlike the EU-US proposal, the paper also provides that the "question of the end date for phasing out of all forms of export subsidies remains under negotiations."

  The G-20 text calls, instead, for the elimination of the second category of export subsidies, but over a longer phase-out period to be agreed upon.

  As part of S&D, developing countries: i) would benefit from longer implementation periods for reductions; ii) would be able to maintain flexibility to exempt certain transport and marketing subsidies from export subsidy reduction (Art. 9.4 of AA) until all exports subsidies have been fully phased out by all Members.

- Export credits: the Chairman's paper, as in the EU-US paper, provides that subsidized export credits (trade-distorting elements of export credits) would be treated in parallel and equivalent manner with export subsidies (i.e. application of the same two-tier approach). Based on the G-20 proposal, the Chairman's text also calls for the establishment of disciplines for the identification and elimination of the subsidy component. The text also provides that Members must ensure that disciplines on export credits must take into account paragraph 4 of the Decision on Measures Concerning the Possible Negative Effects of the Reform Programme on Least Developed Countries and Net Food Importing Developing Countries."[45]

- State trading enterprises ("STE"): the Chairman's paper differs from the EU-US proposal on this point. The Chairman's text provides that "the provisions related to the reductions of, with a view to phasing out, all forms of export subsidies […] shall apply equally to all forms of export subsidies related to or provided, directly

[45] "Ministers further agree to ensure that any agreement relating to agricultural export credits makes appropriate provision for differential treatment in favour of least-developed and net food-importing developing countries." (Paragraph 4)

or indirectly, to, by, or through STE." While the G-20 does not refer to this issue, the EU-US paper only calls for the establishment of disciplines.

- Food aid operations: all proposals call for the negotiations of additional disciplines in order to prevent commercial displacement through food aid operations.

- Export prohibitions, export restrictions and export taxes: the Chairman's text calls for the strengthening of Art. 12 of the AA on export prohibitions and export restrictions. It also calls for further negotiations on modalities to establish disciplines on export taxes.

D. Other Issues

- The Chairman's framework text list several "issues of interest but not agreed" and calls for further work on modalities. The list includes, *inter alia*: the peace clause (the EC and others want it renewed, while the G-20 want it to expire), the continuation clause (Art. 20 of the AA provides for the continuation of the reform process), certain non-trade concerns (supported by the "Friends of Multifunctionablity", such as the EC, Japan, Norway, Switzerland and others), sectoral initiatives (e.g. the cotton initiative of some African countries), inter-pillar linkages (the Philippines want to condition new market access commitments for developing countries to the prior substantial reduction of OECD farm subsidies), and geographical indications (supported by the EC, Switzerland and others).

OUTLOOK

Reaction to the Chairman's draft has been mixed. The EU and the US criticized it for going too far in calling for cuts to domestic and export subsidies and doing too little on market access of developing countries. The G-20 along with such exporters as Australia and Canada insisted that the paper did not go far enough on these issues. Nevertheless, Perez del Castillo has stated that he would not modify the draft and that it would be forwarded to the Ministerial Conference in Cancun in its present form.

With the exception of Australia and New Zealand, which may feel closer to the G-20's positions, the battle on agriculture negotiations at the Cancun Ministerial Meeting is likely to crystallize a North-South divide. This new picture will contrast with the previous patchwork of groupings (e.g. food exporters, net food importers, Members with subsidized agricultural sector, etc.) that has dominated until very recently agriculture negotiations in the WTO. However, it still needs to be seen whether the G-20 will continue to act together as such or it is just a temporary strategy of its members.

It is likely that most of the time of negotiations at Cancun will be dedicated to reach an agreement on the agricultural negotiating modalities. If an agreement could not be reached at Cancun, Members will certainly schedule extraordinary high-level meetings to close a deal in the short-run.

Special Report on WTO Cancun Ministerial Preparations, Number 1:

"Averting an Unhealthy Outbreak at Cancun: WTO Members Conclude an Agreement on TRIPS and Public Health"

SUMMARY

On August 30, 2003, WTO Members reached agreement on an important and overdue Decision (original deadline was December 2002) setting out a system to assure the supply of cheaper drugs to least developed countries and other developing countries in situations of national health emergencies or extreme urgencies.

Since December 2002, the United States has been the lone holdout on reaching a final deal due to concerns of patent infringement arising from illegitimate use of compulsory licensing, among other reasons. Since WTO Members agreed to the Declaration on TRIPS and Public Health at the Doha Ministerial in 2001, they have sought to strike a balance between the interests of patent protection and the health needs of developing countries, especially in sub-Sahara Africa. Paragraph 6 of the Declaration required further guidance on implementation, in particular with respect to countries that have insufficient or no manufacturing capacity.

In addition to the latest Decision, Members agreed on a controversial General Council Chairman's Statement. The Statement contains several key shared understandings of Members regarding the Decision that was adopted and the way it will be interpreted and implemented. In particular, the Statement provides that Members will take "all reasonable measures" to prevent diversion of cheaper drugs produced under the new system, and sets forth some of the anti-diversion measures that are likely to be implemented.

Although the TRIPS and Public Health issue is not formally part of the Cancun agenda, a failure to conclude a deal prior to Cancun would have complicated negotiations on other issues.

ANALYSIS

I. Background on TRIPS and Public Health: An Elusive Remedy

On August 30, 2003, at the last General Council meeting before the Cancun Ministerial, WTO Members reached an important agreement on the implementation of Paragraph 6 of the Doha Declaration on the TRIPS Agreement and Public Health ("TRIPS and Public Health Declaration").

HIV, malaria and tuberculosis, among other diseases, pose enormous public health problems for many developing countries. Paragraph 6 of the TRIPS and Public Health Declaration recognized that "WTO members with insufficient or no manufacturing capacities in the pharmaceutical sector could face difficulties in making effective use of compulsory licensing

under the TRIPS Agreement."[46] Members instructed the TRIPS Council to find a solution to this problem before the end of 2002. By December 2002, all Members except the United States were prepared to conclude a deal based on a draft Decision by Ambassador Carlos Perez Motta of Mexico, then Chair of the TRIPS Council. The United States resisted the deal due to concerns of patent infringement arising from illegitimate use of compulsory licensing by countries with manufacturing capacity such as India and Brazil, among other reasons

The failure of the Members to find a timely solution to this problem, which is of serious concern to many developing country Members in sub-Sahara Africa and elsewhere, has soured the ongoing trade negotiations, including preparations for the Cancun Ministerial.

II. Decision and Statement on TRIPS and Public Health: Steps Toward a Cure

Members on August 30, 2003 adopted:

- *a **Decision*** establishing a system to provide developing countries that lack manufacturing capacity with access to cheaper drugs.[47] The Decision draws on a draft text circulated by the former Chairman of the TRIPS Council Carlos Perez Motta to WTO Members on December 16, 2002.

- a ***Chairman's Statement*** that will be accompanying the Decision, which represents several key shared understandings of Members regarding the Decision that was adopted and the way it will be interpreted and implemented.[48]

A. The Decision of August 30, 2003

The decision provides, *inter alia*, for (i) conditions to be met by the compulsory licensee to be issued; (ii) the waiver procedure; (iii) remuneration to the patent owner; (iv) measures to prevent trade diversion; (v) the commitment to not challenge any measures taken in conformity with the provisions of the waivers; and (vi) criteria for the assessment of manufacturing capacities in the pharmaceutical sector. It is worth noting that the decision does not limit the scope of the system to specific diseases.

For the purpose of this Decision, the following terms are applicable:

[46] Declaration on the TRIPS Agreement and Public Health, Paragraph 6, WT/MIN(01)/DEC/W/2, November 14, 2001. A major limitation in compulsory licensing under Article 31 (f) of the TRIPS Agreement is the requirement that a product made under a compulsory license ***be supplied predominantly to the licensee's domestic market,*** unless the license was issued to remedy anti-competitive practices (Art. 31 (k) of the Agreement). This means in practice that a large number of developing and least developed country Members cannot effectively grant such licenses because they lack or have insufficient capacity to manufacture medicines. At the same time, they cannot import generic medicines manufactured under a compulsory license by another Member because Article 31 (f) requires that production must be predominantly for the domestic market.

[47] WT/L/540.

[48] A footnote to the Decision provides that "this Decision was adopted by the General Council in the light of a statement read out by the Chairman, which can be found in JOB (03)/177. This statement will be reproduced in the minutes of the General Council to be issued as WT/GC/M/82."

- Covered products – The Decision defines as a "pharmaceutical product" any patented product, or product manufactured through a patented process, of the pharmaceutical sector needed to address the public health problems as recognized in paragraph 1 of the Declaration (*i.e*. "especially those resulting from HIV/AIDS, tuberculosis, malaria and other epidemics"). It is understood that active ingredients necessary for its manufacture and diagnostic kits needed for its use would be included;

- Eligible importing Member – Defined as any least-developed country Member, and any other Member that has made a notification to the Council for TRIPS of its intention to use the system as an importer. A Member may notify at any time that it will use the system in whole or in a limited way, for example only in the case of a national emergency or other circumstances of extreme urgency or in cases of public non-commercial use. It is noted that some Members will not use the system set out in this Decision as importing Members (*e.g*. developed, including most OECD countries) and that some other Members (*e.g*. advanced developing, including Chinese Taipei, Korea and Turkey); have stated that, if they use the system, it would be only in situations of national emergency or other circumstances of extreme urgency; and

- Exporting Member – Defined as a Member (*e.g*. some developing countries, including India and Brazil) using the system set out in this Decision to produce pharmaceutical products for, and export them to, an eligible importing Member (*e.g*. least developed countries, including in sub-Sahara Africa).

B. The General Council Chairman's Statement

During the course of an extraordinary meeting of the TRIPS Council held on August 28, WTO Members discussed a draft Chairman's statement intended to introduce additional safeguards to the draft Decision – at the insistence of the United States. At first, the draft statement generated a considerable amount of controversy relating to its wording and legal effect, necessitating several meetings held over the course of three days, before the residual difficulties were solved on August 30.

The final Statement is widely perceived by both developed and developing country WTO Members to be balanced, and to provide the assurances sought by the pharmaceutical industry that drugs manufactured under compulsory licenses will not be diverted to markets where they could command a higher price, and for commercial reasons. This issue was an important stumbling block for manufacturers in developed countries, particularly in the United States.

The final Statement contains:

(i) ***"Good faith"*** – Assurance that the new system will be used in "good faith" and not as an instrument to pursue industrial or commercial policy objectives;

(ii) ***Prevention of diversion*** – Recognition that the new system would be defeated if products are diverted from intended markets;

(iii) ***Provision for special packaging*** – An understanding that special packaging, shapes and coloring for pharmaceuticals supplied through the new system should not have a significant effect on the price of these pharmaceuticals;

(iv) ***Best Practices*** – Guidelines on Best Practices to prevent diversion;

(v) ***Transparency*** – Provisions promoting transparency and the resolution of issues;

(vi) ***Members opting out*** – List of (*e.g*. developed and most OECD) WTO Members who have opted out of the system;[49]

(vii) ***Future EU members opting out*** – List of countries soon to join the European Union who will then opt out of the system and who will only use the system in the interim in situations of national emergency or other circumstances of extreme urgency,[50] and lastly,

(viii) ***Limited use by other Members*** – List of WTO Members (*e.g*. advanced developing) who have agreed only to use the system in situations of national emergency or other circumstances of extreme urgency.[51]

C. Agreement to Conclude an Amendment to the TRIPS

The final provision of the Decision contains an agreement by Members to initiate by the end of 2003, work on the preparation of an amendment to the TRIPS Agreement with a view to its adoption within six months. This amendment should be based, where appropriate, on the terms of the Decision adopted on August 30. Members also agreed that the Decision, including the waivers granted in it, will terminate for each Member on the date on which the amendment to the TRIPS Agreement replacing its provisions (*i.e*. Art. 31.f) takes effect for that Member.

Finally, Members agreed that this mandate for further negotiations on this issue should not be part of the single undertaking of the Doha Round of negotiations.

OUTLOOK

Progress on the TRIPS and Public Health issue is of vital importance to many developing countries, particularly those of Sub-Saharan Africa that are gravely affected by HIV, malaria and tuberculosis and that lack the capacity to manufacture sophisticated pharmaceutical products.

[49] Australia, Austria, Belgium, Canada, Denmark, Finland, France, Germany, Greece, Iceland, Ireland, Italy, Japan, Luxembourg, Netherlands, New Zealand, Norway, Portugal, Spain, Sweden, Switzerland, United Kingdom and United States of America.

[50] Czech Republic, Cyprus, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovak Republic and Slovenia.

[51] Hong Kong China, Israel, Korea, Kuwait, Macao China, Mexico, Qatar, Singapore, Chinese Taipei, Turkey, United Arab Emirates.

Due to the previous impasse on this issue, many developing countries had begun to fear that they would gain little from the so-called Doha "Development Round." In fact, some countries warned that without progress on the TRIPS and Public Health Issue – they might not support moving the agenda forward on other issues at Cancun.

WTO Members' ability to reach agreement on the Decision and Chairman's Statement has cleared a potentially serious obstacle at Cancun, and has provided the current round with a much needed boost in the run up to Cancun. The recent agreements also provide the developing world with greater hope to respond to heath crises in the longer term.

UNITED STATES

Free Trade Agreements

Bush Administration Continues Push for Competitive Liberalization

SUMMARY

The Bush Administration is forging ahead with its competitive liberalization strategy by negotiating Free Trade Agreements (FTAs) at the bilateral, regional and multilateral level. Since our last update, the following developments took place:

- President Bush signed the implementing bills for the FTAs with Singapore and Chile. The implementation of the FTAs will take effect starting January 1, 2004.

- The Administration continued negotiations with Morocco, Central America, the Southern African Customs Union (SACU), and Australia;

- The Administration formally notified Congress of its intention to initiate FTA negotiations with Bahrain and the Dominican Republic.

In this report, we highlight the different steps that the Administration had to take, under Trade Promotion Authority (TPA), for the negotiation of the Singapore and Chile FTAs, as well as for the ongoing and announced negotiations.

ANALYSIS

I. President Bush Signs Implementing Bills Chile and Singapore FTAs

On September 3, 2003, President George W. Bush signed the implementing legislation for the bilateral Free Trade Agreements (FTAs) with Chile and Singapore. The signing was the last step before the implementation of the FTAs, which will take effect starting January 1, 2004.

The U.S. agreed to negotiate the Chile and Singapore FTAs in November 2000, and the United States Trade Representative (USTR) launched negotiations in December 2000. At that time, the U.S. had concluded FTAs with Israel (April 22, 1985), Canada and Mexico (NAFTA) (December 17, 1992), and Jordan (October 24, 2000).

The Chile and Singapore FTAs are the first agreements to be completed under the renewed Trade Promotion Authority (TPA), which was passed with the Trade Act of 2002 on August 6, 2002.

According to TPA, the USTR must:

- Notify Congress of its intention to negotiate at least 90 days before initiating FTA negotiations. In the case of Chile and Singapore, USTR was required

to notify Congress of the ongoing negotiations as soon as possible after the enactment of the Trade Act.

- Conduct environmental reviews of future FTAs.

- Conduct reviews of the impact of future FTAs on U.S. employment.

- Submit a report regarding labor rights of the countries with which the US is negotiating FTAs and describe the extent to which these countries have in effect laws governing exploitative child labor.

- Request at least 90 days before entering into an FTA that the International Trade Commission (ITC) prepare a report assessing the likely impact of the FTA on the U.S. economy as a whole and on specific industry sectors. The ITC must submit this report to the USTR and to Congress by a maximum of 90 days after entering into the FTA.

- Notify Congress at least 90 days before entering into an FTA of its intention to enter into the FTA.

- Submit to Congress, within 60 days after entering into the agreement, a description of the changes to existing laws that would be required in order for the US to be in compliance with the agreement.

- Submit to Congress, after entering into an agreement, (i) a copy of the final text, (ii) a draft of an implementing bill, (iii) a statement of any administrative action proposed to implement the agreement and (iv) the supporting information. Then Congress votes up-or-down on the implementing bill. If Congress approves the implementing bill, it is enacted into law.

- As a result, Congress will have a maximum of 90 legislative days from formal introduction to consider the implementing bill.

Furthermore, USTR must consult regularly and upon their request with the Congressional Oversight Group (COG), formed in September 2002, as well as with the Senate Finance Committee, the House Ways and Means Committee, and other Committees that the President deems appropriate.

We highlight below these different steps as they were taken for the Singapore and Chile FTAs.

TPA Provision	90-Day Notification period of intention to initiate FTA negotiations	Environmental review	Employment Impact Review	Labor Rights Reports	ITC Reports on Economic Effects
Partners					
Chile	-USTR notified Congress on October 1, 2002[52]	-Initiated December 14, 2000 (65 FR 78253) -USTR requested comments on the draft environmental review by November 21, 2001 (66 FR 56366) -Released on July 16, 2003	-Initiated on October 21, 2002 (67FR 64692) -Released on July 16, 2003	-Initiated on February 26, 2003 -Comments due by March 28, 2003 (68 FR 8928) -Released on July 16, 2003	-Initiated on April 23, 2001 (66 FR 21180)[53] -Initiated on March 19, 2003 (68 FR 13324) -Hearing on May 1, 2003 was cancelled (68 FR 18673) -Released on June 9, 2003
Singapore	-USTR notified Congress on October 1, 2002[54]	-Initiated November 29, 2000 (65 FR 71197) -USTR requested comments on the draft environmental review by September 20, 2002 (67 FR 53035) -Released on July 16, 2003	-Initiated on October 21, 2002 (67 FR 64693) -Released on July 16, 2003	-Initiated on January 28, 2003 -Comments due by February 27, 2003 (68 FR 4239) -Released on July 16, 2003	-Initiated on February 19, 2002 (67 FR 8821)[55] - Initiated on March 21, 2003 -Hearing held on April 24, 2003 (68 FR 13952) -Released on June 9, 2003

52 The USTR announced its intention to initiate negotiations with Chile in the Federal Register on December 14, 2000 (65 FR 78253).

53 The ITC initiated an economic review of the elimination of tariffs on agricultural products in the U.S.-Chile FTA on July 9, 2002 (67 FR 45542)

54 The USTR announced its intention to initiate negotiations with Singapore in the Federal Register on November 29, 2000 (65 FR 71197).

55 ITC initiated an economic review of the elimination of tariffs on agricultural products in the U.S.-Singapore FTA on July 2, 2002 (67 FR 45543).

TPA Provision	90-Day Notification period of intention to enter into an FTA	Publication final text	Congressional Approval	Signing
Partners				
Chile	-President notified Congress on January 30, 2003	-USTR released the final text on June 6, 2003.	-On July 24, 2003, the U.S. House of Representatives approved the FTA (HR 2738) by a vote of 270-156 *(Please see W&C July 2003 Report)*. -On July 31, 2003, the U.S. Senate approved the FTA (S 1416) by a vote of 66-31*(Please see W&C 2003 Report).*	-USTR Zoellick and Foreign Minister Soledad Alvear signed the FTA on June 6, 2003. -President Bush signed the implementing bill of the FTA on September 3, 2003
Singapore	-President notified Congress on January 30, 2003	-USTR released the final text on May 6, 2003.	-On July 24, 2003, the U.S. House of Representatives approved the FTA (HR 2739) by a vote of 272-155 *(Please see W&C July 2003 Report)*. -On July 31, 2003, the U.S. Senate approved the FTA (S 1417) by a vote of 66-32 (*Please see W&C August 2003 Report)*.	-President Bush and Prime Minister Goh Chok Tong signed the FTA on May 6, 2003. -President Bush signed the implementing bill of the FTA on September 3, 2003

II. U.S. Conducts Negotiations with Morocco, Central America, SACU, and Australia; Announces Negotiations with Bahrain and Dominican Republic

Since the renewal of TPA, the U.S. also launched FTA negotiations with Morocco, Central America, the Southern African Customs Union (SACU), and Australia, and recently announced its intention to initiate negotiations with Bahrain and the Dominican Republic.

We highlight below the status of these FTA negotiations that the U.S. is conducting or has announced.

TPA Provision	90-Day Notification period of intention to initiate FTA negotiations	Environmental review	Employment Impact Review	Labor Rights Reports	ITC Reports on Economic Effects
Partners					
Morocco	-USTR notified Congress on October 1, 2002 -TPSC hearing held on November 21, 2002 (67 FR 63187)	-Initiated on November 22, 2002 (67 FR 70476)	-Initiated on February 7, 2003 -Comments due by March 28, 2003 (68 FR 6529)	-Initiated on April 21, 2003 -Comments due by June 5, 2003 (68 FR 19579)	-Initiated on September 13, 2002 -Hearing held on October 10, 2002 (67 FR 59312)
Central America	-USTR notified Congress on October 1, 2002 -TPSC hearing held on November 19, 2002 (67 FR 63954)	-Initiated on November 22, 2002 (67 FR 70475) -USTR requested comments on the draft environmental review by October 15, 2003 (68 FR 51822)	-Initiated on March 19, 2003 -Comments due by April 25, 2003 (68 FR 13358)	--	-Initiated on September 16, 2002 -Hearing held on October 18, 2002 (67 FR 59312)
SACU	-USTR notified Congress on November 4, 2002 -TPSC hearing held on December 16, 2002 (67 FR 69295)	-Initiated on March 13, 2003 (68 FR 12150)	-Initiated on May 7, 2003 -Comments due by June 6, 2003 (68 FR 24532)	--	-Initiated on November 20, 2002 -Hearing held on January 28, 2003 (67 FR 70757)

TPA Provision	90-Day Notification period of intention to initiate FTA negotiations	Environmental review	Employment Impact Review	Labor Rights Reports	ITC Reports on Economic Effects
Australia	-USTR notified Congress on November 13, 2002 -TPSC hearing held on January 15, 2003 (67 FR 76431)	-Initiated on March 13, 2003 (68 FR 12149)	-Initiated on May 8, 2003 -Comments due by June 6, 2003 (68 FR 24785)	--	-Initiated on December 20, 2002 -Hearing held on January 15, 2003 (67 FR 79149)
Partners					
Bahrain	-USTR notified Congress on August 4, 2003 -TPSC will hold a hearing on November 5, 2003 -Comments due by November 17, 2003 (68 FR 51062)	--	-Initiated on September 4, 2003 -Comments due by October 1, 2003 (68 FR 52622)	--	-Initiated on August 26, 2003 -ITC will hold a hearing on September 25, 2003 (68 FR 51301)
Dominican Republic	-USTR notified Congress on August 4, 2003 -TPSC will hold a hearing on October 8, 2003 -Comments due by November 2, 2003 (68 FR 51823)	--	-Initiated on September 4, 2003 -Comments due by October 1, 2003 (68 FR 52623)	--	-Initiated on August 22, 2003 -ITC will hold a hearing on October 7, 2003 (68 FR 50808)

	Next steps	Negotiating structure	Expected challenges
Partners			
Morocco	-A fourth negotiating round took place on July 21-25, 2003, in Washington. -USTR presented draft texts on agriculture, services, and market access for industrial goods. -A fifth round will be held at the beginning of October 2003, in Morocco. -The goal is to reach agreement by the end of 2003.	-USTR has scheduled 10 negotiating rounds in 2003, involving 11 negotiating groups: (i) textiles, (ii) market access, (iii) labor, (iv) environment, (v) IPR, (vi) government procurement, (vii) services, (viii) investment, (ix) e-commerce, (x) customs, and (xi) agriculture. -Negotiations progress on all fronts simultaneously. -The objective is to implement the FTA over 10 years, with "some areas of exception", such as agriculture, where a larger transition period is foreseen.	-Agriculture, services, and investment remain difficult issues that still have to be solved. -The most difficult issue will likely be agriculture.
Central America	-A sixth negotiating round took place on July 28-August 1, 2003, in New Orleans. -USTR nearly completed negotiations on e-commerce and customs administration. USTR also made proposals on investment, IPR, services, dispute settlement, rules of origin for textiles, market access for goods, and labor. -The goal is to reach agreement by the end of 2003.	-USTR has scheduled 9 negotiating rounds in 2003, involving 5 negotiating groups: (i) market access, (ii) investment and services, (iii) government procurement and IPR, (iv) labor and environment, (v) institutional issues such as dispute settlement -Central America is negotiating as a bloc. -The FTA will build on the FTA with Chile.	- Labor and environment; agriculture; rules of origin for textiles and apparel; IPR; liberalization of telecommunications in Costa Rica. -Labor and agriculture will likely be the last issues to be resolved.

	Next steps	Negotiating structure	Expected challenges
Partners			
SACU	-A second negotiating round took place on August 4-6, 2003 in Namibia. -USTR submitted initial proposals on agricultural and industrial trade, standards, customs, rules of origin, trade remedies, investment, and services. -A third round will be held on October 14-17, 2003, in Washington. SACU is expected to table text on services, SPS rules, customs, market access, TBT, and trade remedies. -A fourth round will be held in December in one of the SACU countries. -The goal is to reach agreement by the end of 2004.	-A large plenary group will lead the negotiations. Smaller negotiating groups will discuss specific issues, including (i) market access for agricultural and non-agricultural products, (ii) technical barriers to trade (TBT), (iii) customs, (iv) labor rights and environmental standards, (v) SPS measures, (vi) investment, (vii) IPR, (viii) services, (ix) e-commerce, (x) and dispute settlement. - A first phase of the negotiations will take place in 2003 and will deal with non-controversial issues such as market access, rules of origin, and SPS measures. A second phase will take place in 2004 and will deal with more difficult issues such as services, investment, government procurement, trade remedies, and IPR. -Special and differential treatment and trade capacity building will be included in the negotiations. -SACU will negotiate as a bloc.	-Agriculture; special and differential treatment; IPR; e-commerce; government procurement; industrial market access; investment.

	Next steps	Negotiating structure	Expected challenges
Partners			
Australia	-A third negotiating round took place on July 21-25, 2003, in Hawaii. -The negotiators tabled market access proposals. -A fourth round will be held on October 27-31, 2003, in Australia. -A fifth round will be held on December 1-5, 2003, in Australia. -The goal is to reach agreement by the end of 2003. Both sides aim to produce a draft agreement by Christmas for consideration by the Australian Parliament and the U.S. Congress in the New Year.	-There will be 17 negotiation groups, including: (i) agriculture, (ii) textiles, (iii) telecommunications, (iv) environment and labor, (v) industrial goods, (vi) investment, (vii) IPR, (viii) e-commerce. -The FTA will build on the FTA with Singapore.	-Agriculture; IPR; Australia's Pharmaceutical Benefits Scheme (PBS), which provides pharmaceutical subsidies. -Agriculture will likely be the toughest issue.
Bahrain	-Negotiations will start in January 2004.	--	--
Dominican Republic	-Informal discussions have already begun. USTR will launch formal negotiations in January 2004. -USTR hopes to reach agreement by March or April 2004, and then to integrate the FTA into CAFTA. -The goal is to submit the FTA and CAFTA to Congress by late April or May 2004.	-The FTA will build on the FTA with Chile. -The negotiations will focus on market access issues.	--

III. U.S. Considers Other FTAs

Numerous countries have proposed FTAs with the U.S., especially after the collapse of the Cancun WTO talks. Below we highlight some of the countries and the prospects of a bilateral/regional FTA with the U.S.

Middle East

On May 9, 2003, President Bush announced a plan to establish a U.S.-Middle East Free Trade Area (MEFTA) by 2013 (*Please see W&C May 2003 Report*). On June 23, 2003, USTR Robert B. Zoellick held a speech at the World Economic Forum (WEF) in Jordan in which he outlined the following steps that the U.S. would follow to realize MEFTA:

- Support active membership in the WTO;
- Expand the Generalized System of Preferences (GSP);
- Offer to negotiate Trade and Investment Framework Agreements (TIFAs);
- Offer to negotiate Bilateral Investment Treaties (BITs);
- Negotiate comprehensive FTAs;
- Provide technical and financial assistance.

At the same occasion, Zoellick commented on the possibility of a U.S.-Egypt FTA, stating that Egypt still "has some work to do", especially in the area of customs, before an FTA could be possible. Zoellick earlier characterized Egypt as a "strong candidate" for an FTA. Sources indicate that the real reason is U.S. disappointment over Egypt's failure to back the U.S. challenge in the WTO against the E.U. moratorium on Genetically Modified Organisms (GMOs).

Andean Community (Bolivia, Colombia, Ecuador, Peru)

On August 8, 2003, Zoellick met with Colombian President Alvaro Uribe in Colombia to discuss the challenges and opportunities involved in negotiating a U.S-Colombia FTA. Zoellick thereby pointed out that IPR and investment rules are aspects that Colombia has to work on prior to an FTA.

Zoellick indicated that consultations with Colombia will continue in October or November 2003, when a delegation from Colombia will meet with Assistant USTR Regina Vargo to review the U.S.-Chile FTA. Sources indicate that the USTR is expected to formally notify Congress of its intention to launch FTA negotiations with Colombia by the end of the year.

Reports indicate that Peru hopes to sign an FTA with the U.S. in the first half of 2004, while Bolivia and Ecuador also expressed their interest in an FTA. Sources indicate that Zoellick said that the U.S. is looking for a way to package Colombia and Peru together while "leaving the door open for Bolivia and Ecuador."

ASEAN (Association of South East Asian Nations: Burma, Brunei Darussalam, Cambodia, Indonesia, Laos, Malaysia, the Philippines, Thailand, Vietnam, Singapore)

On October 26, 2002, President Bush announced the Enterprise for ASEAN Initiative (EAI), which aims to create a "network of FTAs" with the ASEAN countries, using the FTA with Singapore as a model. As precursors to such FTAs, the U.S. has pledged its support for ASEAN members acceding to the WTO. Other preliminary steps would include negotiating Trade and Investment Framework Agreements (TIFAs) or Bilateral Investment Treaties (BITs) with the U.S.

Thailand currently seems the most likely candidate for an FTA. President Bush and Thai Prime Minister Thaksin Shinawatra stated on June 10, 2003 that they intend to work under the existing TIFA towards a possible FTA. Sources indicate that the Administration will decide on the negotiation of an FTA by the next Asia-Pacific Economic Cooperation (APEC) Leaders' summit in October 2003.

Sources indicate that the Philippines is also interested in an FTA with the U.S. Analysts speculate that Philippines President Gloria Arroya may have broached the subject with President Bush when they met in Washington on May 19, 2003.

Panama

Panama expressed disappointment that the U.S. did not include them in the CAFTA negotiations and urged the U.S. to ensure that they would also have an opportunity to use trade for development. On September 5, 2003, Panamanian Ambassador to the U.S. Roberto Alfaro Estripeaut stated at a meeting by the U.S. Chamber of Commerce that Panama hopes that the U.S. will formally announce the launch of negotiations on a U.S.-Panama FTA by the end of 2003.

Zoellick has stated that the U.S. may consider "docking" Panama to CAFTA, which means that Panama could be incorporated into the agreement at some point.

Korea

Korea has expressed an interest in an FTA, but the U.S. seems unresponsive. On January 9, 2001, the ITC instituted an investigation of the likely economic impact of an FTA with Korea (66 FR 4859), but made no recommendations on whether to initiate negotiations.

New Zealand

Despite New Zealand's interest in an FTA with the U.S., Zoellick has stated that the U.S. is not interested in an FTA with New Zealand at this time, partly because of strong opposition from U.S. farmers and partly because New Zealand did not support the war in Iraq. Analysts suggest that New Zealand's refusal to allow nuclear-powered ships in its waters has also contributed to U.S. reticence.

Sri Lanka

Zoellick has reportedly named Sri Lanka as a developing country advanced enough to qualify for an FTA with the U.S.

Taiwan

On February 11, 2002, the ITC instituted an investigation of the likely economic impact of an FTA with Taiwan (67 FR 6276), which they submitted to the USTR on October 17, 2002. The ITC held a public hearing on May 13, 2002, in conjunction with the study. The report made no recommendations on whether to initiate negotiations.

On June 2, 2003, House Majority Leader Tom DeLay (R-Texas) said that the House is committed to an FTA with Taiwan and will increase pressure on the Administration by passing a resolution (H. Con. Res. 98) that calls for such an FTA. However, a U.S.-Taiwan FTA is not a current priority for the Administration.

United Kingdom

On March 28, 2003, the Senate approved an amendment to the Senate version of the fiscal 2004 budget resolution (H Con. Res. 95), which would create room in the budget for the Congress to consider the negotiation of an FTA with the United Kingdom. The budget resolution is not binding legislation and does not require the President's signature. The Senate approved the amendment in light of the United Kingdom's support for the U.S.-led war against Iraq.

Most analysts agree that a U.S.-United Kingdom FTA is unlikely.

OUTLOOK

After World Trade Organization (WTO) Members failed to reach agreement on the Cancun Ministerial Declaration, which resulted in the collapse of the negotiations to bolster the Doha Development Agenda (DDA), the U.S. Administration made it clear that it will intensify its efforts to negotiate bilateral FTAs. Chairman of the Senate Finance Committee Charles Grassley (R-Iowa), supported the Administration's strategy and insisted that the U.S. would pursue agreements with countries that were ready to negotiate in Cancun.

USTR is using the Chile and Singapore FTAs as models (not exact templates) for the ongoing trade negotiations.

The timelines of the FTAs are important, because Congressional passage of FTAs becomes more difficult as the 2004 presidential elections draw nearer. Members of Congress have expressed concerns about proposed FTA partners, including labor and environmental violations and intellectual property rights violations. In addition, Members of Congress and some people in the business community question the commercial significance of some of the proposed agreements. In an election year, these issues likely would become politicized and, therefore, complicate congressional passage.

Timelines of current FTA negotiations also affect future negotiations. USTR is a relatively small agency and cannot accommodate all the requests from countries that want to negotiate with the U.S. The conclusion of one set of negotiators frees USTR resources to negotiate with other countries.

Panama Hopes U.S. Will Announce FTA Negotiations by the End of the Year; U.S.-Dominican Republic FTA Will Focus on Market Access Issues

SUMMARY

On September 5, 2003, Panamanian Ambassador to the U.S. Roberto Alfaro Estripeaut stated at a meeting by the U.S. Chamber of Commerce that Panama hopes that the U.S. will formally announce the launch of negotiations on a U.S.-Panama FTA by the end of 2003.

At the same event, the Ambassador of the Dominican Republic to the U.S. Hugo Guiliani Cury indicated that the U.S. and the Dominican Republic will launch formal FTA negotiations in January 2004. The negotiations will focus on market access issues and will conclude by March or April 2004, after which the FTA will be integrated into CAFTA. The final agreement would then be submitted to Congress in late April or May 2004.

ANALYSIS

On September 5, 2003, the U.S. Chamber of Commerce ("Chamber") hosted a discussion on the prospects for the addition of the Dominican Republic to the U.S.-Central America Free Trade Agreement (CAFTA) negotiations and its impact on a possible Panama Free Trade Agreement (FTA). The speakers included the Ambassador of Panama to the U.S. Roberto Alfaro Estripeaut and the Ambassador of the Dominican Republic to the U.S. Hugo Guiliani Cury.

We highlight their comments below.

I. Panama Aims to Conclude Separate Agreement Based on the U.S.-Chile FTA

Estripeaut stated that, among other things, liberalized market access, transparency in the services sector, and high-quality customs regulations, intellectual property rights (IPR) protection, and labor and environmental standards make Panama a good candidate for an FTA. Panama does not have a large textile and apparel or agriculture sector and does not compete with the U.S. in those areas.

Estripeaut noted that Panama and the U.S. have been discussing a possible FTA "for the last six months", and that in June 2003, United States Trade Representative (USTR) Robert Zoellick offered Panama the option of being "docked into" CAFTA. Estripeaut said however that because of its "unique" relationship with the U.S., Panama prefers to negotiate a separate FTA, using the recently concluded U.S.-Chile and U.S.-Singapore FTAs as a framework.

II. U.S.-Dominican Republic FTA Negotiations Will Focus on Market Access Issues

Cury said that the Dominican Republic and the U.S. already started informal negotiations, and will launch formal negotiations in January 2004.

He pointed out that the FTA negotiations will focus on market access issues, using the U.S.-Chile FTA as a framework. The Dominican Republic agrees with 80% percent of the text of the U.S.-Chile FTA and hopes to work away the remaining differences when the formal negotiations begin.

OUTLOOK

Estripeaut said that the U.S. and Panama will have further consultations in October, 2003, where Panama will propose its ideas for an FTA. He stated that Panama hopes that the U.S. will formally announce the negotiation of an FTA by the end of the year. Negotiations would then likely begin by March 2004, and conclude by the end of 2004.

Cury thought the negotiations will conclude in March or April 2004, after which the U.S.-Dominican Republic FTA will be integrated into CAFTA. The final agreement would then be submitted to Congress in late April or May 2004.

Senate Appropriations Bill Would Prohibit Negotiation of Trade Agreements with Temporary Entry Provisions

SUMMARY

On September 4, 2003, the Senate Appropriations Committee unanimously approved the Commerce-Justice-State (CJS) Appropriations Bill (S.1585), which includes an amendment offered by Senator Dianne Feinstein (D-California) that would prohibit the Office of the US Trade Representative (USTR) from negotiating free trade agreements (FTAs) "contain[ing] provisions relating to the entry of foreign nationals into the United States."[56] Representative Steve King (R-Iowa) proposed a similar amendment (H.AMDT.290 to H.R.2799) in the House during consideration of the CJS Appropriations Bill in late July, however that amendment was withdrawn.

Some analysts worry that, if approved, the Feinstein amendment would set a precedent for Members of Congress to use restrictions on appropriations to "negotiate" FTAs. Members of Congress essentially could demand certain provisions are met by holding funds necessary to implement the agreement hostage to their individual concerns. These restrictions would hamper the ability of the USTR to negotiate.

ANALYSIS

Congressional concern over the inclusion of temporary entry provisions in trade agreements surfaced in July during consideration of the Chile and Singapore FTAs. At one point, House Judiciary Chairman James Sensenbrenner (R-Wisconsin) stalled consideration of the FTAs because of provisions that would have created a new class of temporary visa for workers from Chile and Singapore. An 11th hour amendment offered by Representative Peter King (R-New York), and approved by USTR converted the proposed visas from a new class (W) to the existing H-1B visa program.[57] (*Please see W&C July 2003 Report*)

Bipartisan Condemnation of Changes in US Immigration Laws

Despite the eventual adoption of the two FTAs with provisions for temporary workers, members from both the House and Senate have warned the USTR against including such measures in future agreements. The House Judiciary Committee issued its reports on the Chile and Singapore FTAs with stern warnings to the USTR that future FTAs should not include changes to US immigration laws.[58] Democrats and Republicans alike have argued that constitutional authority over immigration matters is vested with the Congress, and should not be left to trade negotiators. Trade unions have also rallied against work visas in FTAs.

[56] S. 1585, Title II, Section 214 (CJS Appropriations Bill)

[57] Under the H-1B Visa Program, the US issues temporary work permits to aliens, approximately 65,000 for fiscal year 2004, who fill positions that cannot be filled by American workers.

[58] House Report 108-224 (Part II) p. 204.

USTR and Some In Congress Defend Movement of Professionals

The USTR, and some in Congress have defended immigration provisions within FTAs. Representative Phil Crane (R-Illinois) spoke against the King amendment to the CJS Appropriations Bill arguing that the mobility of professionals is essential "to competitive markets for both suppliers and consumers."[59] The USTR has also defended the provisions arguing that such programs are based on reciprocity and ensure access by US professionals to foreign countries.[60]

Immigrations Related Provisions in FTAs Not Unprecedented

Outside observers have noted that the movement of persons is recognized in 1994 WTO General Agreement on Services. Previous US FTAs, including those with Canada and Mexico have also included provisions for foreign temporary workers to enter the US.

OUTLOOK

During the "mock markup" of the Chile FTA, House Judiciary Committee members asked representatives of the USTR if proposed FTAs with Bahrain, Morocco, and Central America would be modeled on the Chile and Singapore FTAs. Ralph F. Ives, assistant USTR for Southeast Asia and the Pacific said that the USTR "has heard very clearly and understands the strong concerns of this committee and other members of Congress," and will "examine those concerns in terms of how we proceed with future FTAs."

Congressional consideration of the Singapore and Chile FTAs did not generate much debate. They are small open economies and most analysts consider labor and environmental laws in these countries to be good. Congress approved the FTAs with these countries, despite opposition to the temporary entry provisions, largely due to the commercial benefits.

However, the inclusion of temporary entry provisions in future FTAs would further complicate congressional passage of agreements that already are very contentious. Members of Congress and labor groups have voiced concerns about labor and environmental violations in many of the countries negotiating FTAs with the US, most notably the Central American countries. In addition, upcoming FTAs, such as the Central America and South Africa FTAs, are not expected to be as commercially significant as the Singapore and Chile FTAs. Therefore, Members are not as likely to agree to temporary entry provisions in the upcoming FTAs.

Some analysts worry that, if approved, the Feinstein amendment would set a precedent for Members of Congress to use restrictions on appropriations to "negotiate" FTAs. Members of Congress essentially could demand certain provisions are met by holding funds necessary to implement the agreement hostage to their individual concerns. These restrictions would hamper the ability of the USTR to negotiate.

[59] Congressional Record, July 22, 2003, H7288 – p. 1745.

[60] Office of the US Trade Representative, "Trade Facts – Chile and Singapore FTAs: Temporary Entry of Professionals," July 21, 2003, *available at* http://www.ustr.gov/new/fta/Chile/2003-07-21-temp_entry.pdf.

ITC Report Concludes NAFTA and Other FTAs Contributed to U.S. Growth

SUMMARY

The International Trade Commission (ITC) released a report in August 2003 entitled "The Impact of Trade Agreements on the U.S. Economy". The report concludes that trade agreements were only one of many factors that contributed to U.S. growth in the past twenty years. The five trade agreements analyzed in the report, including NAFTA, have had a positive impact on the U.S. economy.

The report serves as a useful tool for Members of Congress to evaluate U.S. trade policy, especially given the TPA requirements for congressional consultations. The report provides further evidence that multilateral trade negotiations benefit the U.S. economy more than bilateral and regional negotiations.

The full report is available at www.usitc.gov.

ANALYSIS

I. Background

Section 2111 of the Trade Act of 2002[61] established that the ITC should report to the U.S. Congress on the effects of trade agreements on the U.S. economy.[62] As a result, the ITC study analyzes the following topics:

- Negotiation of trade agreements under Trade Promotion Authority (TPA)
- Economic changes in the U.S. since the beginning of the Tokyo Round
- Overall effects of trade liberalization on the U.S. economy
- Overall effects of trade liberalization on 10 different U.S. industry-sectors
- The impact of the North American Free Trade Agreement (NAFTA) on U.S.-Mexico trade

The ITC received comments from more than 22 industry associations, labor unions, and research organizations. Trade agreements supporters' included representatives of electrical and pharmaceutical manufacturers, and manufacturers as a whole. The associations criticizing the agreements were mainly from import-competing sectors such as steel, ceramic tile, and tuna.

[61] The Trade Act of 2002 reinstated fast track authority and approved other procedures such as Congressional oversight of trade negotiations.

[62] The ITC researched the effects of five trade agreements: the Tokyo Round, the Uruguay Round, the U.S.-Israel FTA, the U.S.-Canada FTA, and the North American Free Trade Agreement (NAFTA)

II. Overall Findings

The ITC report concluded that:

- Trade agreements were one of several factors affecting U.S. growth
- Three additional factors affected U.S. growth: (i) U.S. trade policies, (ii) technological innovation, and (iii) demographic changes.
- Multilateral agreements –the Tokyo and Uruguay Round- impacted more the U.S. economy than preferential trade agreements.
- Trade growth in the United States has not been uniform. Trade with countries such as China or Mexico has grown much more rapidly than with other nations. Likewise, trade in U.S. sectors has grown at different rates.
- Between 1974 and 2001, the value of U.S. exports and imports grew from $0.5 trillion to $2.5 trillion.
- The value of exports has grown fastest in the following sectors: (i) machinery and equipment, (ii) transportation equipment, (iii) chemicals sectors, and (iv) miscellaneous manufacturers.
- Trade agreements have not been a determinant factor in increasing the wage gap between skilled and unskilled workers in the United States.
- Trade agreements, along with additional factors mentioned above raised U.S. GDP per capita and productivity growth. Between 1974 and 2001, GDP per capita rose from $19,163 to $32,352 while labor productivity in manufacturing increased 132 percent in the same period.

III. Effects On The U.S. Machinery And Electronics Sector

The effects of the five trade agreements on the U.S. machinery and electronics sector are:

- Other factors rather than the five trade agreements explain growth in production and trade in the electronics and machinery sector.
- Four factors contributed mainly to the sector's growth: (i) a considerable growth in demand, (ii) the development of new technologies, (iii) privatization and deregulation of the telecommunications industry, and (iv) the evolution of wireless communications and Internet services.
- With the exception of the U.S.-Israel FTA, all four agreements had a moderate but positive effect on the U.S. machinery and electronics sector growth.

- During 1991-2000, U.S. shipments of machinery and electronics increased at an annual rate of 2.5 percent (from 488.1 billion to $833.5 billion).

- In 2001, the value of shipments fell 18 percent due to the slowdown of the U.S. economy.

- Production increases in the sector were matched by gains in labor productivity, so total employment for electronics and machinery decreased from 3.7 million in 1978 to 3.6 million in 2001.

- The electronics sub sector –electronic components, computer and communications equipment had a significant growth in output and productivity since the implementation of the Tokyo Round Agreements in 1980.

- The real value of electronic component shipments quadrupled between 1978 and 2000, while the real value of communications, office, and computer equipment tripled.

IV. NAFTA Effects On U.S.-Mexico Trade

The impact of NAFTA on U.S.-Mexico trade can be summarized as follows:

- Total trade among NAFTA partners increased by approximately 128 percent, from $297 billion in 1994 to $676 billion in 2000.

- Reductions in U.S. and Mexican tariffs under NAFTA increased import shares in both countries. During 1990-2001, one third of the growth in the Mexican share of U.S. imports is attributed to U.S. tariff reductions and preferences under NAFTA. The ITC report also suggests that Mexican tariff reductions under NAFTA impacted significantly on U.S. shares of Mexican imports.

- Import shares increased more in industries with larger NAFTA tariff preferences. ITC estimates suggest that the U.S. share of Mexican imports increased most in the sectors with larger NAFTA tariff preferences towards U.S. goods. Those sectors were miscellaneous manufacturers, textiles, apparel, and footwear.

OUTLOOK

The Bush administration and supporters of trade liberalization in the U.S. Congress likely will welcome the conclusions of the ITC report. The fact that five trade agreements have all had a positive impact on the U.S. economy could strengthen domestic support for current trade negotiations.

The report could influence some U.S. legislators who have not yet formed concrete opinions on U.S. trade policy. However, since legislators will concentrate on the liberalization effects on their constituents, instead of the overall impact of trade liberalization, the report's findings are unlikely to alter the opinions of legislators in domestic industries adversely affected by trade liberalization.

Customs

FDA to Issue Final Rule on Registration of Food Facilities Under the Bioterrorism Act by October 2003

SUMMARY

The U.S. Food and Drug Administration ("FDA") indicated recently that it intends to implement Section 305 of the Public Health Security and Bioterrorism Preparedness and Response Act of 2002 (hereinafter "Bioterrorism Act" or "Act") on schedule by October 10, 2003. Section 305 of the Act requires that domestic and foreign facilities that "manufacture, process, pack, or hold food for human or animal consumption" register with the FDA, and no later than December 12, 2003. Currently, the FDA is reviewing public comments on its proposed registration procedures, including on the Draft Food Facility Registration Form ("the Form") – the registration form that food facilities will be required to submit to the FDA.

Facilities that fail to register by December 12, 2003, can be subject to civil and criminal actions. For example, food from facilities that fail to register can be held at the port of entry. Moreover, if facilities and their agents provide false information, they can be subject to fines, imprisonment or both. The FDA estimates that about 400,000 domestic and foreign facilities must register by the deadline. Some U.S. trading partners, however, have argued that the process appears burdensome and might violate WTO disciplines on technical barriers.

ANALYSIS

I. FDA Draft Rule on Registration of Food Facilities

The FDA on February 3, 2003, issued draft regulations to implement Section 305[63] and expects to publish its final rule by October 10, 2003. Currently, the FDA is in the final stages of reviewing public comments on the registration procedures, including on the Draft Food Facility Registration Form ("the Form"). The FDA has indicated that it has received "favorable feedback" regarding the proposed registration process and has encouraged most entities to register through the Internet starting this autumn. No registrations will be accepted before the registration system is operational in October 2003. There will be no registration fee. The FDA estimates that over 400,000 facilities will be required to register (e.g. 202,000 domestic and 205,000 foreign).

II. Designation of a U.S. Agent Required

The Bioterrorism Act requires foreign exporters to designate a U.S. agent as stipulated by Section 7 of the Form. Recently, some private companies have advertised their services to register domestic and foreign facilities. The FDA has stated that it does not endorse these services, and that registration should not be done prior to the issuance of a final rule in October 2003.

[63] *See* 68 FR 5378, 3 February 2003.

Section 305 amends Section 415 of the Federal Food, Drug, and Cosmetic Act (21 U.S.C 341 et seq.) and requires that an "owner, operator or agent" of a "facility" register with the FDA. Facility is defined as "any factory, warehouse, or establishment of an importer that manufactures, processes, packs, or holds food." Regarding foreign facilities, the regulation states "for a foreign facility, the owner, operator or agent in charge of the facility shall submit a registration to the Secretary and shall include with the registration the name of the United States agent for the facility."

The terms "United States Agent" is vaguely defined in the regulation as "an entity designated by a foreign facility as its agent in charge for purposes of registering the foreign facility." The regulation does not clarify who should act as an agent for foreign facilities. The FDA has indicated that this matter will be clarified in the final rule.

III. Penalties for Failure to Register and for Providing False Information

Facilities that fail to register by December 12, 2003, can be subject to civil and criminal actions under Section 301 of the Act, and as indicated in Section 12 of the Form. For example, food from these facilities can be held at the port of entry. Generally, the sanctions include fines and imprisonment up to 5 years, or both. For example, transfer of certain biological agents and toxins to a person who the transferor knows or has reasonable cause to believe is not registered as required by the law, or knowing possession of certain biological agents or toxins for which the possessor has not obtained registration required by the law, are punishable by a fine, or imprisonment up to 5 years, or both.[64] The specific guidelines as to which penalty should be administered, can be found in the Federal Sentencing Guidelines.

The authority for assessing penalties is Title XVII of United States Code Section 1001 ("Crimes and Criminal Procedure"). 18 U.S.C. 1001 provides that penalties be assessed if individuals or organizations make false statements on matters within the jurisdiction of the government; penalties include monetary fines, imprisonment up to 5 years, or both. Pursuant to 18 U.S.C. 3571, the amount of the fine depends on whether the person providing the false information is an individual or an entity, and on whether death resulted as a consequence of the offense. Fines administered to organizations (between $10,000 for a Class B or C misdemeanor and $500,000 for a felony) are generally double the amount administered to individuals. For example, while the top fine for a felony or misdemeanor resulting in death committed by an individual is $250,000, the penalty for the same type of crime for organizations is $500,000.

OUTLOOK

The FDA has indicated that it has received generally positive feedback regarding its proposed registration procedures for foreign and domestic food facilities. U.S. trading partners, however, have been critical of the Bioterrorism Act's requirements. The EU and China, among others, have asserted that the new procedures would be burdensome to their exporters, and possibly in violation of WTO disciplines on technical barriers. Notwithstanding, the FDA intends to proceed on schedule and issue its final rule by October 10, 2003. If the registration

[64] See, e.g., Sections 231 of the Bioterrorism Act regarding Certain Biological Agents and Toxins.

process proceeds as the FDA anticipates, most food facilities will register through the Internet and prior to the deadline of December 12, 2003. Nevertheless, the FDA has a challenging task ahead to compel about 400,000 facilities to register within a period of two months.

Customs Publishes Final Rule of Definition of "Customs Business"

SUMMARY

On August 11, 2003, the Bureau of Customs and Border Protection ("Customs") published its final rule amending Section 111.1 of the Customs Regulations as it pertains to the definition of "customs business." Section 111.1 implements Section 641 of the Tariff Act of 193, as amended, which provides that a person must hold a valid customs broker's license and permit in order to transact customs business on behalf of others.

The final rule becomes effective on September 10, 2003.

ANALYSIS

I. Background

On August 11, 2003, the Bureau of Customs and Border Protection ("Customs") published its final rule amending Section 111.1 of the Customs Regulations as it pertains to the definition of "customs business." Section 111.1 implements Section 641 of the Tariff Act of 193, as amended, which provides that a person must hold a valid customs broker's license and permit in order to transact customs business on behalf of others. Section 111.1 of the regulations defines what is "customs business."

The former definition of "customs business" was quite broad and essentially included all activities as they relate to the preparation and filing of documentation with Customs. With the advent of the Customs Modernization Act (Mod Act) in 1993, which shifted certain responsibilities to the importer, the definition of "customs business" began to become somewhat outmoded as companies strove to find efficient ways to meet the new standards. Under the Mod Act, an importer of record is required to exercise "reasonable care" in connection with entry requirements (19 USC 1484). One of the primary considerations in the exercise of "reasonable care" has been the use of Customs experts. As a result, many importer groups consisting of a parent corporation and one or more subsidiary corporations chose to centralize their in-house customs experts into one corporate entity and to make the services of those experts available to the group as a whole. The centralization of these experts was considered to be more cost effective.

Unfortunately, however, Customs consistently took the position that many activities performed under this type of arrangement would involve the transaction of "customs business," which would require a broker's license. Customs reasoned that parent and subsidiary corporations were separate legal persons, and therefore, the parent or subsidiary corporation in which the customs expert resides would be transacting customs business not solely for its own account, but rather on behalf of another, and therefore requiring a customs broker's license.

The importing community prevailed upon Customs that the agency's position was an impediment to the exercise of reasonable care, and in October 2002, Customs proposed to amend the definition of "customs business" and the basic rules regarding when a person must obtain a customs broker's license and permit. Specifically, the proposed rule amended the definition of

"customs business" to exclude "corporate compliance activity," and added a new definition for that term.

II. Discussion

Although the amendment of Section 111.1 was intended to provide an exception for the conduct of corporate compliance activities without a customs broker's license and permit, the amendment does not specifically list those activities which are permitted under the exception.

The new definition for 'corporate compliance activity' provides in pertinent part that:

"Corporate compliance activity" means activity performed by a business entity to ensure that documents for a related business entity or entities are prepared and filed with Customs using "reasonable care", but such activity does not extend to the actual preparation or filing of the documents or their electronic equivalents.

(The term "related business entity or entities" encompasses a business entity that has more than a 50% ownership interest in another business entity, a business entity in which another business entity has more than a 50% ownership interest, and two or more business entities in which the same business entity has more than a 50% ownership interest. References in the proposed rule to "voting shares" have been replaced with more general references to "ownership interest" because voting shares are not the exclusive basis for determining the ownership level in a business.)

While Customs declined to provide a list of specific authorized activities within the regulations, its response to comments on the proposed rule lend some insight into the activities Customs may consider to be within the exception of "corporate compliance activity." In response to one comment, Customs stated that "related companies will be permitted to conduct any activities mentioned in the definition of "customs business," other than the actual preparation and filing of documents, so long as those activities fall within the definition of "corporate compliance activity." Customs implies that a related company can advise and consult on the preparation and filing of documents with Customs and potentially gather that information. Customs stated that corporate compliance activity precludes only the "actual preparation or filing of the documents or their electronic equivalent, and that "actual" means that the documents are those that will be filed with Customs.

When asked if it envisioned that responding to Customs Form 28 Requests for Information or Customs Form 29 Notices of Action, or preparing Post Entry Amendments, or preparing documents related to audits, etc., would be considered corporate compliance activity, Customs indicated that such responses would be prohibited under the exception, as customs business but that the agency could only make such a determination on a case-by case basis. However, Customs recognized the specific distinction, noted by one commenter, between assigning a Harmonized Tariff Schedule number to an inbound item and the review of internal classification databases. The former would be customs business and the latter is merely a corporate compliance activity.

Customs responses to comments also recognized the need to permit corporate compliance offices to communicate directly with the agency on behalf of a related company regarding the activities performed by that office to ensure reasonable care. However, Customs cautioned that such offices should be prepared to demonstrate their authority to represent the interests of the related company by means of a power of attorney or authorization letter.

Also, Customs noted that there are some specific instances where no customs broker's license would be required for filing documents on another company's behalf, such as those actions which specifically provide may be performed by an authorized agent, such as protests, ruling requests, and certain drawback documents.

Finally, to the extent that there exists administrative rulings contrary to the amended rule, Customs explained that those rulings would be considered modified or revoked without further action on Customs part.

OUTLOOK

Accordingly, the new rule provides that no customs broker's license or permit is required to perform corporate compliance activities on behalf of a related business entity. However, corporate compliance activities do not include the actual preparation and filing of documents with Customs or other activities that are inherently "customs business."

Twenty-eight comments were received by Customs regarding its proposal and relevant comments were incorporated into the final rule. The final rule becomes effective on September 10, 2003.

Customs Adopts Final Rule on Manufacturing Substitution Drawback; Updates List of International Organizations Eligible for Free Entry Privileges; Withdraws Proposal on Listing of Trademarks on Imported Merchandise

SUMMARY

We want to alert you to the following customs developments:

- On August 22, 2003 the Bureau of Customs and Border Protection (CBP), Department of Homeland Security (DHS), adopted as a final rule an amendment on the Manufacturing Substitution Drawback: Duty Apportionment. The final rule is effective from August 22, 2003.

- On August 22, 2003 the CBP updated its list of international organizations eligible for visa-free entry. The final rule is effective from August 22, 2003.

- On August 22, 2003 the CBP published its decision to withdraw a proposed rule that would require importers to provide on their invoices a listing of all trademarks appearing on imported merchandise and its packaging. As of August 22, 2003, the proposed rule is withdrawn.

ANALYSIS

I. Customs Adopts Final Rule on Manufacturing Substitution Drawback

On August 22, 2003 in the Federal Register (68 FR 50700), the Bureau of Customs and Border Protection (CBP), Department of Homeland Security (DHS), adopted as a final rule an amendment on the Manufacturing Substitution Drawback: Duty Apportionment. The interim rule was published on July 24, 2002, and amended the methodology for calculating duty drawback where import merchandise contains chemical elements used in manufacture or production of articles that are either exported or destroyed under custom supervision.

Recent court decisions held that chemical elements contained in an imported material that is subject to an *ad valorem* rate of duty may be designated as same kind and quality merchandise for drawback purposes. The final rule provides a methodology for calculation of the apportionment eligible for duty drawback.

II. Customs Updates List of International Organizations Eligible for Free Entry Privileges

On August 22, 2003 in the Federal Register (68 FR 50698), the CBP updated its list of international organizations eligible for visa-free entry.

Public international organizations on the list are entitled to certain free entry privileges provided under provisions of the International Organization Immunities Act. The last update

was made in 1996. Since this time, certain organizations have received this privilege through several Presidential executive orders.

III. Customs Withdraws Proposal on Listing of Trademarks on Imported Merchandise

On August, 22, 2003 in the Federal Register (68 FR 50073), the CBP published its decision to withdraw a proposed rule that would require importers to provide on their invoices a listing of all trademarks appearing on imported merchandise and its packaging.

The rule was intended to deter counterfeit products and strengthen trademark protection laws. However, the CBP has determined, based on public comments and its own evaluation, that the proposed rule will not be an efficient and effective way to fight counterfeiting.

As of August 22, 2003, the proposed rule published on September 13, 1999 (64 FR 49423) is withdrawn.

OUTLOOK

The final rule on the Manufacturing Substitution Drawback, the updated list of international organizations eligible for visa-free entry, and the withdrawal of the proposal on the listing of trademarks on imported merchandise are effective from August 22, 2003.

GSP

USTR Announces Review of 2001 and 2002 Country Practice Reviews; US Extends Duty-Free Treatment for Israeli Agricultural Products

SUMMARY

On September 3, 2003, the Office of the United States Trade Representative (USTR) announced which of the 2001 and 2002 petitions it intends to review to determine whether applicant developing countries are in compliance with the eligibility criteria to receive benefits under the Generalized System of Preferences (GSP).

In a related event, President Bush on August 27, 2003 extended duty-free treatment for certain Israeli agricultural products to December 31, 2003. This duty-free treatment was previously scheduled to expire at the end of 2002.

ANALYSIS

I. USTR Announces Review of 2001 and 2002 Country Practice Reviews

On September 3, 2003, the Office of the United States Trade Representative (USTR) published a notice in the Federal Register (68 FR 52437), announcing which of the 2001 and 2002 petitions it intends to review to determine whether applicant developing countries are in compliance with the eligibility criteria to receive benefits under the Generalized System of Preferences (GSP).

The GSP program grants duty-free treatment to certain products from more than 140 designated developing countries and territories. The GSP was authorized by the Trade Act of 1974, and was renewed by the Trade Act of 2002.

The notice also sets forth the schedules for public comment procedures, the public hearing on these petitions, and other ongoing country practices reviews.

II. US Extends Duty-Free Treatment for Israeli Agricultural Products

On August 27, 2003, President Bush extended duty-free treatment for certain Israeli agricultural products to December 31, 2003. This duty-free treatment was previously scheduled to expire at the end of 2002.

The United States and Israel reached an agreement on agricultural trade in 1996, as part of the creation of a Free Trade Area; an agreement concluded in 1985. The duty-free treatment in the 1996 Agreement was renewed in 2001, and has been renewed again to the end of 2003. Both parties are trying to conclude a successor agreement on agriculture trade, and have decided to extend the existing benefits until another agreement is concluded.

OUTLOOK

The GSP Subcommittee will hold a hearing on October 7, 2003, and parties that intend to appear must notify the USTR by September 26, 2003. Parties can also submit comments after the hearing until October 31, 2003.

US-EU

EU, US, and Acceding Countries to Agree on Amendments to the Acceding Countries-US Investment Treaties

SUMMARY

At the beginning of September 2003 the European Commission authorized Commissioners Lamy and Verheugen to sign a Memorandum of Understanding (MOU) with the US and eight future Member States[65], which is expected to resolve the legal issues arising from the existing Bilateral Investment Treaties (BITs) between the US and those eight acceding countries. The EU has long warned that the BITs need to be amended or denounced, as some of their provisions are inconsistent with EU law. It now seems that the parties have reached a political agreement on most of the controversial issues. However, some matters, e.g. capital movements, still need to be negotiated. In addition to this, BITs that were concluded between the acceding countries and other countries such as Canada will also need to be revised.

ANALYSIS

Background

During the 1990's the governments of eight Central and Eastern European countries signed BITs with the US granting each other reciprocal National Treatment (NT) and Most Favored Nation (MFN) treatment. The BITs were signed for a period of ten years (the last one expiring in 2011), and accordingly stipulated that US investors must be treated the same way as domestic investors. This is now a matter of serious concern for the EU, which wants to prevent US investors from acquiring rights which the EC Treaty reserves solely to EC operators.

During the accession negotiations, the acceding countries willingly committed to "denounce or renegotiate treaties with third countries, which are incompatible with the EC law and to confirm that all agreements with third countries which they wish to maintain after accession are compatible with its EU obligations." They also undertook to keep the Commission informed of any steps they might take to analyse existing agreements, along with details of steps taken/to be taken to renegotiate or terminate any agreements incompatible with their EU obligations. These undertakings were also reiterated in the April 16, 2003 Act of Accession.[66]

[65] Bulgaria, Czech Republic, Estonia, Latvia, Lithuania, Poland, Romania and Slovakia.

[66] Article 6.10 Act of Accession: " To the extent that agreements between one or more of the new Member States on the one hand, and one or more third countries on the other, are not compatible with the obligations arising from this Act, the new Member State shall take all appropriate steps to eliminate the incompatibilities established. If a new Member State encounters difficulties in adjusting an agreement concluded with one or more third countries before accession, it shall, according to the terms of the agreement, withdraw from that agreement. »

Issues

The Commission considers that a number of provisions in the BITs are not compatible with EU law. According to the Commission, if the BITs are not amended, US investors will be able to benefit from Community subsidies, including funding under the Common Agricultural Policy (CAP), energy, telecommunications, services and audiovisual policies. The BITs will also limit actions which the European Council of Ministers may undertake to preserve the functioning of Economic and Monetary Union (EMU). Articles 57.2, 59 and 60 EC Treaty provide that in times of financial or economical difficulties the Council may impose temporary safeguard or other measures to limit capital movements between a Member State and third countries.

Finally, the Commission is concerned that if the BIT provisions are not amended, they will affect the prerogatives and the discretion of the EU institutions, including that of the Commission as guardian of the Treaty and the *acquis* (e.g. on the basis of Article 226 EC Treaty).

Memorandum of Understanding

The EU and the acceding countries have now announced they have negotiated a solution with the US which is expected to solve most of the incompatibility issues. However, it should be remembered that the MOU, which is due to be signed on September 22, 2003, is a political deal and has no international legal standing. Under the MOU, the candidate countries will have to ensure that their BITs comply with EU law by May 1, 2004 (for Bulgaria and Romania, by their target date for EU accession). In the MOU the parties propose solutions in all conflicting areas:

- **Sensitive sectors** – the MOU will make exceptions to the NT rule possible in agriculture, audiovisuals, securities, investment services and other financial services, fisheries, hydrocarbons, subsidies, transport (air carriers, inland waterways and maritime). Exceptions to MFN will be possible in agriculture, audiovisual and hydrocarbons.

- **Performance requirements** – the MOU proposes amendments to the BITs that will remove the restrictions on the ability of the signatories to impose performance requirements in the agricultural and audiovisual sectors. In addition, the MOU proposes that no performance requirement which is the condition for receipt of an "advantage" should be subject to the prohibition on performance requirements.

- **Capital movements** – the MOU acknowledges the need for a lasting solution to the conflict between EMU safeguard action[67] and the BIT provisions on capital movements, but does not propose any measures. This is because the EU and the US have not yet reached a satisfactory solution to these issues, and will continue negotiations. According to the MOU, if no solution is

[67] Articles 57.2 and 60 which allow the Council to take measures to limit movement of capital and payments to and from third countries.

reached in the medium term, the Commission could potentially initiate infringement proceedings.

- **Protecting existing investments** – the MOU proposes that only current (and not future US) investments should enjoy BIT protection under EU law for the period during which they would have enjoyed such protection assuming the BITs were terminated at the first opportunity, i.e. ten years. However, this rule will not cover the "sensitive sectors".

- The MOU also proposes solutions to issues regarding (i) future development of EU law, (ii) Article 48 EC Treaty and (iii) the regional integration clause in the BITs

Positive US Reaction

On September 3, 2003 the US Department of State released a letter endorsing the EU enlargement process and expressing satisfaction with the understanding reached. The letter states that the understanding will both maintain a positive investment environment in the acceding countries and further the objective of assuring compatibility between obligations under the BITs and the obligations of EU membership.

OUTLOOK

The MOU will be signed by representatives of the EU, the acceding countries concerned and the US on September 22, 2003. The deadline by which signatories of BITs have to implement the MOU proposals is April 30, 2004 for the first wave of acceding countries and, the respective date of accession for Bulgaria and Romania. Although some issues are still to be negotiated, the MOU is a major step forward in solving the issues raised by the BITs.

US-LATIN AMERICA AND FTAA

Mexico and US Clash Over Trade Issues

SUMMARY

US-Mexico trade disputes involving cement, oil tubing, steel sheeting, pork and high-fructose corn syrup (HFCS) and telecommunications have increased tension in the bilateral relationship.

On August 5, the Ministry of Economy filed formal panel requests at the World Trade Organization (WTO) protesting anti-dumping duties that the United States imposed on Mexican exports of cement, oil tubing and steel sheeting. The same day, the US Trade Representative (USTR) raised the possibility of raising a WTO complaint against Mexico for barriers to U.S. HFCS imports. Regarding the pork dispute, U.S. authorities believe that Mexico will delay until September the decision to accept or reject an antidumping petition filed by Mexican pork producers against U.S. imports, and will continue to monitor the situation closely. Moreover, a WTO panel will soon issue its findings in the U.S. complaint regarding access to Mexico's telecommunications market.

Meanwhile, Members of the U.S. Congress, including Senate Finance Committee Chairman Grassley (R-Iowa), have raised concerns in letters to both U.S. and Mexican officials criticizing Mexico's failure to implement its NAFTA commitments.

ANALYSIS

I. Increase in US-Mexico Bilateral and WTO Disputes

US-Mexico trade disputes have increased recently, and have involved a wide range of products and services, including steel, cement, HFCS, pork and telecommunications. The pork dispute is a direct result of the scheduled phase-out of NAFTA provisions. The cement dispute dates from the pre-NAFTA era and is not related to the Agreement's phase-out provisions. The HFCS dispute involves, among other things: (i) differences of opinion on the interpretation of NAFTA provisions regarding the amount of U.S. quotas on sugar imports from Mexico, and (ii) disagreement regarding the HFCS tax imposed by Mexico. The telecommunications dispute is a long-running struggle with Mexico's monopoly Telmex, and its barriers to the domestic market despite Mexico's liberalization commitments under the WTO Basic Telecommunications Agreement.

A. US – Antidumping Duties on Mexican Products

On August 5, the Ministry of Economy filed formal requests for WTO panels protesting anti-dumping duties that the United States has imposed on Mexican exports of cement, oil tubing, and steel sheeting. Mexico claims that the duties are not legitimate, and act as protectionist barriers to the U.S. market. For the past eight years, Mexican cement exporters have faced anti-dumping duties as high as 120 percent in the U.S. market. For the past several years, U.S. and

Mexican negotiators have met repeatedly in an effort to resolve the cement dispute, but have failed to reach an agreement. At the WTO Dispute Settlement Body (DSB) meeting on August 18, the US rejected all three panel requests. The WTO will establish formal panels when Mexico makes its second requests at the next DSB meeting on August 29.

B. U.S. High-Fructose Corn Syrup Exports

The US Trade Representative has raised the possibility of a formal WTO complaint against Mexico protesting Mexico's barriers to U.S. high-fructose corn syrup (HFCS). The USTR agriculture negotiator, Allen Johnson, suggested that the US aims to resolve the problem through formal negotiations, but will keep its options open at the WTO. Recently, U.S. senators from major corn-producing states have raised concerns about the HFCS issue with USTR officials.

C. Mexican AD Pork Petition

U.S. authorities believe that Mexico will delay until September 2003 the decision to accept or reject an antidumping petition filed by Mexican pork producers against U.S. imports. Since January of this year (coincidentally, also the date of scheduled NAFTA tariff phase-outs), U.S. government officials and industry representatives have pressured the Mexican government to reject the Mexican Pork Council antidumping petition against U.S. pork. Mexican officials currently are reviewing the Council's data before making a decision. Mexico's 15,000 pork producers enjoyed protection under NAFTA until December 31 2002. After December 31, competition increased significantly due to the removal of Mexican tariffs on pork imported from the US.

D. WTO Set to Rule on Telecommunications Dispute

The U.S. dispute against Mexico's telecommunications market at the WTO continues, and the panel is expected to issue a decision soon. The dispute is a challenge to Telmex, the entrenched monopoly and its interconnection charges, as well as the independence of Mexico's regulator Cofetel, among other issues. If the WTO panel rules in favor of the US (as expected), it will be difficult for the Mexican government to comply with the WTO findings given Telmex's political influence.

OUTLOOK

Thus far, U.S. and Mexican negotiators have failed to agree on solutions to the bilateral trade irritants, which have led to Mexico's recent WTO panel requests on U.S. antidumping actions, as well as U.S. recourse to the WTO regarding telecommunications and possibly HFCS. Nevertheless, negotiators on both sides will attempt to resolve other outstanding issues such as pork.

Many of the recent bilateral disputes deal with agricultural trade between Mexico and the United States. In fact, the pork dispute is directly related to NAFTA's mandate to remove Mexican tariffs on a range of agricultural products imported from the US as of January 2003. With the tariff elimination on key products (pork, potatoes, rice, and chicken) scheduled for this

year and up to January 2008, new agricultural disputes could arise. Since some Mexican producers will not be ready to compete with their American counterparts, at least not in the short term, they will continue demanding restrictions on the flow of U.S. agricultural products through trade remedies and other barriers.

In Mexico, the National Farm Accord left President Fox with little room to maneuver and open Mexico's agricultural market, as the Bush administration demands *(see W&C Report June 2003)*. The Accord, which has not been implemented yet, establishes that the Government must monitor agriculture imports and apply safeguards when necessary. Analysts argue that if the Accord is not implemented quickly (such as through new barriers), the Fox administration could face a new upsurge of protests. Public protests could further politicize the trade issues, which would make it more difficult for the Fox administration to soften its negotiating position.

Moreover, the trade disputes not only hinder the bilateral relationship, but also could affect future U.S. trade negotiations. Some Members of the U.S. Congress cite the U.S.-Mexico disputes as faults in U.S. trade policy. Members argue that the U.S. has failed to enforce effectively the agreements and, therefore, existing trade agreements harm U.S. companies and workers.

With trade issues taking a higher-profile on both sides, Presidents Bush and Fox might address these issues at the upcoming presidential meeting, scheduled for sometime during the Fall. High-level intervention at the presidential level could give a political boost to resolving current disputes as well as addressing future conflicts.

On a broader perspective, the U.S.-Mexico bilateral disputes, combined with concerns regarding China's compliance with its WTO accession and the U.S.-E.U. GMO dispute, all serve as ammunition for anti-liberalization forces in the U.S. to criticize U.S. trade policy. However, pro-liberalization forces note the trade agreements have established an effective dispute settlement system at the WTO to pressure countries like Mexico to comply with their commitments. Mexico could make the same argument as it seeks to expand its market share in the US for cement, steel and other products. In fact, the US is facing compliance difficulty at the WTO, including on WTO findings against the 1916 Act, the Foreign Sales Corporations, Byrd Amendment, among others.

Colombia and Dominican Republic FTAs Could Add Momentum to FTAA Negotiations

SUMMARY

On August 4, 2003 the United States Representative (USTR) sent a notice to the U.S. Congress announcing its intention to integrate the Dominican Republic into negotiations of the US-Central America Free Trade Agreement (US-CAFTA). Among the sectors that could benefit most from the US-CAFTA are: electrical power systems, refrigeration and telecommunications equipment.

On August 8, 2003, U.S. Trade Representative, Robert Zoellick met with the Colombian Minister of Trade Jorge H. Botero to discuss the possibility of negotiating an FTA. USTR sources reported that the Colombian Government is willing to eliminate all agricultural tariffs, which are a key concern of U.S. industries.

The Bush administration is using the bilaterals in the region to advance its "competitive liberalization" strategy, hoping that the bilaterals will provide momentum for the FTAA negotiations.

ANALYSIS

I. USTR Intends to Include Dominican Republic in CAFTA Negotiations

On August 4, 2003 the United States Representative (USTR) notified Congress that the Bush Administration is seeking to include the Dominican Republic in the Free Trade Agreement (FTA) that it is negotiating with Central America (CAFTA).[68] USTR cites that the sectors that will benefit most from the FTA are: electrical power systems, refrigeration and telecommunications equipment, building materials, computers, textile fabrics, food processing, and soybean meal.

The USTR intends to integrate the Dominican Republic with CAFTA for various reasons. The country is the fourth largest U.S. trading partner in Latin America and one of the fastest growing economies in the region. The country is already an important market for U.S. apparel, textile, and agricultural products. The Dominican Republic has also an attractive investment and tax regime due to recent reforms implemented in those two areas. Moreover, it has recently improved significantly its enforcement of patent protection.

The United States expects to negotiate specific market access commitments and eliminate restrictions in the following areas:

- Services (telecommunications, financial services, energy) and investment;
- Agriculture, fish and forestry;

[68] The five countries to be included in CAFTA are: Costa Rica, Guatemala, Honduras, El Salvador, and Nicaragua.

- Apparel and textiles;
- Customs matters, rules of origin and trade remedies;
- Intellectual property rights, and
- Environment and Labor

According to the USTR, integrating the Dominican Republic in CAFTA will add momentum to the negotiations of the Free Trade Agreement of the Americas (FTAA). The Dominican Republic is one of several countries that support hemispheric negotiations and trade liberalization at the WTO.

A number of U.S. legislators and industry associations have expressed their support to include the Dominican Republic in the FTA with Central America, most notably Rep. Rangel (D-New York), the Ranking Member of the House Ways and Means Committee – whose district is comprised of many citizens originally from the Dominican Republic.

In a related development, the U.S. International Trade Commission (ITC) on August 15, 2003, following a request from USTR, has instituted an investigation on the probable economic effects of the US-Dominican Republic FTA. The ITC will hold a public hearing in connection with this investigation on October 7, 2003. Details of the ITC investigation and scheduling of the public hearing was published in the Federal Register (68 FR 50808) on August 22, 2003.

II. USTR Discusses Possible FTA With Colombia

On August 8 2003, U.S. Trade Representative, Robert Zoellick met with the Colombian Minister of Trade Jorge H. Botero to discuss the possibility of negotiating an FTA. USTR sources reported that the Colombian Government is willing to eliminate all agricultural tariffs, which are key concerns of the U.S.

In the past few years, Colombian exports to the United States have benefited from the Andean Trade Preference Act (ATPA), which is due to expire in 2006. The FTA would give Colombia unlimited preferential access to the U.S. market, and far greater benefits than under the ATPA.

Colombia has worked closely with the United States in the FTAA negotiations and at the WTO. Several U.S. legislators have expressed their support for the Bush administration to conclude a trade pact with Colombia. The country accounts for more than 50 percent of U.S. exports to ATPA countries. As a result, Colombia offers strong economic arguments as well as political reasons, to be considered a candidate for an FTA.

OUTLOOK

The proposed FTA with the Dominican Republic and the possible U.S.-Colombia FTA would serve as more "building blocks" in the U.S. strategy to build support for regional and multinational negotiations through "competitive liberalization."

Critics contend, however, that the bilateral agreements are detracting attention and resources away from more meaningful multilateral negotiations. Critics characterize the bilaterals as "stumbling blocks" instead of "building blocks." Some Latin American countries may perceive that the U.S. is securing as many trade pacts as possible in case the FTAA negotiations fail, or the U.S. Congress does not support a final deal on the FTAA.

The success of the FTAA will largely depend on the Bush administration's commitment to trade liberalization at the regional and multilateral level. A successful negotiation of the most sensitive issues (e.g. agriculture) in CAFTA and in a future FTA with Colombia could prove that the U.S. is committed to hemispheric trade liberalization. Agriculture, for example is a difficult issue for the U.S., which would prefer to handle agriculture liberalization at the WTO. Nevertheless, additional FTAs between the U.S. and Latin American countries might pressure Brazil and others in the region to expedite FTAA negotiations.

US-ASIA

Congress Takes Aim At Currency Manipulation; China Chief Target

SUMMARY

Over the past ten days, three bills, H.R. 3058, S.1586, and S.1592, and one non-binding Senate resolution, S.Res 219, have been introduced in the US Congress to address alleged currency manipulation by the largest East Asian economies, notably China. While providing the President with a wide array of remedial action, all three bills contain language suggesting that "currency manipulation" has been an important factor in the loss of over 2.6 million American manufacturing jobs since early 2001. On a recent visit to Asia, Treasury Secretary Snow raised the issue of exchange rates with officials in China, however he failed to win any promises on the floating of China's currency the renminbi (RMB).

The introduction of multiple bills signals growing concern among lawmakers about the link between China and the loss of manufacturing jobs in the US, particularly with elections just over a year away. Trade lobby groups have also been discussing possible action to confront China's undervalued currency, and momentum is building. However, some analysts have cautioned that a floating RMB would not automatically correct the US trade deficit with China; reported at US$11.3 billion for July 2003.

ANALYSIS

The three bills introduced to address currency manipulation are broadly similar in that they suggest that distortions in exchange rates have been a factor in important factor in the loss of American manufacturing jobs. Furthermore, the bills make references to GATT provisions, and Section 301 of the Trade Act (1974) to justify action domestically and in international forums to counter China's undervalued currency.[69]

Where the bills diverge is in the proposed remedial actions to be taken by the President. We review here the actions contemplated by the three bills:

I. Schumer Bill (S. 1586) Seeks to Impose New Tariffs

Under S.1586, sponsored by Senators Schumer (D-New York), Bunning (R-Kentucky), Graham (R-S. Carolina), Dole (R-N. Carolina), Durbin (D-Illinois), and Bayh (D-Indiana), the Secretary of the Treasury and the USTR are given 180 days to essentially negotiate the floating of the RMB. Should the President fail to certify this development within 180, a **27.5% ad valorem tariff** would be automatically applied to all Chinese goods, in addition to existing tariffs. Although not as fast acting as the House legislation, the Schumer bill is equally as harsh.

[69] Section 301 of the Trade Act of 1974 provides the United States with the authority to enforce trade agreements, resolve trade disputes and open foreign markets to U.S. goods and services. Section 301 is the principal statutory authority under which the United States may impose trade sanctions on foreign countries that either violate trade agreements or otherwise maintain laws or practices that are unjustifiable and restrict U.S. commerce.

II. Fair Currency Enforcement Act: A Lot of Reports and a Tempting Escape

Of the three bills recently introduced on currency manipulation the Fair Currency Enforcement Act (S.1592), introduced by Senator Lieberman (D-Connecticut), provides for the most number of reports to be filed, and gives the President a valuable escape from taking action. Within 90 days of enactment, the President must conclude bilateral and multilateral negotiations with the most egregious currency manipulators (i.e. China and Japan) to end the practice. Additionally, the International Trade Commission and the US Trade Representative are required to submit reports within 90 days that assess the injury suffered by the US resulting from currency manipulation, strategies for enforcing trade agreements, and strategies for promoting US manufacturing abroad.

Should negotiations fail to produce an end to currency manipulation, the Lieberman bill would require the President to institute Section 301 and 406 proceedings against those countries that continue to manipulate their currency.[70] However, the President may decline to institute such proceedings and elect to explain to Congress within 120 why he has failed to do so.

III. The CHINA Bill: Bring on the Tariffs, But How Much?

The House bill, sponsored by Representative English (R-Pennsylvania), H.R. 3058, known as the Currency Harmonization Initiative through Neutralizing Action (CHINA) Act would require the Treasury Secretary to report to Congress within 60 days on whether or not China is manipulating its currency, and if so by how much in percentage terms. Should manipulation be found, the CHINA Act would impose an additional tariff on all Chinese goods equal to the percentage manipulation reported by the Treasury Secretary. The CHINA Act contains the shortest timeline for action of the three bills introduced, and makes no provisions for negotiations.

OUTLOOK

Congress is not the only source of potential action on currency manipulation by China. The Coalition for a Sound Dollar continues to raise money to file an ITC complaint under Section 301 of the Trade Act (1974). The Coalition, comprised of 85 member companies, has urged the Administration to take a tougher line with China and Japan over currency manipulation. Both the Coalition and the National Association of Manufacturers have indicated that a Section 301 challenge is not imminent.

American and European officials have expressed opposition to using the World Trade Organization (WTO) as a vehicle for settling disagreements over exchange rate polices. At a September 4, 2003 meeting, both Robert Zoellick and European Trade Commissioner Pascal Lamy said they had raised the matter with the Chinese, and acknowledged that the WTO as presently constituted would not be effective in dealing with the situation.

[70] Section 406 of the Trade Act includes special provisions for the US to redress trade disputes with China under the terms of the United States-China Bilateral Agreement on World Trade Organization Accession.

Capitol Hill analysts are expressing doubts about whether any of the bills will make serious inroads in Congress, despite widespread concern over the loss of manufacturing jobs. Concern over China's currency has been likened to Congressional Japan bashing in the 1980s. While a Senate resolution encouraging the Treasury Secretary's efforts to address the issue is likely to make it to the floor, the Administration could pressure Republicans in Congress to back off the three bills, especially given China's important role in dealing with North Korea.

Witnesses appearing before a Senate Foreign Relations committee hearing on September 11, 2003 cautioned that China's adoption of a floating exchange rate would not cure America's growing trade deficit with China. Nicholas Lardy of the Institute for International Economics warned Senators that China's banking system is ill prepared to cope with a floating exchange rate, and that such a move could lead to further depreciation of the RMB.[71] All the witnesses before the panel agreed that something has to be done, however the hearings were dominated be a sense of helplessness.

[71] The full testimony of Nicholas Lardy can be found at http://www.iie.com/publications/papers/goldstein0903.htm

ANNEX: COMPARISON OF CURRENCY MANIPULATION LEGISLATION

H.R. 3058 Introduced September 10, 2003	S. 1586 Introduced September 5, 2003	S. 1592 Introduced September 8, 2003
SPONSORS		
English (R-Pennsylvania)	Schumer (D-New York), Bunning (R-Kentucky), Graham (R-S. Carolina), Dole (R-N. Carolina), Durbin (D-Illinois), Bayh (D-Indiana)	Lieberman (D-Connecticut)
COMMITTEE OF JURISDICTION		
Ways and Means	Finance	Finance
COUNTRIES TARGETED		
China	China	All countries "engaged most egregiously in currency manipulation." Specifically names China, Japan, South Korea and Taiwan in the Findings.
DEFINITION OF CURRENCY MANIPULATION		
No specific definition offered. Cites Article XV of the GATT (1994) in findings.	No definition offered. States that China's currency should be valued "in accordance with accepted market based trading policies."	1. Large-scale manipulation of exchange rates by a nation in order to gain an unfair competitive advantage as stated in Article IV of the Articles of Agreement of the IMF; 2. Sustained, large-scale currency intervention in one direction, through mandatory foreign exchange sales at a nations central bank at a fixed exchange rate; or 3. Other mechanisms, used to maintain a currency at a fixed exchange rate relative to another currency.
KEY FINDINGS		
Estimates that the trade deficit between China and the US will grow to $120 billion in 2003.	According to economists, the renminbi (RMB) is undervalued by 15 – 40%	Since July 2000, nearly 90% of job losses in the US, totaling 2.7 million, have come from the

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the US will grow to $120 billion in 2003. US imports from China are growing twice as fast as China's imports from the US.	undervalued by 15 – 40% Since 1998, the US trade deficit with China has grown from $57 billion to $103 billion, and has totaled $396 billion over the last five years. Since March 2001, 90% of job losses in the US, totaling 2.6 million, has come from the manufacturing sector. China's foreign currency reserves totaled $345 billion in June 2003. Article XXI of the GATT allows any country to take measures that it considers necessary for the protection of its essential security interests. Protecting the manufacturing sector is an essential interest of the US.	manufacturing sector. A significant obstacle to US manufacturers is the aggressive intervention of foreign governments in currency markets. Certain Asian countries exemplify the practice of currency manipulation, such as China, Japan, South Korea and Taiwan. Since 1998, the US trade deficit with China has grown from $57 billion to $103 billion, and has totaled $396 billion over the last five years. Currency manipulation is a subsidy, and a significant non-tariff barrier to trade. Section 3004 of the Omnibus Trade Act (1988) requires the Treasury Secretary to determine if countries are deliberately manipulating their currencies in order to gain a trade advantage. The US has the authority to pursue remedial trade action under Section 301 of the Trade Act (1974).
PROVISIONS ON NEGOTIATIONS		
None	Gives the Secretary of the Treasury and USTR 180 days to negotiate with China ensuring that China adopted a market-based currency system	Gives the President 90 days to enter into bilateral and multilateral negotiations with those countries most egregiously engaged in currency manipulation.
REPORTING PROVISIONS		
Requires the Treasury Secretary to report within 60 on whether China is distorting its currency, and if so by how much in percentage terms.	Requires the President to certify within 180 days that China is no longer manipulating its currency and is valued in accordance with market principles.	Requires the ITC to report within 90 days on the facts surrounding currency manipulation, including the extent to which countries are manipulating currencies and what adverse impacts this practice has on the US economy.

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		Requires the Secretary of Defense to report within 90 days on the extent to which currency manipulation has affected national security. Requires the ITC and USTR to report within 90 days on trade enforcement options against unfair trade practices by competitor nations and strategies for trade promotion.
RETALIATORY PROVISIONS		
If the Treasury Secretary reports China is distorting its currency, imposed an additional ad valorem tariff on all Chinese goods equal to the percentage distortion reported.	After 180 days, if the President fails to make certification on China's currency valuation, **imposes 27.5 ad valorem tariff** on all Chinese goods in addition to existing tariffs.	Requires the President, after 90 days to institute proceedings under Sections 301 and 406 of the Trade Act (1974) against countries failing to agree to end currency manipulation practices. President may elect not to institute proceedings, but must report to Congress within 120 days explaining why no action has been taken.