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Convergence in the Americas: Some Lessons from the DR-CAFTA Process

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1. INTRODUCTION

FEW regions in the world have seen such an aggressive proliferation of Regional Trade Agreements (RTAs) as the Americas. This decentralised and uncoordinated process is beginning to cause concern as it threatens to undermine efforts to build a hemispheric trading system. One of the most urgent tasks now facing trade policymakers in the Hemisphere is to analyse how the various RTAs might be made to converge, and the purpose of this paper is to act as a catalyst for such discussions. We have therefore explored how the issues raised by the coexistence of various dissimilar RTAs among seven different countries were resolved in the recently-negotiated Dominican Republic-Central America[1] United States Free Trade Agreement (hereinafter 'DR-CAFTA' or 'the Agreement'). This Agreement is a microcosm of what could be a broader negotiation process in the Americas, hence the usefulness of analysing its structure and the approaches used in its development.

By 'convergence' we mean the efforts countries make to ensure that the ultimate goals of their trade agreements are consistent and, in particular, that they lead, in the most orderly fashion possible, to the creation of a hemispheric free trade system governed by common rules or at least by disciplines that ensure a minimum variation in regulations. Convergence efforts aim to avoid the fragmentation of

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[1] Central America includes Costa Rica, El Salvador, Guatemala, Honduras and Nicaragua.

the hemispheric trading system. They seek to align countries within a smaller and simpler framework of free trade disciplines, in the understanding that this process generates better results in terms of the public and private administration of trade flows and of the production apparatus. Given the status quo in the Americas, convergence could, in theory, mean several things: (1) replacing the multitude of existing instruments with fewer instruments; (2) reducing the complexity of existing regulations; (3) eliminating obsolete agreements and instruments; (4) harmonising the rules in the new agreements or the rules of pre-existing agreements; and (5) extending the membership of a specific trade agreement.

This analysis has been divided into six further sections. Section 2 outlines the proliferation of trade agreements in the Americas and aims to describe the main causes of this proliferation. Section 3 highlights the main problems generated by the proliferation of RTAs. Section 4 proposes some ways in which the most notable negative effects of this proliferation could be neutralised and highlights the importance of promoting convergence. Section 5 analyses the market access provisions for goods in DR-CAFTA from the standpoint of using convergence techniques. Section 6 performs the same analysis for rules of origin in the Agreement. Finally, Section 7 concludes with some lessons that can be learned from the DR-CAFTA experience as far as convergence is concerned and that may be useful should attempts be made to achieve such convergence in broader contexts within the Americas.

2. BACKGROUND: PROLIFERATION

RTAs in the Americas have traditionally been divided into two types: the first-generation agreements and the second-generation agreements.[2] The first-generation agreements emerged during the 1960s when the strategy of using import substitution as a paradigm for economic development was in vogue throughout Latin America and the Caribbean (LAC). The overriding objective of this first generation was commercial: to integrate what were usually adjacent markets so as to be in a position to take advantage of economies of scale by implementing regional production and joint investment policies. Some of the most far-reaching agreements were signed during this first stage: the Central American Common Market (CACM), the Caribbean Community and Common Market (CARICOM), the Andean Pact, and the Latin American Free Trade Association (LAFTA), which in 1980 became the Latin American Integration Association (ALADI).

Several factors eroded the effectiveness of this development model, however, including countries' balance of payments problems (triggered by the oil crisis

[2] The terms 'old' and 'new regionalism' are also used. See Devlin and Estevadeordal (2001).

of the 1970s and the external debt crisis of the 1980s), asymmetries in the distribution of the benefits of integration, and to a certain extent, the lack of real commitment displayed by the countries towards the trade opening processes they had previously agreed to. A lack of suitable institutional and legal frameworks, furthermore, only exacerbated these problems and meant that little was achieved in solving the other political and border-related issues that bedevilled many of the region's countries well into the 1980s. In most cases, the Customs Unions (CUs) and the Free Trade Areas (FTAs) were not properly established and many soon became riddled with loopholes, exceptions and general non-compliance. Protectionist pressures quickly led to widespread non-compliance with the commitments and disciplines that had been negotiated under the various agreements, at a time when effective enforcement instruments were sorely lacking.

A new wave of integrationist fervour swept the Hemisphere at the end of the 1980s for many different reasons, which can be broadly grouped under the headings of regional security concerns and the desire to participate in the global economy. This new enthusiasm was particularly apparent at the two extreme ends of the Hemisphere: in the United States and Canada, whose FTA of 1986 laid the foundations for NAFTA in 1993, and the 1988 economic complementarity agreements between Argentina and Brazil, which culminated in the creation of MERCOSUR. It was in the midst of this second wave of integrationist enthusiasm that George Bush Sr.'s administration launched the Enterprise for the Americas Initiative, which was to extend free trade from Alaska to Tierra del Fuego. This process had tried to build on an idea that has been floating around the Latin American psyche in one form or another for almost 200 years: the integration of Latin America and/or of the Americas as one entity.

NAFTA, which was the first of the second-generation FTAs to have a North-South component, is limited in scope to an effective free trade agreement that was rigorously negotiated and implemented as an exercise in inter-governmental cooperation (without supranational components). NAFTA was designed using a top-down approach. Its commitments came into force collectively and simultaneously. The rigour of this agreement is derived from the clear definition of its disciplines that come into force on a specific date and whose application is largely guaranteed by the existence of solid dispute settlement mechanisms. The depth of this agreement is reflected in the level of detail attained in the specification of both trade- and non-trade-related disciplines, such as investment, intellectual property, government procurement, and labour and environmental issues.

Though a NAFTA contemporary, MERCOSUR continued with the integration philosophy in fashion at that time in Latin America. From the beginning, its four member countries set high aspirations, including the creation of a free trade area for goods and services and even a customs union that would be built from the bottom up by having the countries gradually adopt commitments in a relatively flexible way. This approach and the notable absence of sound enforcement

TABLE 1
MERCOSUR and NAFTA: Comparing Modalities and Architectures

Issue	*MERCOSUR*	*NAFTA*
1. Negotiating modality	Permanent negotiating mode	One-off
2. Entry into force	Over time as instruments are negotiated	One single instrument enters into force in a specific date
3. Negotiations with third parties	4 + 1	Multilateral
4. Tariff elimination	Preference margins	Residual tariffs
5. Base tariff	Not fixed	Fixed
6. Exclusions	Many goods are excluded	Fewer goods are excluded
7. Built-in flexibilities in market access	Many	Limited
8. Scope of the origin regime	Broad and imprecise	Very precise
9. Rules of origin	General rule plus some specific rules	Specific rules for all products
10. Certification of origin	By certifying entities	Self-certification
11. Updating of the rules of origin	Permanent	Sporadic
12. Nature of dispute settlement mechanisms	Has evolved from weak to judicial approaches	Quasi-judicial
13. Safeguards	Lack of clarity in the rules	More precise rules
14. Investment	Post-establishment	Pre-establishment
15. Intellectual property	Based on WTO TRIPS Agreement	WTO TRIPS-plus
16. Government procurement	Limited coverage	Wide coverage
17. Services	Positive list	Negative list
18. Labour issues	Not a full chapter or agreement	Side agreement
19. Environmental issues	Not a full chapter or agreement	Side agreement

mechanisms, however, led to a high degree of non-compliance in the implementation of the commonly agreed policies. It is only recently with the creation of the Permanent Review Tribunal – with some supranational elements – that enforcement mechanisms have been improved. Table 1 offers a basic comparison of modalities and architectures in MERCOSUR and NAFTA.

The change in the economic development paradigm adopted by developing countries in the 1980s in favour of greater participation in the global economy was the key factor that boosted integration processes in LAC in general and launched Mexico on what was a truly ambitious adventure: its accession to NAFTA. This led other countries to overhaul the instruments used in the integration schemes they were party to. The RTAs were restructured to adjust to the new circumstances, existing agreements were expanded, and more comprehensive agreements were signed, including with developed countries. Countries such as Mexico and Chile spearheaded an FTA negotiating frenzy with neighbouring countries that spread throughout the Hemisphere in the 1990s (see a list of RTAs in Appendix A).

When viewed in perspective, this universe of RTAs can be seen to have two centres of gravity: on the one hand, there is the NAFTA-inspired model, which was avidly extended throughout the region by Mexico, and on the other, there is the MERCOSUR model, which was applied in this bloc's negotiations with Chile and Bolivia under a 4 + 1 negotiating format. Chile, for its part, has turned into a 'hinge' country[3] that has developed formal trade ties with both centres of gravity.[4]

These two centres of gravity of integration in the Americas pursue completely different economic policies. In general terms and as suggested above, the MERCOSUR model, having taken shape in the wake of ALADI, is actually no more than a continuation of that organisation's basic philosophy as far as trade is concerned; in other words, a kind of free trade *ma non tropo*. A cautious political stance towards the process is highly evident, and integration is consequently pursued through the implementation of successive stages of economic liberalisation that have notably defensive features. In this context, trade opening is strongly susceptible to internal lobbying by interest groups. Two factors could lie behind this approach: the countries' structural fragility and their limited capacity to support the adjustment process on the one hand, and the clear influence of the specific interests that lobby for a more flexible regulatory framework, with fewer commitments, that allows for safeguards in cases of urgent need, on the other.

The NAFTA model is quite different: the specifics of this model were first worked out by two developed countries, the United States and Canada. It spread southwards against the backdrop of marked asymmetries in development and capacity, and consequently, in power. The content, scope and depth of this model were not defined by the least-developed member. The United States (the hemispheric behemoth) set the 'gold standard' as broad trade liberalisation. The approach was more ambitious in areas of interest to the United States, such as intellectual property, some services, government procurement and investment, but like MERCOSUR it did allow for exceptions and certain restrictive arrangements in areas in which domestic lobbying in that country was particularly strong (basically the textiles and apparel industries, sugar and other agricultural products, maritime services and other services that involve the relocation of unskilled labour, etc.).

In the wake of NAFTA, Mexico embarked on an aggressive FTA negotiation process with other Latin American trading partners. The ensuing agreements were based on the NAFTA model and led to the creation of a central hub of multiple independent FTAs within and outside the Hemisphere. Other countries, such as Chile and Costa Rica, were soon engaged in similar, though less intense, processes. The emergence of these hub countries may best be explained by the fact that: (1)

[3] See Jara (2005).

[4] There are many points of coincidence, however, in rules of origin. See Garay and Cornejo (2001).

once an FTA has been negotiated with major trading partners, the marginal costs of granting concessions to third countries in other negotiations are lower; (2) placing all local producers on an equal competitive footing in the international market can prevent trade from being diverted to supplier countries; (3) there are advantages to accessing new markets under preferential treatment; and (4) progress in multilateral negotiations has been slow and has failed to respond quickly enough to the market access needs of countries that are aggressively trying to insert themselves into the global economy as part of their overall development strategy.

In between these two extremes of integration activity, other subregions are pursuing their own trade development and expansion agendas. In the 1990s, Central America overhauled its regulatory and institutional integration framework with two aims in mind: to promote the end of the conflict that had rocked the subregion during the 1980s; and to use regional integration as a platform for the subregion's insertion in the global economy. After what turned out to be a tortuous negotiation process, disciplines were substantially reinforced in key areas, such as tariffs (progress was made regarding internal free trade and a rather imperfect common external tariff was established), as well as mechanisms and criteria for the adoption of safeguards and other measures. The countries are currently working on establishing an effective customs union. Much remains to be done in this respect, however.

For its part, the Andean Community has, throughout its history, striven to attain regional integration. Simon Bolivar, Andean hero *par excellence*, was the first to expound the idea of continental integration almost 200 years ago. Such efforts have constantly been thwarted, however, by centrifugal forces such as the region's complicated geography, the uneven distribution of the benefits of integration, low volumes of intra-regional trade and investment, and the complex political and economic situations in each of the participating countries.

The empirical evidence available suggests, however, that these bilateral and subregional negotiation strategies produced significant returns in the 1990s. The Inter-American Development Bank has concluded, for example, that a comparison of extra- and intra-regional trade during 1990 and 2000 shows a marked increase in the relative importance of intra-regional trade, with subregional trade agreements being the vehicle for the countries that are members of them.[5]

3. THE PROBLEM OF PROLIFERATION: FRAGMENTATION

This latest free trade agreement negotiation boom, however, has revealed some of the problems that arise when an important set of new bilateral agreements

[5] See Inter-American Development Bank (2002).

among a limited number of countries, many of which belong to different traditional integration schemes in the Hemisphere, accumulate and overlap. Although there are, of course, significant similarities among many of these agreements, there are also notable differences in the market access negotiation modalities for goods and related disciplines. Economists have come to refer to this meshing of agreements among various actors as a 'spaghetti bowl'.[6] The overlapping of agreements has led to a fragmentation of the hemispheric trading system, the effects of which include:

(a) Multiple tariff treatments: the existence of numerous and different tariff elimination schedules (the same product is subject to a rapid tariff reduction in one agreement, but a slow reduction in another; elimination timetables vary from one agreement to another; sensitive products are subject to different definitions and treatment) creates significant problems in the negotiation and administration of trade agreements. From a business point of view, planning production and organising traffic can also become very difficult tasks. Often, the difficulties are exacerbated by the use of multiple nomenclatures (some of which are no longer valid, such as the NALADISA 96 nomenclature used in the recent MERCOSUR-Andean countries negotiations).
(b) Different origin regimes: the existence of highly divergent chapters on origin that vary in depth and, more importantly, impose different origin requirements for each product makes it extremely difficult for producers to define their input supply structure. When the various trade agreements contain different tariff elimination schedules and origin requirements, it becomes impossible to accumulate third-country inputs, which undermines one of the main objectives of trade liberalisation.
(c) Different documentation requirements: when engaging in international trade involves presenting different documents under different agreements in order to obtain preferential treatment, administrative costs soar for both the economic operators and the customs services and other agencies that monitor international trade.
(d) Different trade disciplines: planning trade and transactions becomes highly complicated when different disciplines regulate matters such as: special regimes (free trade zones, duty drawbacks, transit of goods, outward processing schemes, etc.); sanctions regimes; differentiated safeguard adoption criteria and procedures; and the unequal treatment of used and remanufactured goods, for example.

[6] See Bhagwati and Panagariya (1996).

In addition to a lack of transparency and predictability, economists have identified a number of other problems that might be germinating in the spaghetti bowl. The first is that specific interests are becoming entrenched. Firm commitments are established during negotiation processes in the defence of such interests and, once the regional agreement has been negotiated, it becomes difficult to later dismantle these commitments in the context of another negotiation process.[7] In the textile sector, for example, the United States has negotiated successive agreements with demanding rules of origin that require the virtually exclusive use of regional inputs. Recently, it has consolidated this approach by establishing special regimes for verifying origin and compliance with other commitments. The second problem arises when one or several countries are particularly active in the negotiation of bilateral agreements and therefore end up turning into hubs of trade relations. The best explanation for this problem is furnished by the hub-and-spoke theory, which states that the advantages for the hub country, which stocks up on low-priced inputs from its FTA trading partners, enable it to supply its own market and export to third countries under more favourable conditions.[8] To date, countries such as Mexico, Chile, the United States and, to a lesser extent, Costa Rica, seem to have become hubs for a series of relationships with their trading partners.

Some hub countries have made significant efforts to negotiate identical or highly similar disciplines in most of their agreements. The most notable cases are the United States and Mexico: the terms negotiated in the agreements they have signed vary only slightly. This makes administering the agreements much easier and facilitates procedures for the trader. Other countries, such as Chile, have displayed greater flexibility by accepting terms in the same subject area that vary considerably from one agreement to another. Often this flexibility does not reflect so much a greater or lesser negotiating capacity as it does the adoption of different strategies which are defined according to the costs involved in administering the agreement in question and the requirements of national production and export structures (the sensitivity of their products).

In the long term, it will be possible to solve the tariff tangle in the spaghetti bowl because the various tariff elimination schedules will eventually create free trade among trading partners, at least for substantially all trade. The ongoing problems are posed by differing product exclusions, origin regimes,

[7] The argument is made more notably by Krueger (1995).

[8] The basic argument of the hub-and-spoke theory is that when there is a hub country that has free trade with peripheral countries (spokes), and there is no free trade among these spokes, or these spokes cannot accumulate inputs amongst each other to produce and sell to the hub country or the other spokes, the hub is at a considerable advantage because it can sell to all the countries. When the hub country is rich in inputs, the possibility of further gain increases. The 'hub-and-spokes' theory was first put forward in the weekly contributions made by Wonnacott (1975), Park and Yoo (1989) and Lipsey (1990).

documentation requirements and trade disciplines. It is perhaps in these areas that a concerted effort to achieve convergence of norms and procedures in the Americas is most urgently needed.

4. HOW TO NEUTRALISE THE NEGATIVE EFFECTS OF PROLIFERATION

In theory, there may be several ways in which to neutralise the most important negative effects that are being generated by the proliferation of agreements and the increasing divergence of norms and procedures:

(1) Effective multilateral trade liberalisation. Concerted tariff liberalisation efforts at the multilateral level would render the RTAs meaningless as far as tariffs are concerned. The objectives of, and mechanisms currently used in, the WTO do not indicate, however, that such a trade liberalisation will be achieved in the short or medium term. In fact, the latest Uruguay Round negotiations and the Doha Development Agenda show a strong entrenchment of defensive positions in key sectors of the global economy, such as agriculture and services.
(2) National trade liberalisation. Unilateral tariff elimination has the virtue of standardising the rules for imports, regardless of their origin. The process cannot, however, correct export-related problems and substantially hampers the country's international negotiating capacity. The promotion of internal trade liberalisation requires the implementation of incentive schemes to mobilise winners and neutralise protectionist interests. This can be more readily achieved within the context of a negotiation with another trading partner, in which concessions are also obtained for national exporters. Unilateral liberalisation may look attractive on paper, but is often a complex solution in political terms.[9]
(3) Subregional convergence. A group of countries that have signed a large number of agreements with one another and substantially liberalised their trade could start a convergence process by aligning their trade disciplines in such a way that they converge towards a single scheme. The attempt made by ALADI to create a Free Trade Space, as proposed by the Ministers of the ALADI countries in October 2004, is an example of subregional convergence. This initiative aims to harmonise trade regulations as much as possible without this necessarily requiring the granting of new preferences.[10]

[9] Adding to that, some argue that for individual countries without high protection, some forms of regionalism will likely result in substantially larger gains than unilateral trade liberalisation. See Harrison et al. (2003).
[10] Decision 55 (XII) of the ALADI Council of Ministries (22 February, 2002).

(4) A hemispheric free trade area. The countries of the Americas could also negotiate the creation of an extensive free trade area that would render all the RTAs that have been signed among them obsolete. This can be achieved in two ways. First, by totally eliminating all the RTAs at a given point in time in order to make way for a very broad agreement, and second, by implementing a hemispheric FTA that over the years gradually supersedes all the pre-existing RTAs. The FTAA is, to a certain extent, a variation of the second option, as it provides for the establishment of a future hemispheric agreement that '. . . can co-exist with bilateral and subregional agreements, to the extent that the rights and obligations under these agreements are not covered by or go beyond the rights and obligations of the FTAA'.[11]

The FTAA has been the most notable and promising free trade initiative to promote convergence in the Americas. The negotiations, however, have been on hold for two years. See Box 1 for a synthesis of the most relevant aspects in the evolution of the FTAA initiative.[12]

The spaghetti bowl problem has thus worsened recently, and the question now is: what to do next, how to tackle the problem, under what kind of scheme, and with which instruments? The purpose of this paper is

[11] This provision is open to different interpretations. On the one hand, some interpret the text as allowing countries to maintain their integration schemes when these are more profound, for example, when they go beyond free trade to establish common external tariffs, coordinated external trade policies, the shared collection of tariffs or other features common to economic or monetary unions. There is no clear understanding among the countries, however, of what 'are not covered by or go beyond' means. Another interpretation is that the text does not guarantee that a country can maintain certain pre-existing trade concessions or restrictions, and therefore the FTAA could replace the other FTAs in force in the Hemisphere when, for example, identical preferential tariff rates are attained.

[12] Paradoxically, the FTAA process is intended to eliminate the spaghetti bowl problem, but its bigger country, the United States – which to date had not been a part of the spaghetti bowl – has actually pursued the creation of the FTAA by negotiating other FTAs with countries in the region, the so-called 'competitive liberalisation' strategy. This strategy has ultimately increased the tangles in the spaghetti bowl and, according to some, led to the deadlock in the FTAA negotiations by eliminating, in various ways, the interest key actors may have had in the FTAA negotiation process. The effectiveness of the competitive liberalisation strategy as a tool for furthering hemispheric integration has thus yet to be proven. The FTAA was possibly one of the most controversial issues at the recent Summit of Heads of State and Government of the Americas, held in Mar del Plata, Argentina, in November 2005. There, the polarisation of the Hemisphere's opinions regarding the topic became patently clear. Twenty-nine countries wish to continue the process. Five countries (MERCOSUR and Venezuela), on the other hand, made the continuation of the negotiations subject to the real progress that was expected from the WTO Ministerial Conference in Hong Kong. Consequently, the only agreement reached on the matter was that Colombia would make consultations with a view to convening a ministerial meeting in the first semester of 2006. At the time of writing this paper, the deadlock is still firmly in place.

BOX 1
Short Evolution of the FTAA Initiative

The FTAA initiative was launched in San José in 1998, basically with a view to integrating the trade of the 34 democracies of the Americas in an ambitious free trade zone. The negotiations were due to conclude in 2005. Significant progress was made by 15 negotiations entities in the first five years. Three versions of the draft agreement were produced, each one more orderly, clean and consensual than the last. Initial offers and requests for improvements were made in the four areas of market access: goods, investment, services and government procurement.

The negotiations floundered, however, when the positions of MERCOSUR and the United States became polarised, and it has been impossible to make the complex webs of offensive and defensive interests of these two countries complement one another within the framework of the FTAA's objectives and mandates. This forced the countries to reconsider the structure and final objectives of the FTAA.

In November 2003, they decided that the FTAA would not be established through a single agreement with equal rights and obligations for all its members. Instead, a much more pragmatic and flexible two-tiered arrangement was proposed with a view to fulfilling the mandate to conclude negotiations in 2005: the first tier would consist of a set of common rights and obligations for the 34 countries; the second would consist of a series of plurilateral agreements to be signed by those countries that wished to do so. In order to make this proposal a reality, the Ministers of Trade entrusted their Vice Ministers with the task of working out the details of this new structural modality at the beginning of 2004 so that negotiations could be concluded before the end of that year. The Vice Ministers tried to reach a consensus, but after six months of meetings and consultations, the Co-Chairmanship, held by Brazil and the United States at the time, decided to temporarily suspend the FTAA negotiations.

The crux of the matter lies in the fact that for Brazil and the United States it has been very difficult to display more flexibility in their positions regarding certain key issues in the negotiations on agriculture, services, trade remedies, intellectual property, or the scope of application of the eventual dispute settlement mechanism. Consequently, they have both been dissatisfied with the balance of concessions that would be granted and received under the scheme.

Neither the conclusion of the presidential elections in the United States at the end of 2004, nor the results of the Doha Ministerial Meeting of the WTO at the end of 2005 spurred the resumption of the FTAA process as they were expected to when the negotiations were suspended.

not to analyse the different answers to all these problems. We merely aim to identify convergence techniques or modalities that have been used in smaller-scale negotiation processes such as DR-CAFTA, without passing judgement on the content or scope of those negotiations, with a view to suggesting that they be taken into consideration in any broader convergence initiatives that may be undertaken in the Americas in the future. We shall therefore examine

the various aspects of market access for goods and the origin regime in DR-CAFTA.[13]

5. MARKET ACCESS FOR GOODS IN DR-CAFTA[14]

As far as tariffs are concerned, DR-CAFTA is a particularly complex agreement, as it attempts to consolidate the commitments included in three different agreements into a single legal instrument. These three agreements are:

(1) the free trade agreement between the United States, each of the five countries of Central America, and the Dominican Republic;
(2) the free trade agreement among the five countries of Central America; and
(3) the free trade agreement between the five countries of Central America and the Dominican Republic.

In terms of generating trade and investment opportunities, this consolidation effort makes sense. A costs/benefit analysis would probably show that the costs incurred in the implementation and administration of the complex tariff and origin regime arrangements are lower than the aggregate profits that are likely to be generated in production and trade by this attempt to integrate the seven economies. In other words, if no attempt had been made to consolidate the three agreements, a hub-and-spoke arrangement probably would have emerged in the region, perhaps with the United States as the main beneficiary. This consolidation effort has enabled the countries of Central America and the Dominican Republic to avoid the fragmentation of their trade because, without overlooking their subregional commitments, they will now be able to accumulate inputs from the

[13] There are other initiatives which, deliberately or otherwise, promote subregional convergence in the Americas. These include: (i) the efforts in NAFTA to simplify rules of origin in light of the rules set forth in other agreements; (ii) the Plan Puebla-Panama and the consolidation of the customs union in Central America, which aim to harmonise the multiple sets of rules of origin set forth in the various agreements signed by the seven member countries of these initiatives; (iii) the ALADI countries' efforts to establish a Free Trade Space, starting with the negotiation of common rules for matters such as origin, safeguards and dispute settlement; (iv) MERCOSUR's endeavours to expand its membership to include Venezuela and perhaps Bolivia; (v) the attempt to create a South American Community of Nations, and (vi) the Initiative for the Integration of Regional Infrastructure in South America (IIRSA by its Spanish acronym), which is working towards establishing a regional infrastructure in South America.

[14] The DR-CAFTA was negotiated with a view to it taking effect in January 2006. At the time of writing, the Agreement had still not entered into force due to delays in its implementation. In one country, Costa Rica, the Agreement has not been approved by the Legislative Branch. These delays seem to be transitory, however, and the Agreement is expected to come into force in all seven member countries by the end of 2006 or very soon thereafter.

seven DR-CAFTA countries, attract investment and export to one another, with a few exceptions as mentioned below.[15] While some parts of the negotiations were common and others were bilateral, the disciplines in DR-CAFTA are mostly multilateral; that is, the disciplines – save for a few exceptions – are now common to all seven of the DR-CAFTA countries, and any one of them can demand compliance from the other six.[16]

The three axes along which tariff commitments have been structured under DR-CAFTA are briefly described below.

a. First Axis: The DR-CAFTA Tariff Elimination Schedule

The tariff elimination schedule of DR-CAFTA must be understood as the product of the negotiations that were undertaken mostly jointly by the five Central American countries and the United States in the second semester of 2003. The joint negotiation process enabled intra-Central American negotiating positions to be coordinated to a large extent but did not lead to the establishment of a single tariff elimination schedule in which the Central American countries stipulate the terms for liberalising their trade with the United States. Instead, the Agreement established different tariff elimination schedules for each Central American country and the Dominican Republic *vis-à-vis* the United States. A significantly large portion of the merchandise covered in each Central American country's TES, however, is classified in staging categories or baskets that are subject to similar tariff elimination schemes. This was accomplished thanks to the relatively homogeneous Central American common external tariff (75 per cent of the tariff lines were harmonised at the time), which facilitated the coordination of efforts at the intra-Central American level.[17] Treatment is often similar, though not always identical, even in the case of sensitive products, as we shall see below. The pre-existing differences among the Central American countries with regard to the remaining 25 per cent resulted, of course, in dissimilar final tariff elimination schedules for each of the five countries.

The United States' TES, on the other hand, does contain single commitments that are equally applicable to all the other six countries in the Agreement. In other words, if a specific good is classified as staging category 'A' (immediate

[15] For an analysis of this argument that was written prior to the DR-CAFTA negotiations, see Xirinach and Granados (2004).
[16] See González (2005).
[17] A common external tariff implies that harmonisation negotiations have taken place among member countries in a CU. Interests and expectations have been aligned thereby providing a common baseline from which tariff negotiations with third parties are substantially facilitated.

elimination) on the US Schedule of tariff commitments, that 'A' classification benefits all six countries equally. Generally speaking, under no circumstances is a good subject to category 'A' treatment in some countries, and different treatment in others.

The Dominican Republic's case was particularly unusual. It negotiated its accession to DR-CAFTA during the first quarter of 2004, after the negotiations between the Central American countries and the United States had concluded in December 2003/January 2004. As there was no pre-existing common external tariff between the Dominican Republic and Central America and no significant level of coordination with the region either, there is no similarity between the tariff elimination schedule of each Central American country and that of the Dominican Republic.[18]

The principle of using a multilateral approach in the application of tariff commitments was apparent from the outset of the negotiations for the Agreement. The seven countries (the 'Parties') form an FTA among each other (see Article 1.1) but do not specify the scope of the Agreement. They merely restrict the application of the commitments among certain Parties.[19] In this way, the fundamental principle of DR-CAFTA is established: the application of DR-CAFTA commitments is multilateral unless otherwise specified in the text of the Agreement. The footnote on page 1 to para. 2 of Article 3.3 makes the multilateral nature of tariff application in DR-CAFTA even clearer. It states:

> For greater certainty, except as otherwise provided in this Agreement, each Central American Party and the Dominican Republic shall provide that any originating good is entitled to the tariff treatment for the good set out in its Schedule to Annex 3.3, regardless of whether the good is imported into its territory from the territory of the United States of any other Party . . .

As we shall see below, there are several exceptions to this principle in terms of both tariffs and rules of origin. The tariff elimination schedule set out in the Agreement establishes 25 tariff reduction categories, each one labelled with a letter from 'a' to 'y'. Eight of these categories are common to the schedules of

[18] Annex 3.3 of the Agreement presents the tariff concession schedules of the seven DR-CAFTA countries.

[19] Compare this situation, for example, with that of other regional plurilateral agreements that establish that commitments are strictly bilateral in kind and clearly state this. See, for example: Article 1.01, para. 2, of the Free Trade Agreement between Central America and the Dominican Republic, and Article 1.01, para. 2, of the Free Trade Agreement between Central America and Chile. Both of these agreements state: 'Unless stipulated otherwise, this Agreement shall be applied bilaterally between (Chile) (the Dominican Republic) and each of the countries of Central America considered individually'. Also, as mentioned above, the MERCOSUR agreements use a '4 + 1' modality, and the bloc's agreement with the Andean countries is bilateral in kind.

the seven countries, while the others are applicable only among certain countries or applied by a certain country.[20]

Normally, sensitive goods are subject to more restrictive measures.[21] Many of these sensitive products, which are usually agricultural goods in the case of DR-CAFTA, are ones which the countries have a strong desire to export. If the market access conditions for these goods are too restrictive, enthusiasm for the Agreement would soon wane. In order to balance pressure for transitory but long-term protection on the one hand against the need to create immediate market access for these products on the other, Tariff Rate Quotas (TRQs) are negotiated. TRQs are basically quotas that establish the annual volume of products that can be imported under more favourable conditions than those to which the products are usually subject. In DR-CAFTA, this means, in most cases, the application of a zero tariff for the products imported within the annual quota.[22]

No products in DR-CAFTA are totally excluded from the trade liberalisation commitments, but in certain specific cases (white corn for Guatemala, Honduras, El Salvador and Nicaragua; fresh potatoes and onions for Costa Rica), products are subject to what could be considered 'exclusions' given that the treatment consists of zero tariffs being applied to TRQs for minimal 'symbolic' volumes (estimated in terms of the equivalent of a few days' national consumption per year). The volumes of these quotas are not set to change or will only be increased very slowly. Due to their minimal size, these TRQs have a negligible impact on trade. Any imports of these sensitive products outside the quotas, furthermore, will continue to pay the most-favoured nation (MFN) rate, without enjoying any other preference.

b. Second Axis: Intra-Central American Free Trade

Next we shall look at how intra-Central American trade affects DR-CAFTA.

The Central American integration instruments ensure that trade in products originating in the five countries is already not subject to any tariff restrictions

[20] For a precise description of the tariff reduction categories in DR-CAFTA, see Tripartite Committee (2005). This document also provides a summary of the trade volumes and number of tariff lines for each reduction category for each DR-CAFTA country.

[21] This treatment may consist of: (i) slow tariff reduction processes; (ii) grace periods; (iii) special or global safeguards; (iv) exclusion from the application of the national treatment principle; and (v) outright exclusion.

[22] The products subject to TRQs are: pork, chicken and beef, dairy products, rice, certain types of potatoes, onions, corn, sorghum, beans, glucose, peanuts and ethyl alcohol. For further details, see the summary of the Tripartite Committee, op. cit., pp. 26–31.

except in a minimal number of cases.[23] DR-CAFTA acknowledges this and has made no attempt to alter this arrangement. Article 3.3, para. 2, of DR-CAFTA, which sets out the tariff elimination schedule, states:

> 2. Except as otherwise provided in this Agreement, each Party shall progressively eliminate its customs duties on originating goods, in accordance with Annex 3.3.

For its part, para. 3 of the same article establishes that the Agreement shall not alter intra-Central American free trade:

> 3. For greater certainty, paragraph 2 shall not prevent a Central American Party from providing identical or more favorable tariff treatment to a good as provided for under the legal instruments of Central American integration, provided that the good meets the rules of origin under those instruments.

This provision ensures that the trade liberalisation process that has been under way among the five countries of Central America for over 40 years, as set forth in the aforementioned integration instruments (basically the aforementioned Article III of the General Treaty and its Annex A),[24] is not to be affected by DR-CAFTA. The exceptions referred to in this Annex were partially taken into consideration in DR-CAFTA, inasmuch as they continue, in general terms, as exceptions to intra-Central American free trade.[25]

As intra-Central American free trade coexists happily with the principle of multilateral tariff concessions, a Central American exporter can opt to export to other Central American countries by applying either the tariff elimination schedule of DR-CAFTA (Annex 3.3) or the free trade regime established in the Central American integration instruments. Two significant points need to be made in this respect. First, when using either of these options, the origin and tariff regimes of each agreement must be respected. We will discuss this in greater depth in the next section of this paper. Second, for reasons of convenience, exporters are most

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[23] Article III of the General Treaty on Central American Economic Integration of 1960 establishes the following:

> The Signatory States shall grant each other free-trade treatment in respect of all products originating in their respective territories, save only for the limitations contained in the special regimes referred to in Annex A of the present Treaty.

Annex A, on the other hand, contains specific exceptions to the free trade system that are applicable among all five countries or to trade with certain ones. The products included in Annex A are basically coffee, sugar, alcohol, alcoholic beverages, and crude oil and its derivatives. These products are subject to import duties or licences.

[24] Article 1.3, para. 2, also specifies that the Agreement shall not affect the Central American integration instruments nor hamper the deepening of regional integration.

[25] General Note No. 6 of the General Notes to the Schedules of the five Central American countries and the Dominican Republic states this specifically in the case of sugar imports (SA1701) and coffee imports (SA0901.11, 0901.12, 0901.21 and 0901.22) These notes do not mention the other products: alcohol, alcoholic beverages, and crude oil and its derivatives, which we shall refer to later.

likely to continue using the intra-Central American free trade scheme until the transition to zero tariff rates has been completed in DR-CAFTA or might be interested in doing it even after the tariff phase-out in cases where the Central American rule of origin is more favourable. Therefore, once goods are subject to zero tariffs under the Agreement, traders will have two clear options at their disposal, and the deciding factor will then be the specific rule of origin under each scheme. US exporters wishing to export to Central America will obviously not have these two options: they will only be able to export under the DR-CAFTA scheme. Exporters in the Dominican Republic, on the other hand, will also have two options for exporting to Central America, thanks to the Free Trade Agreement between Central America and the Dominican Republic. This constitutes the third axis of tariff commitments in DR-CAFTA, which we will analyse below.[26]

c. Third Axis: Free Trade between Central America and the Dominican Republic

The countries of Central America negotiated an FTA with the Dominican Republic in 1998. This agreement is based on the principle of negative lists: trade is liberalised immediately for all goods except those included in a list of sensitive products that are subject to special treatment, be it total exclusion, gradual tariff elimination and/or specific TRQs. DR-CAFTA incorporates – with minor modifications – the principle of free trade between the Dominican Republic and the Central American countries into its text, as well as the special treatment accorded under that FTA, in order to maintain the status quo insofar as possible (see Annex 2). This renders the FTA unnecessary, and the six countries have agreed to terminate it when DR-CAFTA comes into effect.

The complexities involved in attempting to consolidate the pre-existing conditions established in three different agreements and new conditions in a single

[26] The fate of the products that are exceptions to intra-Central American free trade (those listed in Annex A of the General Treaty on Central American Economic Integration) has yet to be resolved. As mentioned above, the situation of sugar and coffee is clear, inasmuch as General Note No. 6 establishes that the liberalisation commitments for these goods, according to Annex 3.3, are only to benefit the United States. This renders it impossible, however, to multilateralise the eventual free trade of these products under DR-CAFTA at the intra-Central American level. If a good is removed from Annex A, however, it will fall under the intra-Central American free trade regime. General Note No. 6 would then become irrelevant and Central American exporters would once again be able to choose between the two options mentioned above. What will happen, however, with the other products in Annex A that are not specifically regulated under DR-CAFTA and, in particular, with crude oil and its derivatives, alcohol and alcoholic beverages? One logical interpretation would be for these products to remain subject to free trade within Central America under the same terms as they will be subject to according to the Schedules for each Central American country as set forth in Annex 3.3. In other words, under the principle of multilateral application of DR-CAFTA, these products will eventually be subject to zero tariffs in intra-Central American trade.

instrument are patently clear in DR-CAFTA. The Agreement, however, makes every effort to leave no loose ends. Some products are subject to particularly complex arrangements. The most notable examples of these are coffee, sugar, and crude oil and its derivatives:

Sugar and coffee: For exporters from Central America or the Dominican Republic, these products are subject to tariff elimination commitments only in the United States as set forth in the tariff elimination schedule, as well as to other important restrictions that are established in the text of the Agreement itself. As mentioned above, as far as intra-Central American trade is concerned, these two products are subject neither to free trade nor to any tariff elimination schedule. As far as exports from Central America to the Dominican Republic are concerned, these two products are included in the list of goods that are to be negotiated in a year's time. If no agreement is reached, a ten-year grace period will come into effect, with total tariff elimination occurring in the year 2020.

Crude oil and its derivatives: For exporters from Central America or the Dominican Republic, these products are subject to tariff elimination commitments in the United States as set forth in the tariff elimination schedule of DR-CAFTA. As far as intra-Central American trade is concerned, trade in these products will be liberalised due to the principle of multilaterality enshrined in DR-CAFTA. Central American exports to the Dominican Republic are subject to the plurilateral tariff elimination schedule set out in Annex 3.3.6, para. 3, of the DR-CAFTA.

6. THE DR-CAFTA ORIGIN REGIME

The existence of the three DR-CAFTA axes assumes a particular level of complexity in the establishment of rules of origin for goods. The efforts to consolidate these three axes resulted in the Agreement providing for two origin regimes and setting out specific rules in three annexes.

Designing an origin regime to be applied multilaterally in the context of multiple sets of rules does not depend simply on decision-making capacity. The task necessitates a process that facilitates the gradual alignment and eventual coexistence of pre-existing origin regimes in the region, while respecting the needs of the countries involved.

The existence of a spaghetti bowl of origin regimes is a real problem both for traders and the authorities in charge of control and verification procedures. Differences in origin regimes oblige producers and governments to adapt their organisation and to absorb higher costs.[27] Producers not only have to design a production and supply structure that is compatible with all regimes, they also

[27] Garay and Cornejo (1999). See also Estevadeordal and Suominen (2004).

have to bear the costs incurred by that adaptation and the ensuing loss of efficiency. Governments meanwhile have to implement particularly complex processes to determine and verify origin. This complexity does not contribute much in terms of transparency and predictability; in some cases, it creates more opportunities for corruption. Furthermore, since inputs and processes are not broadly accumulated in a spaghetti bowl configuration, the capacity for increasing trade and creating deeper economic integration is considerably limited. The multilateral application of an origin regime can help resolve these problems.

The implementation of a multilateral origin regime is not a hitch-free process either, however. Making the transition to any new regime is traumatic for producers. The replacement of substantive and procedural rules, for example, may encounter the following problems:

(a) Different ways of defining the rule of origin vector: the different criteria for determining origin and the varying frequency of their use can restrict or expand the supply sources permitted under an agreement (see Table A1 in Appendix C for an example of this).
(b) Discrepancies in the application of *de minimis*: the percentage levels allowed by one country in its various agreements[28] and the varying interpretations of how the principle can be implemented[29] are some of the more frequently-occurring differences; another differing aspect is the list of products excepted from *de minimus* provisions.
(c) Alterations in the method of applying the accumulation principle: trade agreements allow for the accumulation of goods, but not all contain provisions for accumulation by process.[30]
(d) Differential treatments for various production sectors: trade agreements frequently identify sectors or products that receive special treatment that differs from the treatment given to other products. These types of treatment and the selection of the sectors differ among agreements.
(e) Differences in procedures: origin certification is one of the most dynamic aspects of negotiations in the Americas. Various systems currently coexist.

[28] In some cases, countries have signed agreements that do not include *de minimis* provisions or whose level of flexibility, when so permitted, fluctuates between five and ten per cent.
[29] Some countries interpret the *de minimis* provisions of their agreements as not applying to the exceptions to tariff classification changes that the product rule can eventually contain, while most countries consider their agreements as allowing this.
[30] Accumulation by process involves the application of the rules of origin of a good at the regional level and not at the level of each member country of an agreement. This method of applying accumulation allows a good, whose origin requirements are difficult to comply with in one member country of the agreement, to still be used as an input in broader production processes by companies in another member country and not be rejected as having non-originating status.

They all hold different agents responsible for proving origin and establish different responsibilities, duties and rights.

While duties disappear at the end of the elimination periods, rules of origin remain and are one of the few elements of a negotiation that must be enforced in each commercial transaction. The aforementioned discrepancies in origin regimes show that replacing several of them with one alone means that the market access conditions agreed upon are in fact modified. Replacing rules is no easy task, since proposed rule changes do not always have the support of the business community.

In DR-CAFTA, a multilateral origin regime coexists with other pre-existing origin regimes. This coexistence seeks to mitigate the effects of an abrupt replacement of rules by granting special types of flexibility. It also means that, for some products, two regimes are applicable under the Agreement, as well as annexes containing different rules of origin, and producers, exporters or importers can select which regime they prefer to use.[31]

Several articles and some footnotes in the Agreement establish, in a somewhat disorderly manner, the rules of origin for the three axes of trade in the DR-CAFTA system:

(a) the multilateral regime applied to trade in all products among all the countries (Chapter Four and Annex 4.1).
(b) the origin regime and the annex containing specific rules negotiated in the framework of the Central American Common Market (Resolution 20-98, COMIECO VII; Resolution 30-98, COMIECO XI; and Resolution 100-2002, COMIECO XXV) that are applied exclusively to intra-Central American trade and not to trade between the United States and the Dominican Republic.
(c) a third annex containing rules of origin entitled Special Rules of Origin (Appendix 3.3.6, Special Rules of Origin of Chapter Three), the application of which is limited to trade between Central America and the Dominican Republic.[32]

[31] To date, the only origin regime in the Hemisphere that is applied multilaterally to a series of trade agreements involving different countries is ALADI Resolution 78 and its subsequent updating by Resolution 252. This system, negotiated in the early 1980s, functioned well enough for a few years, but as a result of its lack of preciseness and updating, it was set aside, and the ALADI member countries negotiated new origin regimes, which contributed significantly to the spaghetti bowl of today. A multilateral regime applied to a large group of countries is difficult to put together and update, as such an endeavour involves conflicting positions and interests that mutually cancel out any possibility of reaching a consensus. The few modifications introduced in the replacement of Resolution 78 by ALADI Resolution 252 are examples of how difficult this process is.

[32] In addition, Annex 4.1.d sets forth a series of transitional rules of origin (two years) that are applied to trade between the United States and the Dominican Republic for fuels, some plastics and iron castings.

TABLE 2
Main Characteristics of the Three DR-CAFTA Origin Regime Axes

Issue	*Axis*		
	DR-CAFTA	*CACM*	*CACM-DR*
Origin Regime	Chapter IV	Res. 20/98 and 30/98	Chapter IV
Specific Rules	Annex IV	Res. 38/98 and 100/02	Appendix 3.3.6
Transitory Rules	Annex 4-1-D (USA-DR)	X	X
Bilateral Rules	Annex 4-1-D (USA-DR)	X	Appendix 3.3.6 (Part III)
Certification	Producer/Exporter/ Importer	Exporter	Exporter
Special Textile Regime	Art. 3.24/25	No rules for Chapters 58, 60–63	Appendix 3.3.6 (Part III)
Short Supply List	Annex 3.25 (USA approves the list)	X	X

Note:
X = The agreement does not contain this concept.

Table 2 identifies, for each of the trade axes, the corresponding regime, the applicable rules, and some of the exceptions and characteristics of this regulatory system that enshrines multiple origin regimes. The various regimes in force in DR-CAFTA have been articulated in such a way that although operators can choose the regime they wish to use in the cases that alternative origin regimes exist for the same trade transaction (e.g. the multilateral regime and the Central American regime), once that choice has been made, the transaction must be governed throughout the operation by that chosen regime. This means that it is not possible to apply the origin chapter of DR-CAFTA and then the annex of specific Central American rules (or vice versa) to the same transaction.

a. The first axis: the DR-CAFTA multilateral origin regime

The main advantage of this regime is that it provides economic operators with a standardised, detailed and comprehensive regulatory framework that enables them to export their products under the same origin conditions as any other member state. In addition, this regime establishes the essential foundations for the eventual free circulation of originating goods and for taking better advantage of the accumulation principle in terms of both goods and processes. This aspect of DR-CAFTA even allows, albeit in a limited way, for the possibility of Latin

American countries that are signatories to the Agreement to accumulate inputs from Harmonised System Chapter 62, textiles, from third countries (Canada and Mexico) to produce garments.[33]

One characteristic of this regime is the strong influence the United States exerted in its design. This is apparent, for example, in the definition of rules of origin, the treatment of remanufactured products and textiles, and the rules regarding certification by importers.[34] It must be recognised that convergence often depends on hegemonic actors defining the core elements of a system.[35]

The value content criterion is used to define many specific rules of origin (or the rules of origin vector) in DR-CAFTA. Though it is used less often and in a simpler way in DR-CAFTA than in NAFTA, this reflects the new way the United States has been defining and applying this criterion in its trade agreements in recent years. The United States now applies the value content criterion on the basis of regional materials ('build-up') rather than the complex net cost method so often used in NAFTA, which is now only used for automotive industry products, on an optional basis.

Under DR-CAFTA, remanufactured products[36] are accorded the same tariff treatment as new products, but have some exclusive flexibility in terms of origin. The universe of products that can be remanufactured is considerably larger than that agreed upon by the United States in its previous negotiations with Chile and Singapore. For the Central American countries, accepting this larger universe (870 subheadings, 2,000 per cent more than in the agreements with Chile and Singapore) did not pose a difficulty for two fundamental reasons. First, remanufactured goods in Central America are largely subject to zero tariffs due to the absence of regional production. Second, Central American regulations allow used goods to be imported. However, given the commercial importance of this issue in the DR-CAFTA, we believe that its treatment should have been consolidated in a specific article instead of being dispersed in different Chapter footnotes and definitions that are not clearly interlinked.

The multilateral regime of DR-CAFTA allows for certification by importers as well as by exporters or producers. In practice, however, because of the way the regulation is worded, importers have the primary responsibility for proving origin. The advantage of this new system is that the role of the competent

[33] Appendix 4.1-B. This facility will not be applied automatically and is somewhat complex, as it is contingent on future negotiations to adapt the origin rules established in Canada and Mexico's agreements with Central America and the Dominican Republic.
[34] See Cornejo (2005).
[35] Examples of this include the negotiations between MERCOSUR, Chile and Bolivia, between Mexico and various Latin American countries, and the recent bilateral agreements of the United States.
[36] Remanufactured products are goods produced entirely or partially with materials recovered from used goods.

authorities in the importing country is strengthened because all aspects of origin declaration are concentrated in the destination country. This system is a cause for concern, however, because it awards a responsibility to importers that they will find difficult to meet, especially in Latin America. Latin American importers have problems obtaining the required information for origin certification for several reasons: their purchases represent relatively little in terms of volume in the sales of American exporters; they usually purchase from distributors and not from producers; and American exporters are not familiar with trade transactions that involve having to demonstrate and certify the origin of the goods.

In addition to encountering these difficulties and finding themselves in this somewhat 'helpless' situation, most Latin American importers have only a limited knowledge of origin issues. It is therefore clear that in this context, if the multilateral regime is ever to be properly implemented and managed, the customs services of importing countries will have to work relentlessly to upgrade their origin verification capacities (which are virtually non-existent today) and to organise intensive training programmes for economic operators.

As mentioned previously, tariff liberalisation makes provisions for the establishment of TRQs for a number of the sensitive products of the seven countries. In order to properly apply these quotas, the multilateral origin regime included the concept of 'qualifying goods'. The application of quotas in the case of these goods is tied to the principle of accumulation. In the case of products with TRQs granted by the United States, for example, the Central American countries may not accumulate inputs originating from that country. When the country granting the quota is a Central American country or the Dominican Republic, the United States may not accumulate inputs from the other five countries that are party to the Agreement. These restrictions in the application of the accumulation principle make sure goods produced in the United States cannot be used to fill the quota granted by the United States, and that the TRQ granted by one Central American country to the United States cannot be filled using inputs or products from the other Central American countries that are party to the Agreement. The Agreement does not, however, expressly prevent the Central American countries or the Dominican Republic from accumulating inputs among themselves to subsequently export finished products that benefit from a TRQ in the United States.[37]

b. The second axis: the Central American origin regime

The follow-up to the DR-CAFTA negotiations shows that the initial version of the Agreement signed by the negotiators only contemplated the multilateral

[37] The General Notes of the United States do not limit this possibility.

regime.[38] In fact, the wording of the pre-legal scrubbing version invalidated, albeit in a not very explicit way, the Central American origin regime together with other regulations.[39] At the insistence of the Central American countries, that vision was eliminated from the final version, and the definitive article on the subject allows origin regimes to coexist.[40] From that point onwards, DR-CAFTA began to map out its own peculiar architecture.

The Central American origin regime is still in full force for trade among the countries of the Central American Common Market. This regime, the content of which falls somewhere between the first- and second-generation agreements, is characterised by: broad thematic coverage; a detailed procedure verification system; simple origin requirements based exclusively on variable changes in tariff classifications by product; origin certification by exporters; and no origin requirements for certain textile products (Chapters 58, 60 and 62 of the Harmonised System).

c. The third axis: accession of the Dominican Republic

DR-CAFTA's complex origin regime was completed with the belated accession of the Dominican Republic to the Agreement. In order to become a member, the Dominican Republic had to engage in two negotiation processes: one with the United States and one with the countries of Central America. For the Dominican Republic, the results of the former meant having to accept the entire origin chapter originally negotiated by the United States with Central America, along with the specific rules contained therein. The only difference lies in the two-year period of transitory flexibility mentioned above (Annex 4.1.d).

The negotiations with the Central American countries were, for their part, more flexible. With regard to the origin chapter, the Dominican Republic and the countries of Central America (which already had an origin chapter in their 1998 FTA) agreed to apply the chapter negotiated in DR-CAFTA and negotiated only a few interpretive notes among themselves to facilitate the application of their specific rules of origin (Appendix 3.3.6 of DR-CAFTA). One of these notes stipulates that inputs from the United States or any process carried out in that country shall be considered as non-originating, which means they shall not be allowed to be accumulated and

[38] This version was made public through the websites of the signatory countries and corresponds to the draft version that was subsequently used for the legal scrubbing, which introduced fundamental changes in many chapters of the Agreement.

[39] The original text stated: 'For greater certainty, nothing in this Agreement shall prevent the Central American Parties from maintaining their existing legal instruments of Central American integration, adopting new legal instruments of integration, or adopting measures to strengthen and deepen these instruments, provided that such instruments and measures are not inconsistent with this Agreement'. The text underlined by the authors gave rise to the interpretation that any origin regime other than that negotiated in DR-CAFTA was eliminated.

[40] Article 3.3, para. 3.

shall receive treatment similar to that accorded to inputs from countries outside the Agreement. These notes also make direct shipment mandatory, which means that if the commercial operation is to be carried out along this axis, the products must be transported directly between the Central American countries and the Dominican Republic and that if, for some transport-related reason, the shipment must be routed through the United States, the goods must remain in the custody of the United States Customs Service in order to retain their originating status.

As far as specific rules of origin were concerned, the Dominican Republic and the Central American countries agreed on an Appendix containing rules that were less demanding than those contained in DR-CAFTA and similar to those that had been previously negotiated by the six countries in their FTA (Appendix 3.3.6, Special Rules of Origin), but that, for textiles and garment, had not entered into force in any country. These are simple rules of origin based on changes in tariff classification. Some chapters on textiles were negotiated bilaterally with each Central American country. Finally, this Appendix also makes provisions for considering the assembly of parts as a substantial transformation that confers origin.

It should be pointed out that the coexistence of multiple origin regimes by no means constitutes an error in negotiation modality in DR-CAFTA. On the contrary, we believe that it represents a step forward because it paves the way for the construction of a well-articulated system that can derive strength from two features of the Agreement: the confidence generated by a stable regulatory framework; and the advantages stemming from the creation of a new space that facilitates the free circulation and accumulation of originating goods among its member countries.

In concluding our analysis of tariffs and origin, it is important to emphasise that the multilateral aspect of DR-CAFTA applies only to the commitments made within the framework of DR-CAFTA; in other words, along the first axis mentioned above. It does not apply to intra-Central American commitments or to those made by Central America with the Dominican Republic.

7. CONCLUSIONS: LESSONS FROM DR-CAFTA FOR THE PROMOTION OF CONVERGENCE

DR-CAFTA is a microcosm that brings to light many of the same concerns and queries that have been voiced in the Americas regarding the coexistence, overlapping and convergence of agreements. Analysing this Agreement, therefore, is a particularly useful exercise. We do not pass judgement on the content of the Agreement from the point of view of disciplines, commitments and trade-offs. We recognise that for clarity's sake, some elements in the architecture of the Agreement could have been framed in a better way, for example, the treatment of remanufactured goods. However, there are some elements in the architecture of

the DR-CAFTA that could serve as inspiration for developing convergence techniques for other negotiation initiatives in the Hemisphere, such as the FTAA or any other large regional integration scheme, such as the ALADI Free Trade Space.

Perhaps one of the main lessons to be learned from DR-CAFTA in this respect is that promoting a forced and automatic convergence is not politically feasible and can turn into an operational nightmare. DR-CAFTA has managed to consolidate three trade axes into a single agreement and has, since the outset, established a framework of market access commitments that offer trade operators flexible alternatives. The best scheme, therefore, seems to be one that allows commitments to function on a multilateral level while still respecting and upholding obligations established in other, deeper trade agreements. The main convergence techniques used in DR-CAFTA were as follows:

- the multilateral application of commitments among all the member countries regarding the disciplines established in the Agreement, with few exceptions;
- an input accumulation scheme that allows inputs and production processes carried out within the seven countries, except products subject to TRQs, to be considered as originating products;
- a timid attempt to extend accumulation to countries that are not members of the Agreement (Canada and Mexico) in the case of a limited number of goods (Chapter 62 of the Harmonised System: textiles);
- accession possibilities for third countries within a framework that encourages the incorporation of new partners but without modifying the main texts of the Agreement;
- the elimination of some pre-existing agreements that are no longer needed in the new context.

The issue of convergence needs to be broached with pragmatism and flexibility. DR-CAFTA shows that non-dogmatic approaches can allow apparently conflicting national and regional objectives to coexist.

DR-CAFTA also shows that each member country's special peculiarities can to some extent be taken into account by incorporating differential treatment into tariff elimination categories and other market access elements that accommodate specific interests regarding some sensitive products. With a bit of creativity, multiple trade agreements that have been negotiated among the parties over almost 50 years can be consolidated into a single legal instrument. Such consolidation can revitalise the subregional integration process and ensure that it continues parallel to the ambitious and rapid tariff liberalisation efforts undertaken with an important trading partner. More importantly, approaches that permit such coexistence can effectively function as catalysts for deepening subregional integration. Thanks to DR-CAFTA, conditions in Central America are now more conducive to defining, for example, a clear and feasible course

of action that will lead to the establishment of a real common external tariff conducive towards a true CU. It is relevant to add that should Central America decide not to deepen its integration process, it risks extinction due to loss of relevance.

The DR-CAFTA approach neither deliberately nor necessarily leads to the perfect convergence of agreements within a specific time frame. It is far more pragmatic than that. Economic operators will be the ones to define the future need to favour one particular trade scheme over another or whether to abandon one for another. This is of great political importance to the participating countries because it means they will not be forced to assume rigid commitments and will thus continue to have adequate room for manoeuvre in more significant negotiations, such as the FTAA.

This pragmatic approach also has the advantage of reconciling two important objectives; first, to reduce the uncertainty generated by the acceptance of an agreement that makes negotiated commitments multilaterally applicable and the consolidation of multiple agreements; and second, to maintain the predictability, legal security and market access conditions that trade operators enjoy in their intra-regional transactions.

This pragmatism carries an implicit cost, however. The implementation and administration of the Agreement will be far more expensive for the Central American countries as hub than for the other parties as spokes. If DR-CAFTA had replaced three agreements with one new one, its implementation and administration would be less complicated. This would have meant, however, among other things, casting aside the Central American integration process.

Another important lesson in convergence can be derived from the system DR-CAFTA used to permit a third country, the Dominican Republic, to accede to the Agreement. In order to become a member, the Dominican Republic had to accept most of the disciplines set forth in the original CAFTA text and was effectively granted only limited or no capacity to introduce any changes. In fact, it was only permitted to negotiate market access terms that would allow it to protect some national interests regarding sensitive products through bilateral negotiations. Even these terms had to be in keeping with the parameters and modalities established in the original CAFTA. The disciplines were not subject to any modification. In brief, latecomers have a price to pay.

Convergence must be pursued at the hemispheric level. A number of imperfect CUs are operating in conjunction with a multitude of more shallow agreements (notably FTAs) in the Americas at the moment, and the real problem of the spaghetti bowl lies in the proliferation of these FTAs. Although there is a need to strengthen the CUs in the subregions of the Americas (to avoid extinction due to loss of relevance amidst competing integration projects), there is an even greater need to promote the convergence of the various FTAs.

The convergence of the FTAs is not only an urgent but also a highly complex issue. The proliferation of FTAs in the Americas is at the point of touching off a fragmentation of the hemispheric trading system, the effects of which are potentially highly negative. The issue needs to be urgently addressed so that this can be avoided before the interest groups become so entrenched that the task becomes unmanageable.

Convergence instruments have different applications according to the subject area in which they are implemented. The convergence process for tariffs differs considerably from the convergence process for rules of origin, for example. Tariff liberalisation processes are themselves convergent in the long term. The fact that tariff negotiations are usually organised as bilateral processes and that liberalisation is almost always gradual facilitates the long-term convergence towards free trade and endows it with flexibility. When it comes to origin regimes, however, convergence is a much more complex process. A combination of elements is needed: a multilateral application scheme; temporary flexibility so that economic operators can adjust their production to the system that best suits them; and the coexistence of various schemes whose use varies according to the relative importance of each market and their contestability by the traders. Obviously, the gravitational force of the largest markets might contribute to the gradual extinction of other, smaller origin regimes. If all these elements are present, the transition towards a final convergence will be facilitated.

In different locations and with different degrees of intensity, the countries of the Americas have already initiated the convergence process. Despite the lack of coordination among these various efforts and the different mechanisms and objectives involved, they all exceed the geographical scope of current agreements.

The convergence initiatives that involve countries from Canada to Panama reveal the need to pursue the convergence of the operational aspects of agreements, starting with rules of origin for goods. DR-CAFTA has established a new subregion amid the multitude of integration areas operating in the Americas that could function as a pole in a broader framework of trade convergence initiatives north of the equator. The other pole in the Americas may continue to be MERCOSUR (although the lack of progress in this integration project casts doubts on its likelihood of becoming a strong gravitational force), or the future ALADI Free Trade Space. If the South American Community of Nations moves forward, it may become the other pole.

An optimistic view of the situation would conclude that the creation of these subregions will gradually facilitate future hemispheric convergence by reducing the number of actors and interests involved. Mexico and Chile could become ‘hinge’ countries in future hemispheric convergence processes.

A less optimistic view of the situation would claim that the establishment of these new subregions might, however, split the hemispheric trading system into

two consolidated blocs.[41] It should be pointed out, however, that the scope of either of these two scenarios would represent progress in operational terms for the region's integration processes as they would increase convergence and largely resolve the current problem of the spaghetti bowl.

Progress in integration in the Americas therefore seems to take two steps forward and one step back. It is a slow and difficult process of evolution that alternates between explosive processes (the spaghetti bowl) and implosive ones (convergence). Final convergence is not necessarily bound to happen. How the story will end is still unclear. Some recent developments indicate, however, that regional integration is gradually regaining momentum and will be achieved through stages of partial subregional convergence that more accurately reflect the new alliances and arrangements emerging among the forces, ideas and influences at play in the Americas. Convergence is undoubtedly facilitated by the presence of hegemonic actors. As in many trade negotiation processes around the world, power is the ultimate driving force when there are multiple and diverse actors and interests.

In the end, DR-CAFTA is not about convergence. It is about the accommodation of diverging trade axes and interests. The architecture employed and techniques used in the Agreement, however, may facilitate a new type of simpler agreement over the long term that may help to eradicate the main problems arising from the spaghetti bowl. Thus, convergence in the Americas is simply a process towards an end product or products that remain to be seen.

Despite the current impasse, for the sake of trade convergence in the Americas and for many other reasons, preventing the FTAA from becoming just another four-letter word is still a relevant endeavour. The seeds of a third generation of trade agreements in the Americas – the convergence generation – have already been sown. These agreements, which will require at least flexible trade liberalisation, some kind of origin accumulation among all the countries, and the harmonious coexistence of different origin regimes should already figure among the future plans of trade policymakers.

[41] This fracture may be seen by some as the trade manifestation of a broader political divide in the Americas. See more in Shifter and Jawahar (2006).

APPENDIX A

BOX A1
Regional Trade Agreements in the Western Hemisphere
(by year of signature)[42]

1960s

1. Central American Common Market (CACM) 1960
2. Latin American Free Trade Association (ALALC) 1960
3. Andean Community (AC) 1969

1970s & 1980s

4. Caribbean Community (CARICOM) 1973
5. Latin American Integration Association (ALADI) 1980
6. US-Israel 1985
7. Australia, Brunei, Canada, Chile, China, Hong Kong, Indonesia, Japan, Korea, Malaysia, Mexico, New Zealand, Papua New Guinea, Peru, Philippines, Russia, Singapore, Chinese Taipei, Thailand, US, Vietnam (APEC) 1989

1990s

8. Southern Cone Common Market (MERCOSUR) 1991
9. Canada-Mexico-US (NAFTA) 1992
10. Chile-Venezuela 1993
11. Colombia-Chile 1994
12. Colombia-Mexico-Venezuela (G-3) 1994
13. Costa Rica-Mexico 1994
14. Bolivia-Mexico 1994
15. Bolivia-MERCOSUR 1996
16. Canada-Israel 1996
17. Canada-Chile 1996
18. Chile-MERCOSUR 1996
19. Mexico-Nicaragua 1997
20. CACM-Dominican Republic 1998
21. Chile-Peru 1998
22. Chile-Mexico 1998
23. CACM-Chile 1999

[42] Not all of the 72 ALADI agreements are included in this list. Some partial scope agreements are not included. For a full list see www.aladi.org

2000–2003

24. Mexico-European Community 2000
25. Mexico-Northern Triangle (El Salvador, Guatemala, Honduras) 2000
26. CARICOM-Dominican Republic 2000
27. Mexico-EFTA 2000
28. Mexico-Israel 2000
29. US-Jordan 2000
30. Canada-Costa Rica 2001
31. CACM-Panama 2002
32. Chile-European Community 2002
33. El Salvador-Panama 2002
34. Chile-South Korea 2003
35. Chile-EFTA 2003
36. Chile-US 2003
37. MERCOSUR-India (framework agreement) 2003
38. Mexico-Uruguay 2003
39. Panama-Taiwan 2003
40. US-Singapore 2003

2004–2006

41. CARICOM-Costa Rica 2004
42. Central America – DR – US (DR-CAFTA) 2004
43. Mexico-Japan 2004
44. US-Morocco 2004
45. US-Australia 2004
46. US-Bahrain 2004
47. Andean Community-MERCOSUR 2004/2005
48. Chile-China 2005
49. Chile-New Zealand, Singapore, Brunei 2005
50. Guatemala-Taiwan 2005
51. Panama-Singapore 2005
52. Peru-US 2005
53. Colombia-US 2006

APPENDIX B

BOX A2
Special Tariff Treatment
between the Dominican Republic and Central America
Incorporated into DR-CAFTA

1. Appendix 3.3.6.4. This appendix lists the products that are excluded according to the General Notes, including sugar and coffee. It also stipulates that negotiations for certain goods must be held within one year. If no agreement is reached in that time, a special timetable listed in General Notes 7b is activated. These products were not permanently excluded and are listed in Appendix 3.3.6.4, but the products from the following General Notes are excluded: those of notes 7a to 11a of the Dominican Republic and note 7a of the five Central American countries.
2. Annex 3.3.6, para. 2. A fixed maximum duty of 15 per cent is set for these products and the need to enter into bilateral negotiations in accordance with General Notes para. 8 is stipulated.
3. National Exclusions: These exclusions are reciprocal, permanent and listed in the General Notes of each country (*).
4. Excluded goods that are, however, subject to an agreed plurilateral elimination schedule. Crude oil is referred to specifically (see Annex 3.3.6, para. 3).
5. Products subject to bilateral tariff rate quotas: the products listed in Appendix 2 to the General Note of Costa Rica and Nicaragua and Appendices 2 and 3 of the Dominican Republic. These products must be negotiated within one year.

(*) The exceptions are:

a. Dominican Republic-Costa Rica: beer, beans, rice, onions, alcohol and tobacco. Stipulated in General Note 7a of the Dominican Republic and in General Note 7a of Costa Rica.
b. Dominican Republic-El Salvador: chicken, powdered milk, rice, beans, wheat flour, beer, alcohol and tobacco. Stipulated in General Note 8a of the Dominican Republic and in General Note 7a of El Salvador.
c. Dominican Republic-Guatemala: chicken, powdered milk, rice, beans, wheat flour, beer, alcohol and tobacco. Stipulated in General Note 9a of the Dominican Republic and in General Note 7a of Guatemala.
d. Dominican Republic-Honduras: chicken, powdered milk, rice, beans, wheat flour, beer, alcohol and tobacco. Stipulated in General Note 10a of the Dominican Republic and in General Note 7a of Honduras.
e. Dominican Republic-Nicaragua: beer, alcohol and tobacco. Stipulated in General Note 11a of the Dominican Republic and in General Note 7a of Nicaragua.

APPENDIX C

TABLE A1
Divergences in the Rules of Origin for Subheading 2106.90

H.S. 2002	*Product Description*	*CACM Rule*	*DR-CAFTA Rule*
210690	Food preparations not elsewhere specified or included – Other	A change to heading 21.06 from any other chapter.	
210690*	Sugar syrup of subheading 2106.90		A change to sugar syrups of subheading 2106.90 from any other chapter, except from Chapter 17.
210690*	Concentrated juice of any single fruit or vegetable fortified with vitamins or minerals of subheading 2106.90		A change to concentrate juice of any single fruit or vegetable fortified with vitamins or minerals of subheading 2106.90 from any other chapter except from heading 08.05 or 20.09 or subheading 2202.90.
210690*	Mixtures of juices fortified with vitamins or minerals of subheading 2106.90		A change to mixtures of juices fortified with vitamins or minerals of subheading 2106.90: (A) from any other chapter, except from heading 08.05 or 20.09 or from mixtures of juices of subheading 2202.90; or (B) from any other subheading within Chapter 21, heading 20.09 or from mixtures of juices of subheading 2202.90, whether or not there is also a change from any other chapter, provided that a single juice ingredient, or juice ingredients from one non-party to the Agreement, constitute in single strength form no more than 60 per cent by volume of the good.

TABLE A1 *Continued*

210690*	Compound alcoholic preparations of subheading 2106.90	A change to compound alcoholic preparations of subheading 2106.90 from any other subheading except from heading 22.03 to 22.09.
210690*	Goods containing over ten per cent by weight of milk solids of subheading 2106.90	A change to products containing over ten per cent by weight of milk solids of subheading 2106.90 from any other chapter, except from Chapter 4, or from dairy preparations containing over ten per cent by weight of milk solids of subheading 1901.90.
210690*	Other products of subheading 2106.90	A change to other goods of heading 21.06 from any other chapter.

Notes:
*Partial openings.
This tariff line (2106.90), which constitutes the most important intra-Central American trade item, provides a good example of the differences in treatment that a DR-CAFTA rule of origin may have *vis-à-vis* the CACM origin regime. The level of difference in this example, however, is rather extreme and is not typical.

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