INTERNATIONAL REGULATION OF CARIBBEAN TEXTILE AND APPAREL TRADE

Georgina Ines Chaves Olarte (c)

Institute of Comparative Law

McGill University, Montreal

August, 1993

A Thesis submitted to the Faculty of Graduate Studies and Research in partial fulfilment of the requirements of the degree of Master of Laws.

To my parents

ACKNOWLEDGEMENTS

I wish to thank the supervisor of this thesis, Prof. A. L. C. de Mestral, for his very useful advice throughout the preparation of this work.

My thanks are also addressed to the Canadian International Development Agency (CIDA) for the financial support given to me during the Master's program. As well, I am very grateful to the staff of the Institute of Comparative Law and of the McGill Law Library for their able assistance.

Finally, I wish to thank my parents for their unconditional support.

ABSTRACT

In the last five years, textiles and apparel have represented the largest source of growth of U.S. imports from countries covered by the Caribbean Basin Initiative. The economic importance of this sector to the Caribbean countries gave rise to this study which discusses the international regulation of textile and apparel trade and the possible effects of the Uruguay Round of Multilateral Trade Negotiations and the North American Free Trade Agreement on the Caribbean textile and apparel industry. This analysis takes into account not only the legal mechanisms developed to control trade in this sector, but also the underlining powers that have allowed the shaping of the current textile and apparel order. Special emphasis is placed on U.S. trade policies toward the Caribbean Region which have played a significant role in the present development of the Caribbean apparel industry.

RESUME

Pendant les cinq dernières années, les tissus et les vêtements ont constitué la plus importante source de croissance des importations américaines provenant de pays couverts par le "Caribbean Basin Initiative". L'importance économique de ce secteur pour les pays des Caraïbes a donné lieu à cette étude qui traite de la réglementation internationale du commerce des tissus et des vêtements ainsi que des effets éventuels des négociations commerciales multilatérales de l'Uruguay Round et de l'Accord de libre échange nord-américain sur l'industrie des tissus et des vêtements dans les pays des Caraïbes. Cette analyse prend en considération non seulement les mécanismes légaux développées pour contrôler le commerce de ces produits mais aussi les forces sous-jacentes qui ont permis l'établissement de l'ordre actuel dans ce secteur. Les politiques commerciales américaines face à la région des Caraïbes qui ont joué un rôle important dans le développement actuel de l'industrie des vêtements des Caraïbes, se verront accorder une attention particulière.

TABLE OF CONTENTS

INTRODUCTION 1

CHAPTER I: THE MULTIFIBER ARRANGEMENT (MFA) 3

SECTION I: General Overview 3

A. Early Development of International Textile Trade 3
B. Evolution of International Textile Trade Law 8
C. The GATT and the MFA 13

SECTION II: MFA Safeguard Framework 15

A. Safeguard measures 15
B. Limitations on Restraint Actions 17

1. Base Level, Growth Rate and Flexibility 17
2. Treatment of Small Suppliers, New Entrants, Least Developed Countries and Offshore Assembly Countries 19

SECTION III: MFA Effects on Textile and Apparel Trade 21

A. Proliferation of quotas and supplier countries 22
B. Cheating and Trade Diversion 24
C. High Costs to Consumers 25

CHAPTER II: U.S. TRADE POLICIES TOWARDS THE CARIBBEAN REGION 26

SECTION I: The Caribbean Basin Initiative (CBI) 27

A. The Caribbean Basin Economic Recovery Act (CBERA) 28
B. Operative means 29

1. Beneficiary Countries 29
2. Rules of Origin 31
3. Ordinary and Necessary Business Expenses Allowance 32

C. Effectiveness 34
D. Recent Developments: The CBI II 38

SECTION II: U. S. Harmonized Tariff Schedule Subheading 9802.00.80 39

A. General Overview 41

1. Subheading 9802.00.80: U.S. Components Assembled Abroad 43
2. The CBI Special Access Program 45

B. Textile and Apparel Imports under Subheading 9802.00.80 47
C. U.S. "National Interest" Viewpoint 51

CHAPTER III: RECENT DEVELOPMENTS IN INTERNATIONAL TRADE AND ITS EFFECTS ON THE CARIBBEAN TEXTILE AND APPAREL INDUSTRY 54

SECTION I: The Uruguay Round: Phasing Out the MFA 54

A. Liberalizing Textile Trade: A General Overview 54

B. The Dunkel Text 62

1. The integration Process 64
2. The Transitional Safeguard Mechanism 68
3. Treatment of Least Developed Countries, Small Suppliers, Small Wool Suppliers and Offshore Assembly Countries 71

C. Possible Effects of a Successful Uruguay Round in Textiles and Clothing on the CBI countries 73

1. Nature of the Caribbean Apparel Industry 73
   a. Producing in the Caribbean 73
   b. The Caribbean Apparel "Maquiladoras" 75
2. The Uruguay Round and the Caribbean Apparel Industry 78
   a. The Hypotheses 78
   b. The Dunkel Text 79

SECTION II: The North American Free Trade Agreement 81

A. Textile Trade under NAFTA 82

1. Rules of Origin 82
2. Tariff Elimination 84
3. Quantitative Restrictions 85

B. The Mexican Apparel "Maquiladora" 87

C. Foreseen Consequences of NAFTA on the Caribbean Textile and Apparel Industry 90

CONCLUSION 95

BIBLIOGRAPHY 97

ANNEXES 112

INTRODUCTION

Trade in apparel and textiles is one of the more protected sectors at the international level. The early protectionist tendencies in industrialized countries required the establishment of an international textile trade regime that, as an exemption to the General Agreement on Tariffs and Trade, could legally justify the use of quantitative restrictions on a discriminatory basis.

Over time, the international regulation of textiles and apparel has become increasingly tightened, thus impeding or delaying the natural emergence of the industry in developing countries.

Particularly, the apparel sector, in which developing countries have a comparative advantage, is an important source for the economic growth and further development of the Third World. Liberalization of textile and apparel trade, together with agricultural trade, may represent a unique opportunity for developing countries to participate more fully in the international trading system.

The configuration of the textile industry in developing countries is not homogeneous. While some efficient suppliers such as Hong Kong, Taiwan, Korea and China have developed a vertically integrated textile industry, others, such as the Caribbean and Central American nations, have been basically sites for offshore apparel production.

This paper analyses specifically the textile and apparel industry of the countries under the U.S. Caribbean Basin Initiative, mainly, the countries of the Caribbean Sea and Central America (Caribbean countries), and its relationship with the international textile trade regime.

Apparel is at present the largest source of growth of U.S. imports from CBERA countries. Therefore, its study is imperative in the formulation of any future strategy of regional development. Although our study is focused on the current regulation of textile and apparel trade in the Caribbean Basin, and the possible implications the liberalization of this sector could have for the region, reference is made to the importance of this industry as a mechanism for promoting development in the Caribbean Region on a sustained basis.

The first chapter studies the international regulation of textile and apparel trade from an historical and legal point of view. The evolution of the "Arrangement Regarding International Trade in Textiles" (Multifiber Arrangement) is analyzed taking into account the political forces in industrialized countries that have determined the current legal structure of trade in textiles. A legal study of the main provisions of the Multifiber Arrangement is also included together with a general comparison of the principles that govern trade under the GATT and those that rule textile and apparel trade. Finally, the effects that the Multifiber Arrangement have generated at the international level, particularly in the development of the textile and apparel sector, are enumerated and analyzed.

The U.S. trade policies with respect to the Caribbean Region are studied in the second chapter. The United States is at present the biggest market for Latin America and the Caribbean, and as such, its trade policies toward the region are of extreme importance for the growth of their economies. In this chapter, we study the Caribbean Basin Initiative and the U.S. offshore assembly provisions, that is, subheading 9802.00.80 of the Harmonized Tariff Schedule of the United States. The development of the Caribbean textile and apparel industry is analyzed taking into account the policies implemented by the United States in the Caribbean Basin and the U.S. underlying interests in the Region.

Finally, the last chapter studies the present tendencies of textile and apparel trade liberalization and the possible effects of such strategies on the Caribbean textile industry. Special emphasis is made on the Uruguay Round of Multilateral Trade Negotiations, and its attempt at "phasing-out" the Multifiber Arrangement. The regulation of textile trade under the North American Free Trade Agreement is also included, taking into account its significance for the Caribbean Basin.

CHAPTER I: THE MULTIFIBER ARRANGEMENT

SECTION I: General Overview

A. Early Development of International Textile Trade

The textile sector has usually played a crucial role in the early industrialization process of developed countries. Britain, the United States, France, and Germany, among others, showed strong comparative advantage in textile and apparel in the early stages of industrialization.[1]

At present, the textile and clothing industries are still a very important sector in the economies of developed countries. The industrialized countries have developed protectionist policies towards this sector due to its political and economic significance in the national economies[2]. Indeed, any incursion of low-cost textiles and apparel imports has generally generated the opposition from the national industry, and the governments have usually answered positively to its pleas[3]. The trade policy in clothing and textiles in the last century has been characterized by an "above-average level of government intervention"[4].

---

[1] Dilip K. Das, "Dismantling the Multifibre Arrangement" (1989) 19 Journal of World Trade Law 67 at 68-69.

[2] "Clothing industries are often a very large part of an economy, employing many people; and these are often distributed among a wide variety of locations, which adds to their political importance". John H. Jackson, *The World Trading System* (Massachusetts: The Massachusetts Institute of Technology, 1989) at 182.

[3] "In the late 1940s [in the United States], the industries requesting import protection tended to be relatively small and not very influential politically. However, by the mid 1950s the politically powerful cotton textile, coal and domestic petroleum industries, whose employees tended to vote Democratic, were asking for protection. In 1955, the Eisenhower administration, as part of its efforts to obtain the support of the Democrats for its liberalization efforts, pressured the Japanese into voluntarily restricting their exports of cotton textiles to the United States". Robert E. Baldwin, *Trade Policy in a Changing World Economy* (Chicago: The University of Chicago Press, 1988) at 26.

[4] GATT, *Textiles and Clothing in the World Economy* (Geneva: GATT, 1984) quoted by Jackson, *supra* note 2 at 181.

The problem of protectionism in textiles and apparel trade is not new[5]. Indeed, as early as 1936 Japanese textile exports to the United States were limited through a voluntary export restraint[6] agreement. This was the first significant use of voluntary export restraints as a mechanism of solving trade disputes. Negotiations between U.S. and Japanese producers began due to the massive influx of Japanese cotton textiles. Japanese cotton textiles imports in the U.S. grew from 1.22 million square yards in 1929 to 7.29 million square yards in 1936. For 1937 it was projected to reach 150 million square yards. By the 1936 agreement deliveries were limited to 155 million square yards in 1937 and to 100 million square yards in 1938. The arrangement was renewed for two more years in 1938, establishing a limit of 100 million square yards yearly[7].

Japanese cotton capacity was, however, seriously damaged in World War II. As the cotton textile industry had been the basis of Japanese industrialization, its recovery became the immediate aim of the Government[8]. Moreover, the U.S.

---

5 "... in 1936 Japanese export cotton textiles were subject to quantitative restrictions in 40 out of 106 exports markets". Horst Gunter Krenzler, "The Multifibre Arrangements as a Special Regime under GATT", in Meinhord Hilf, Francis G. Jacobs, Ernst-Ulrich Petersmann, eds., *The European Community and GATT*, Vol. 4 (Deventer: Kluwer, 1986) at 143.

6 "Voluntary export restraint is a form of trade restriction distinguished by the fact that the exporting country controls the limitation on trade. Such action is termed 'voluntary' in the sense that the exporting country formally imposes it unilaterally and could technically modify or eliminate it. In reality, however, 'voluntary' export restraint is a response to pressures from an importing country that typically threatens unilateral import restrictions against the exporter." Kent Jones, "Voluntary Export Restraint: Political Economy, History and the Role of the GATT" (1989) 23:3 Journal of World Trade Law 125. John H. Jackson, *World Trade and the Law of GATT* (Indeanapolis: the BOBBS-MERRILL COMPANY, INC., 1969) at 572.

7 "Japan negotiated similar agreements with Burma, India, Australia and the United Kingdom during the 1930s. The arrangements reportedly involved the *quid pro quo* of tariff reduction, pledges not to raise tariffs, and in some cases reciprocal barter agreements. In the case of India, for example, the Japanese export limit was dependent on levels of Japanese purchases of Indian goods". Jones *ibid.* at 129.

8 I. M. Destler, Haruhiro Fukui & Hideo Sato, *The Textile Wrangle: Conflict in Japanese-American relations, 1969-1971* (London: Cornell University Press, 1979) at 29. "Japan is perhaps the best-known example of the use of government policies to improve international competitiveness. During the 1950s and 1960s the Japanese government guided the country's industrial expansion by providing tax incentives and investment funds to favoured industries". Baldwin, *supra* note 3 at 212.

postwar policy was also directed to Japan's economic resurgence. Not only did the U.S. provide advanced technology, financial help, and a market for Japanese exports, but it also pressed for Japan's entry into the GATT. Japanese economic success was seen by U.S. leaders as a must if her democracy and alignment were to be maintained[9].

Although the U.S. pressed for non-discriminatory treatment of Japanese goods in the international arena, both countries justified the establishment of restrictions on Japanese imports. Special restrictive agreements were then placed in those areas where Japanese imports "aroused political reactions strong enough to threaten both the larger U.S. free-trade policy and amicable U.S.-Japanese alliance"[10].

The Japanese economic rehabilitation was soon successful[11], and a new trend of discrimination against Japanese goods was initiated. In 1955 President Eisenhower pressured the Japanese into voluntarily restricting their exports of cotton textiles to the United States, and in 1957 a five-year voluntary restraint agreement was negotiated[12].

Thus, the postwar period was characterized by very restrictive trade regimes affecting textiles. This trade area remained untouched by the trade liberalization

---

9 Destler, Fukui & Sato, *ibid.* at 24-29.

10 *Ibid* at 25.

11 "By 1950 the value of Japan's cotton textile exports had recovered to exceed the 1934-36 average. By 1955 these exports had not only grown further worldwide but had also penetrated the American market in dramatic fashion". *Ibid* at 29.

12 Pamela A. Bannon, "Trade Relief: A Benefit or Burden for the Textile and Apparel Industries?" (1987) 19 New York University Journal of International Law and Politics 701 at 706. "The 1957 agreement was precedent-setting not only in the fact of its conclusion but also in the form of the restrictions it imposed. It was *comprehensive* in that it combines an overall quantitative limit on Japanese cotton textile exports--235 million square yards--with limits on narrower groups of products and categories within groups. For example, 113 million square yards of cotton cloth were permitted, within which there was a sublimit of 2.5 million for velveteens." Destler, Fukui & Sato, *ibid.* at 30.

process leaded by GATT[13].

The developed countries experienced an extraordinary growth of manufactured imports in the 1950s. Japanese exports alone increased over 600 percent from 1949 to 1959[14]. The major concern of the developed countries was the low-wage factor reflected in the Japanese low-export pricing[15]. Thus, a different treatment between imports coming from industrialized countries and those coming from Japan was justified in the low labour costs of the latter.

Discrimination through quantitative import restrictions was the common policy followed against Japanese goods[16]. This tendency was not stopped by Japan's accession to the GATT, in 1955, since some countries continued to require voluntary restraints to its exports[17].

In the late 1950s, some developing countries such as Egypt, Hong Kong, India,

---

[13] GATT, *Textiles and Clothing in the World Economy* (Geneva: GATT, 1984) quoted by Jackson, *supra* note 2 at 181.

[14] "These exports were concentrated in a narrow range of standard-technology, labour-intensive, manufactured goods, such as textiles and clothing, footwear, tableware, plywood and, later, optical goods and certain electronic products". Frank Stone, *Canada, The GATT and the International Trade System* (Montreal: The Institute for Research and Public Policy, 1984) at 99. See also Kenneth W. Dam, *The GATT: Law and International Economic Organization* (Chicago: The University of Chicago Press, 1970) at 228.

[15] Stone, *ibid.* note 14 at 99. "The view of Japan as a threat in world trade--a country that exploited cheap labour and undercut its competitors--had deep historical roots. Nonetheless, it was not a major influence on senior U.S. officials until the 1960s brought (1) a reversal of the U.S.-Japanese trade balance, with Japanese exports suddenly exceeding imports; (2) a remarkable change in the commodity composition of Japanese exports to the United States, with the rapid expansion of sales of high-quality, technologically sophisticated industrial products; (3) a crisis in the overall U.S. trade and payments balance; and (4) an acceleration of Japan's remarkable postwar economic growth to the point where Japan became number two capitalist economic power". Destler, Fukui & Sato, *supra* note 8 at 26-27.

[16] The U. S., many Western European countries, Britain and Australia, among others, gave discriminatory treatment to Japanese exports during the 1950s. Stone, *ibid.* at 100.

[17] "When Japan entered GATT in 1955, a number of GATT members from Europe invoked GATT Article XXXV, which allows a member to refuse to enter into GATT commitments with a new member". Robert Hudec, *The GATT Legal System and World Trade Diplomacy* (New York: Praeger Publishers, 1975) at 212.

Portugal, South Korea and Spain[18] became significant exporters of manufactured goods, particularly cotton textiles. However, the precedents already established in relation with Japanese goods gave rise to similar restrictive controls against their exports[19].

The retention of quantitative restrictions on textiles and apparel in a world proclaiming trade liberalization required, therefore, legal justification. Thus, in 1959 the problem was placed in the GATT agenda as "the question of avoidance of market disruption". A working party was then established to study the problem and concluded that the avoidance of market disruption was an appropriate safeguard, within the GATT system, to protect the legitimate interests of importing countries[20].

The working party's argument did not focus on any specific reprehensible operation in the developing countries. It simply resorted to the labour comparative advantage of developing countries[21] and considered it as the cause of disruption in industrialized countries.

Subsequently, the Contracting Parties adopted the definition of market disruption[22] in a decision that gave it international recognition[23]. They also established the existence of a Permanent Working Party on Avoidance of Market

---

18 "Hong Kong became the largest new source of American imports, evidenced by a rise in its share of the U.S. market from 13.8% in 1958 to 27.5% in 1960". Bannon, *supra* note 12 at 706. See also Stone, *supra* note 14 at 102.

19 "By the late 1950s, a number of industrialized countries, including Canada, had concluded bilateral arrangements involving export restraints on various products with several Asian exporters, such as Hong Kong, India and South Korea". Stone, *ibid.*

20 Dam, *supra* note 14 at 299.

21 "...the GATT report [GATT Textiles and Clothing in the World Economy (Geneva: GATT 1984)] notes that [the argument which sustains that developing countries have a comparative advantage when referring to clothing and textiles] only holds good as long as the production of textiles is dependent upon abundant low-skilled labour. The increased levels of automation in the textile industry have possibly moved the comparative advantage back to industrialized, developed countries". Jackson, *supra* note 2 at 365.

22 See Chapter I, Section II (A), below.

23 GATT C.P. Dec. (19 Nov 1960), 19th supp. B.I.S.D. (1960) at 26-28.

Disruption. Nevertheless, this working party apparently never functioned, and the developed countries addressed the dramatic increase of cotton textile imports through the adoption of international agreements[24].

B. Evolution of International Textile Trade Law

The first multilateral agreement established to face the constant increase in textiles imports from some developing countries, such as Hong Kong, India and Pakistan[25], was the 1961 Short-Term Arrangement Regarding International Trade in Cotton Textiles (STA)[26].

President Kennedy promised to assist the U.S. textile industry due its dissatisfaction with the uncontrolled rise in textile imports during the 1950s. In his 1961 "Seven Point Textile Program" he called for an international conference in order to discuss the avoidance of "undue disruption of established industries"[27].

Kennedy's strategy was twofold: On one hand, it intended to appease the domestic industry. On the other, it was directed to reach a multilateral response to the textile problem that was not contrary to his well-known objective of freer world trade. While European countries invoked GATT article XXXV to keep out low-cost textile imports, the United States did not have a legal instrument to rely on when limiting imports. The negotiation of a multilateral agreement on cotton-textiles was, therefore, essential to liberalize European markets and to legalize export restraint

---

24 "One of the reasons that the general approach to market disruption problems never came to anything in GATT may be because the most acute problem of market disruption existed with respect to cotton textiles and, as an outgrowth of this effort on market disruption, special committees and other arrangements were developed for handling cotton textiles". Jackson, *supra* note 6 at 572.

25 Dam, *supra* note 14 at 300.

26 *Short-Term Arrangement Regarding International Trade in Cotton Textiles*, GATT C.P. (21 July 1961), 18th & 19th sess., 10th supp. B.I.S.D. (1962) 18 [hereinafter *STA*].

27 Thomas B. Curtis & John Robert Vastine, Jr., *The Kennedy Round and the Future of American Trade* (New York: Praeger Publishers, 1971) at 165.

agreements[28].

Although the STA was directed to legitimize VERs, Japan supported the negotiations. For Japan, the STA represented a means to avoid its continued loss of U.S. market shares and a possible alleviation of European fears to its exports[29].

From the proclamation of President Kennedy's Seven Point Textile Program, there was a series of agreements that restricted textiles exports from developing countries. In 1962 the Long-Term Arrangement Regarding Trade in Cotton Textiles (LTA)[30] was negotiated. It was later substituted by the 1974 Multifiber Arrangement that has been renewed in 1977, 1981, 1986, 1991 and 1992.

The LTA, modeled in the STA, was focused in the "orderly growth" of cotton-textile trade. Under the LTA, exporter countries should also establish "voluntary" export quotas in textiles products found to be disruptive in the importing markets. In exchange, all major importers would guarantee a gradually increasing quantity of textile imports[31].

By the early 1970s, the domestic industry, facing the rise of synthetic and artificial fibres, as well as the growth in wool products trade, pressed the U.S. government to negotiate a new international agreement[32]. The LTA was no longer useful due to its limitation on cotton-textiles. Indeed, the legitimation of quantitative restrictions in synthetic and wool textiles exports required another multilateral solution. Thus, in 1973 the Arrangement Regarding International Trade in Textiles

---

28 David B. Yoffie, *Power and Protectionism: Strategies of the New Industrializing Countries* (New York: Columbia University Press, 1983) at 83.

29 *Ibid.*

30 *Long-Term Arrangement Regarding International Trade in Cotton Textiles*, GATT C.P. (9 February 1962), 20th sess., 11th Supp. B.I.S.D. (1963) 25 [hereinafter *STA*].

31 Hudec, *supra* note 17 at 212.

32 Hilf, Jacobs & Petersmann, *supra* note 5 at 143.

or Multifiber Arrangement (MFA)[33] was negotiated in GATT; it entered into force in January 1974.

The MFA was a mutually advantageous compromise involving both developed and developing countries. Industrialized countries would count on an international instrument for limiting imports of practically all textile and apparel products. Bilateral agreements could be negotiated[34], but unilateral action was allowed in the case of market disruption[35]. On the other hand, developing countries would be favoured with the establishment of a Textiles Surveillance Body (TSB) and with the fixing of an annual minimum growth rate of quotas of 6 per cent. The TSB was supposed to guard developing countries' interests, to review actions taken under MFA and to mediate in any dispute related with the application or interpretation of the MFA[36].

The MFA was supposed to control the expansion of trade in textiles through the reduction of barriers and progressive liberalization, while ensuring the orderly development of this trade by avoiding the disruptive effects in individual markets[37].

Furthermore, the MFA was supposedly designed to be a temporary restraint on trade. Developed countries asked for the MFA as a means to give time to the reorganization and adjustment of their textile industries. However, the MFA has become "a more or less permanent feature of world trade in textiles"[38]. Each new MFA extension has generated a more restrictive trade regime. The constant proliferation of bilateral agreements and the imposition of much more restrictive

---

[33] *Arrangement Regarding International Trade in Textiles*, GATT Doc. TEX.NG/1, 30th sess., 21st supp. B.I.S.D. (1973-1974) 3 [hereinafter *MFA*].

[34] *MFA*, art. 4.

[35] *MFA*, art. 3.

[36] Yoffie, *supra* note 28 at 161-162.

[37] *MFA*, art. 1.1.

[38] Nigel Grimwade, *International Trade: New Patterns of Trade, Production and Investment* (London: ROUTLEDGE, 1989) at 355.

quotas[39] has been the feature that has characterized the MFA history.

There have been three major extensions of the MFA. In 1977 the MFA was renewed for the first time (MFA II) for a four year period[40]. The negotiations of MFA II were focused in closing the remaining loopholes in MFA I. The European Community claimed for a more restrictive textile trade regime in order to support its renewal[41]. A "reasonable departure" clause was then established. It allowed the Contracting Parties to depart from specific MFA's provisions if "joint agreement" could be reached on those departures[42]. The safety clause was soon used by industrialized countries in order to reduce the growth rate and restrict the flexibility provisions[43].

In 1981 MFA III entered into force[44]. Again, the increase of textiles imports in the U.S. and European market generated tougher measures. MFA III eliminated the "reasonable departure" clause, but legalized several significant "departures" from the MFA[45]. It permitted agreement in a lower growth rate[46], allowed the

---

39 Roger D. Hansen, *Tariffs, Quotas and Trade: The Politics of Protectionism* (California: The Institute for Contemporary Studies, 1979) at 251.

40 *Protocol Extending the Arrangement Regarding International Trade in Textiles*, GATT (14 December 1977), 33rd sess., GATT Doc. L/4616, 24th suppl B.I.S.D. (1977) 5 [hereinafter *MFA II*].

41 Hilf, Jacobs & Petersmann, *supra* note 5 at 144. "An EEC Commission estimated that a simple extension of the Multifiber Arrangement would cost 1.6 million textile jobs by 1982". Susan Strange, *The Management of Surplus Capacity* at 314 quoted by Yoffie, *supra* note 28 at 163.

42 "Because of the unequal bargaining power of importing and exporting countries, however, 'joint agreement' was not an adequate safeguard". Henry R. Zheng, *Legal Structure of International Textile Trade* (New York: Quorum Books, 1988) at 8.

43 "The Carter administration used its authority under the safety clause to eliminate export growth for Korea, Taiwan and Hong Kong during 1977. Then in 1979-1980 the United States renegotiates the bilateral accords to restrict further these nations' flexibility". Yoffie, *supra* note 28 at 163.

44 *Protocol Extending the Arrangement Regarding International Trade in Textiles*, GATT (22 December 1981), 37th sess., GATT Doc. L/5276, 28th supp. B.I.S.D. (1981) 3 [hereinafter *MFA III*].

45 Zheng, *supra* note 42 at 8.

importing countries to depart from the MFA's basic requirements in the flexibility area[47], and gave importing countries the right to discriminate against exporters with high market shares[48].

In 1986, the third phase of the MFA expired and a new protocol extended the MFA until 1991[49]. Under MFA IV a number of significant modifications that favoured importing countries were introduced[50]. Among other things, MFA coverage was broadened to include vegetable fibres and silk blend fibres[51]. Importing countries were also given more discretion to apply unilateral restrictions under MFA Article 3[52].

MFA IV was renewed in August 1991[53] for a period of seventeen months, and in December 1992, for a period of twelve months[54].

The latter MFA renewals did not include any major changes in the MFA provisions. Nevertheless, the tendency of a steady increase on restrictive measures in textiles and apparel exports from developing countries has continued. *The International Textiles and Clothing Bureau*, when commenting on the operation of the

---

46 "In exceptional cases where there are clear grounds for holding that the situation of market disruption will recur if the above growth rate [6 percent] is implemented, a lower positive growth rate may be decided upon after consultation with the exporting country or countries concerned". *MFA*, Annex B, para. 2. "Under MFA 3, the United States allowed a rate of growth of only 0.5 per cent on two-thirds of textile and clothing imports". *Grimwade*, supra note 38 at 355.

47 *MFA III*, para. 9.

48 *MFA III*, para. 3.

49 *Protocol Extending the Arrangement regarding International Trade in Textiles*, GATT (31 July 1986), 42nd sess., GATT Doc. L/6030, 33rd supp. B.I.S.D. (1986) 7 [hereinafter *MFA IV*].

50 Zheng, *supra* note 42 at 8.

51 *MFA IV*, para. 24.

52 *MFA IV*, para. 8.

53 *Protocol Maintaining in Force the Arrangement Regarding International Trade in Textiles*, GATT (31 July 1991), 47th sess., GATT Doc. COM.TEX/69, 38th supp. B.I.S.D. (1992) 113.

54 *Protocol Maintaining in Force the Arrangement Regarding International Trade in Textiles* (Geneva: GATT, 1992).

MFA[55], has affirmed, among other things, that: a) there had been a greater number of unilateral actions under Article 3 and frequent use of consultation mechanisms leading to automatic imposition of limits and their subsequent prolongation; and b) the objective of avoidance of disruptive effects on individual lines of production in both importing and exporting countries had not been met by some developed countries[56].

Protectionist tendencies of importing countries not only gave rise to the MFA but also have oriented its application and interpretation in a very restrictive way. The textile and apparel sector is, then, one of the world trade areas more accurately restricted in order to avoid disruptive effects in individual markets.

C. The GATT and the MFA

The MFA is an example of managed trade. It allows the establishment of bilateral agreements, and, thus, gives rise to a very restrictive textile trade regime.

The MFA departs from the basic principles of the GATT. While the GATT provides for most favourable nation treatment[57], the MFA allows discriminatory treatment through the legitimation of bilateral agreements. Under GATT's Most-Favourable Nation clause "each contracting party [must] grant to every other contracting party the most favourable treatment which it grants to any country with respect to imports and exports of products"[58]. On the contrary, MFA bilateral agreements are by nature discriminatory since they allow the imposition of quantitative restrictions in a no multilateral basis.

---

55 *Report of the Textiles Committee*, GATT (7 November 1989), 45th sess., GATT Doc. COM.TEX/62, 36th supp. B.I.S.D (1990) 464 at 466-467 [hereinafter *GATT Doc. COM.TEX/62*].

56 Notably in agreements concluded by the United States and Canada. *Ibid.*

57 *General Agreement on Tariffs and Trade*, Geneva (30 October 1947) B.I.S.D., Vol. IV (1969) art. 1 [hereinafter *GATT*].

58 Jackson, *supra* note 2 at 134.

Additionally, the MFA's legalization of quotas violates the GATT prohibition of imposition of quantitative restrictions in import or export products of the Contracting Parties[59]. Under the GATT, the use of quotas is exceptional, being limited to specific cases such as a nation's need to protect its balance of payments[60], national security[61], public health and safety[62], and developing industries[63]. Under GATT Article XIX the imposition of quotas may proceed after the fulfilment of an "injury test". These quotas must be applied in a non-discriminatory fashion, and the exporting countries may have the right to compensation and retaliation. On the contrary, exporting nations under the MFA do not count on any measure against importing countries in order to alleviate the effects of discriminatory quotas.

The MFA completely departs from the basic principles of the GATT. In fact, the MFA legalizes the establishment of quantitative restrictions in a bilateral basis, giving raise to a legal regime characterized by discriminatory treatment. Besides, exporting nations under the MFA are in a less favourable situation that under GATT since they have waived their GATT's rights to compensation and retaliation.

The negative position of exporting countries under the international legal regime of textiles and apparel trade was not modified in the Kennedy and Tokyo Rounds of Multilateral Trade Negotiations. On the contrary, the continuation of the MFA was usually a requirement deemed necessary by importing countries to reduce tariffs in the textile sector[64]. At present, the Uruguay Round of Multilateral Trade

---

[59] *GATT*, art. XI.

[60] *GATT*, arts. XII-XV.

[61] *GATT*, art. XX.

[62] *GATT*, art. XXI.

[63] *GATT*, art. XVIII.

[64] Sanjoy Bagchi "Textiles in the Uruguay Round: Alternative Modalities for Integration into GATT" in Carl B. Hamilton, ed., *Textile Trade and the Developing Countries: Eliminating the Multi-Fibre Arrangement in the 1990s* (Washington: The World Bank, 1990) at 238. See also Alan Oxley, *The Challenge of Free Trade* (New York: St. Martin's Press, 1990) at 105.

Negotiations is contemplating for the first time the integration of this sector into GATT[65].

SECTION II: MFA Safeguard Framework

A. Safeguard Measures

Under the MFA, importing countries are allowed to take unilateral actions and to negotiate bilateral agreements with exporting nations. These measures violate the GATT prohibition on quantitative restrictions and discriminatory treatment since they give rise to the imposition of quotas on an individualized basis. The operation of MFA is focused on the safeguard measures established in Articles 3 and 4[66]. Both provisions base their operation in the concept of market disruption outlined in MFA Annex A. Article 3 primarily provides for unilateral restrictions when there is *actual* market disruption; whereas, Article 4 allows the negotiation of bilateral agreements when there are *real risks* of market disruption.

The factors causing market disruption are generally a sharp and substantial increase or imminent increase of imports of the specific product, and a price differential between the products offered in the domestic market and those offered by the supplier. In order to establish market disruption the importing country must believe that the imports are causing, or threatening to cause, serious damage to the domestic industry[67].

Article 4 agreements are the most commonly used safeguard mechanisms in

[65] See Chapter III, Section I, below, for a discussion of this issue.

[66] *MFA*, arts. 3-4.

[67] *MFA*, Annex A.

international textile trade[68]. The utilization of these bilateral agreements is due to the following reasons: a) Imports covered by Article 4 may not be subsequently limited by actions under Article 3[69]; b) Exporting countries, facing the threat of unilateral actions, have preferred to negotiate bilateral agreements[70]. These agreements are apparently more stable and predictable that actions under Article 3; and c) Bilateral agreements guarantee access to the markets of importing countries. Thus, small suppliers and new entrants do not take the risks of being wiped out by more efficient exporters[71].

In practice, however, there is no major difference between actions taken under Article 3 and Article 4 of the MFA. The inclusion of "consultation" and "price" clauses in bilateral agreements, as well as the use of the "antisurge mechanism", have led to the subsequent imposition of unilateral restrictions.

"Consultation clauses" are more loosely constructed than MFA Article 3. They allow for the imposition of unilateral restrictions without requiring the existence of actual market disruption. The risk of disruption alone allows the importing country to seek consultations with the supplier, and, eventually, to restrain its imports to a level already provided in the agreement[72].

"Price clauses" also justify seeking consultations with the supplier when there are imports arriving at "abnormally low prices"[73]. Eventually, price clauses will permit the unilateral restriction of imports already covered by bilateral agreements.

---

[68] Henry R. Zheng, "The Legal Structure of the International Textiles Trade and the July 1986 MFA Renewal Negotiations" (1986) 4 B. U. Int'l L. J., 285 at 303 quoted by David M. Lazarus "Treading Water in the Caribbean: Recent Developments in United States Textile and Apparel Policy" (1992) 13:1 University of Pennsylvania Journal of International Business Law 141 at 162.

[69] *MFA*, art. 3 para. 3.

[70] Zheng, *supra* note 42 at 33.

[71] *Ibid*. at 34.

[72] "Consultation provisions enable importing countries to adopt unilateral restrictions similar to that under Article 3 with less stringent substantive as well as procedural requirements". *Ibid.* at 36.

[73] *Ibid*. at 35.

Further restrictions on textile trade are provided by MFA's "antisurge" mechanism[74]. The antisurge action may only be directed to imports that underwent a sharp and substantial increase as a result of significant differences between large restraint levels negotiated in accordance with MFA Annex B, and actual imports[75]. This implies that even an allocated quota would not guarantee that the corresponding market share would remain secured[76]. Briefly, the antisurge action permits further restriction of imports already subject to quantitative restrictions[77].

The antisurge mechanism as well as the consultation and price clauses modify the safeguard framework originally established in MFA Articles 3 and 4. The superior bargaining power of importing nations enabled them to introduce these amendments, which further regulated the international textile and apparel trade to the detriment of exporting nations[78].

B. Limitation on Restraint Actions

1. Base Level, Growth Rate and Flexibility

The MFA emerged as a compromise between developed and developing countries. While developed countries secured the right of limiting textile imports, the

---

[74] *MFA IV*, para. 11.

[75] "The EEC regards the 'large restraint level' as any quota that accounts for more than one percent of the extra EEC trade, while a 'sharp and substantial increase' refers to a 10 percent increase in EEC imports over the preceding year; and in some cases it refers to a 2.5 percent increase". Zheng, *supra* note 42 at 37.

[76] Diana Tussie, *The Less Developed Countries and the World Trading System: A Challenge to the GATT* (New York: St. Martin's Press, 1987) at 67.

[77] MFA Article 3 actions may be taken only against imports not already subject to quantitative restrictions. On the other hand, existing quotas negotiated under Article 4 may not normally be tighten. *MFA*, arts. 3(3)-4.

[78] Lazarus, *supra* note 68 at 163.

latter obtained the promise of an orderly and equitable growth of the market[79].

The MFA, in order to protect exporting nations from excessive restrictions on their exports, placed some limits in restraint measures to be taken by importing countries, viz., the base level, growth rate and flexibility provisions.

Base level refers to a minimum level of imports that must be respected when applying safeguard measures. MFA Annex B provides that the base level may not be lower than the actual volume of imports during the previous twelve months[80].

Growth rate refers to the minimum annual increase over the base level when quantitative restrictions are in effect for more than a one year period[81]. MFA provides an annual growth rate of 6 per cent[82]. However, where there are clear grounds for holding that the situation of market disruption will recur if the 6 per cent growth rate is implemented, a lower positive growth rate may be decided upon after consultation with the exporting country concerned[83]. This exception clause has been frequently invoked by importing countries giving rise to the continuous establishment of growth rates lower than 6 per cent[84].

Finally, the flexibility provision refers to the adjustment system of quotas within the total restraint limit. "When more than one product category is restricted, an exporting country may exceed, within the overall restraint level, quotas of some products if other quotas will be proportionately underused"[85]. The agreed level of restrictions may be exceeded by 7 per cent. However, a lower percentage, not less than 5 per cent, may be justified by an importing nation facing "exceptionally and

---

79 *MFA*, art. 1, para. 2.

80 *MFA*, Annex B, 1(a).

81 Zheng, *supra* note 42 at 40.

82 *MFA*, Annex B, 2.

83 *Ibid.*

84 Zheng, *supra* note 42 at 41.

85 *Ibid.*

sparingly used circumstances"[86].

Nevertheless, the 5 per cent minimum has not been maintained. Lower percentages of flexibility were usually negotiated under MFA II through the "reasonable departure" clause[87]. This practice was subsequently legitimized in MFA III[88]. At present, it is possible to reach agreement with regard to flexibility when there is a growing impact of a heavily used quota accounting for a very large share of the importing market[89].

2. Treatment of Small Suppliers, New Entrants, Least Developed Countries and Offshore Assembly Countries

The MFA has accorded a special treatment to small suppliers, new entrants and least developed countries. This preferential treatment recognizes the existence of particular needs in developing countries that must be taken into account when restricting their exports.

MFA Article 6 provides that small suppliers should not normally be subject to quantitative restrictions[90]. Besides, it stipulates that limitations on new entrants should not consider their past performance[91]. Clearly, this provision grants preferential treatment to new entrants when establishing their base levels.

MFA IV strengthed MFA Article 6. It provided that not only small suppliers but also new entrants and least developed countries should be free from

---

86 *MFA*, Annex B, 5.

87 Zheng, *supra* note 42 at 41.

88 *MFA III*, para. 9.

89 *MFA IV*, para. 9.

90 *MFA*, art. 6 para. 3.

91 *MFA*, art. 6, para. 2.

restraints[92]. MFA IV further stipulates that when quantitative restrictions are applied on exports from small suppliers and new entrants, the growth and flexibility rates should be fixed having due regard of their social and economic development[93]. If restrictions are imposed on least developed countries, the treatment accorded to these nations should be significantly more favourable than that accorded to small suppliers, new entrants and cotton producing nations[94]. Although the least developed country group is specially singled out, MFA IV does not define it. A clarification of this provision would allow a more accurate interpretation of the rule.

Also covered by the MFA is the situation of offshore assembly. Textiles imports introduced in a country under a system of temporary importation for re-export after processing, shall not, as far as possible, be subject to quantitative restrictions[95]. On the other hand, consideration shall be given to special and differential treatment to re-imports which a nation has exported to another country for processing and subsequent re-importation, without prejudice of MFA Article 3[96].

MFA offshore assembly regulation seems to favour the stronger party of the relation: the reimporter. "Whereas the importing processor shall try to limit quota restrictions, the exporter need only give consideration to the re-imported processed goods"[97].

---

92 *MFA IV*, para. 13(a).

93 *MFA IV*, para. 13(c).

94 *MFA IV*, para. 13(b).

95 *MFA*, art. 6, para. 5.

96 *MFA*, art. 6, para. 6.

97 Lazarus, *supra* note 68 at 163.

SECTION III: MFA Effects on Textile and Apparel Trade

The legal structure of international textiles and apparel trade has been extensively criticized. The MFA has been accused of affecting not only the orderly development of trade in textiles but also the general conception of world trade.

The MFA restrictive trade regime may affect the credibility of the GATT and of the aim of a liberalized world trading system. The politics of trade discrimination, that guide the application of the MFA, represent an assertion of economic and political power of importing countries over exporting countries[98]. Indeed, there has been a tendency according to which MFA restrictions have been applied almost exclusively to developing countries. In 1989, from 114 restraint agreements concluded, 94 were with developing countries[99]. This trend has been seen as the result of a "gentleman's agreement" under which, as far as possible, industrialized countries would not restraint each other textile exports[100].

The MFA has also been blamed for creating a "psychosis of protection"[101] that may encourage higher levels of protectionism. Although not many economic sectors have sought arrangements similar to the MFA, voluntary export restrictions have been expanded to other industries like autos, shoes, and steel[102].

Besides the general consequences for world trade, the MFA effects over textile trade have been the following 1) proliferation of quotas and supplier countries; 2) cheating and trade diversion; and 3) high costs to consumers.

---

98 Jones, *supra* note 6 at 138.

99 *GATT Doc. COM.TEX/62* at 468.

100 Curtis & Vastine, *supra* note 27 at 172. See also William R. Cline "Textile and Apparel" in Jeffrey J. Schott, ed., *Completing the Uruguay Round: A Results-Oriented Approach to the GATT Trade Negotiations* (Washington: Institute for International Economics, 1990) at 65; Das, *supra* note 1, 101 at 77.

101 Das, *ibid.* at 78.

102 *Ibid.*

A. Proliferation of Quotas and Supplier Countries

Since the 1960s the textile and apparel trade has evidenced a steady increase in the number of restrained products. There has been an equally marked proliferation of supplying countries. The legal framework of textiles and apparel trade has been pointed out as the cause of this phenomenon. Indeed, when a certain export textile product is limited by quantitative restrictions there is an incentive to shift the production to another textile category. The production of this last category will eventually increase in such a way that generates the opposition of the domestic industries in the importing markets. Therefore, a new bilateral agreement will be required in order to stop the increase in the new line of exports. This process demonstrates one of the problems of quantitative restrictions: "innovation renders them ineffective"[103].

The Far East Asian Producers resorted to the development of new strategies in order to face the restrictions in the 1960s. They looked for short and long term solutions. In the short run, cotton exporters modernized their production in order to reach the higher possible prices for their restricted cotton exports. Additionally, they tried to secure any scarcity gains that might be generated by quantitative restrictions[104]. The short run solution was successful since exporters counted on a well-organized industry able to update production and bargain adequately with importers. On the other hand, in order to find a long term solution, some cotton exporters expanded production to cover synthetic textiles. In fact, the countries that diversified in response to the LTA ameliorated their gains much more than those that kept operating within the restraints. "United States imports of unrestricted synthetic fibres increased 1700 per cent in value and 1800 per cent in quantity during the 1960s, while cotton imports only doubled"[105]. The response to this growth in

---

103 Curtis & Vastine, *supra* note 27 at 170.

104 Yoffie, *supra* note 28 at 117.

105 *Ibid.*

synthetic textiles imports was a new more restrictive legal regime in textiles and apparel trade: the MFA.

This constant tightening of textile exports led to an increase in the number of supplying countries and gave the opportunity for non-restrained exporters to enter the market[106]. However, emerging suppliers are also threatened with future restrictions. New suppliers which are successful soon find themselves in the same position as major suppliers: "the more successful they are, the faster and tighter they are embraced by the MFA"[107]. Although discrimination under the MFA has guaranteed market access to new suppliers, it has also allowed the emergence of less efficient suppliers[108]. While many developing countries oppose the existence of the MFA, others, such as Mexico, have requested only an MFA amendment. Indeed, without this legalized discriminatory system, Mexico and other developing countries may not be able to compete with major suppliers[109].

---

106 Jones, *supra* note 6 at 137. See also H. W. Singer, N. Hatti & Rameshwr Tandon, eds., *Trade Liberalization in the 1990s*, vol. 8 (New Delhi: Indus Publishing Company, 1990) at 738. Japanese and Honk Kong voluntary restraints in cotton textiles exports to the United States gave opportunity to other countries --India, Pakistan, Singapur and Malaysia-- to develop their capacity to produce cotton textiles. Curtis & Vastine, *supra* note 27 at 171.

107 Singer, Hatti & Tandon, *ibid.*

108 It has been affirmed that the LTA promoted textile exports from inefficient sources. For instance, "the United States [stopped] efficient cotton textile producers and [caused] an increasing number of textile producers to invest their scarce resources in questionable economic uses. Mexico and Brazil are examples of countries whose textiles [became] more attractive primarily because of high U.S. demand and U.S. inability, because of the LTA, to buy textiles from the cheaper sources". Curtis & Vastine, *supra* note 27 at 171.

109 Orme, "Developed Countries Urge Multi-Fibre Reform" Journal of Commerce (15 April 1985) quoted by Bannon, *supra* note 12 at 712. "Negotiations on a new Multi-Fiber Arrangement seem certain to split Asian manufacturers into two camps: the few whales and too many minnows. The smaller fry are desperate for a new MFA - even if it proves more restrictive - because it will guarantee them at least some market share". "Asian Countries Split on Strategy", Journal of Commerce (18 July 1986) quoted by Zheng, *supra* note 42 at 176.

B. Cheating and Trade Diversion

Restrained exporters have developed mechanisms to avoid quota limits. Bilateral agreements under MFA are by definition discriminatory, thus, cheating and circumventing are usually utilized[110]. Among these procedures, transhipment has been the most employed in order to escape quantitative restrictions. In fact, although most exporting countries have been covered by the MFA, "entrepreneurial cheaters" always locate a non-restricted country to repackage or relabel their products[111].

During the 1970s and 1980s Honk Kong, Taiwan and Korea successfully confronted the protectionist tendencies in the United States by cheating, by manipulating transgovenmental ties, and by negotiating for loopholes. Nevertheless, this continuous U.S. tendency of restricting textile and apparel exports may finally induce "The Three" to de-emphasize their textiles and apparel exports[112].

MFA quantitative restrictions may also be the cause of trade diversion. Restricted countries often seek to re-direct their exports to markets that remain open to trade leading to surges in imports in those unprotected markets[113]. Therefore, the protectionist cycle is repeated when those third countries, affected by the spontaneous flood of goods, impose trade restrictions in order to avoid disruptive effects in their markets.

---

110 "...restrained exporters will often seek to avoid the quota restrictions by transhipping the goods or by setting up production and exporting facilities in countries not covered by the agreement." Jones, *supra* note 6 at 136.

111 "[L]ike Sri Lanka or Indonesia in the 1970s". Yoffie, *supra* note 28 at 165.

112 *Ibid.* at 158-159, 167.

113 Jones, *supra* note 6 at 137.

C. High Costs to Consumers

Trade protectionism has shown to be costly for consumers of importing countries[114]. Because the MFA is an instrument utilized by national governments to protect their domestic textile and apparel sectors it has affected consumer costs directly[115].

It has been estimated that a U.S. family pays US$238 annually to preserve some 235 000 jobs in the textiles and apparel industries. Thus, the total consumer cost per job saved is nearly US $82 000 in apparel and US$135 000 in textiles per year[116]. Another study shows that quota limits in Canada cost C$370 000 for every job saved permanently[117].

Protection costs seem to have been increasing over time in parallel with the tightening of MFA restrictions[118], and, apparently, the MFA will continue to be expensive for consumers from importing countries.

---

114 "According to one economist, an American family of four pays between $1.500 and $2.000 each year for trade protection. These high costs explain, in part, why policy makers seemingly have attempted to exclude consumers from understanding just how trade restrictions works". Evans, "An Abuse of Patriotism" U.S. News and World Rep. (3 February 1986) quoted by Bannon, *supra* note 12 at 703.

115 "Volume restraints in developing countries exports of textile products, inter alia, raise domestic prices in importing markets (Cline (1987), Hamilton (1984), Hufbauer et al (1988), Jenkins (1980), Spinanger and Ziets (1986) and Tarr and Morkre (1984); yield quota rents to established suppliers (Hamilton (1988), Pelzman (1988) and Tarr and Morkre (1984); and induce "upgrading" of the product exported (Cline (1987) and Wolf 1987)". Singer, Hatti & Tandon, *supra* note 106 at 739.

116 Cline quoted by Jackson, *supra* note 2 at 182-183.

117 "The MFA is Too Costly a Joke" The Economist (22 December 1984) at 73 quoted by Zheng, *supra* note 42 at 125.

118 *Ibid.*

CHAPTER II: U. S. TRADE POLICIES TOWARDS THE CARIBBEAN REGION

Caribbean exports may enter the U.S. market subject to different U.S. trade programs. The most favoured-nation treatment[119], the Generalized System of Preferences[120], the Caribbean Basin Economic Recovery Act (*CBERA*)[121] and Subheading 9802.00.80 of the Harmonized Tariff Schedule of the United States (HTS) are provisions under which certain Caribbean exports may receive preferential treatment in the U.S. However, it is not always possible to clearly delimit each program: a Caribbean product may qualify for special treatment under more than one of these legal schemes. When there is an overlap between two or more programs, the U.S. importer will choose the most beneficial in economic terms.

This chapter does not propose to cover all the U.S. programs mentioned above. Our study will be focus on the Caribbean Basin Economic Recovery Act and HTS Subheading 9802.00.80, since they allow us to identify the U.S. trade policies regarding Caribbean textile and apparel trade. When analysing the CBERA particular attention will be paid to the duty-free access of Caribbean exports to U.S. markets. Other U.S. policies to encourage investment in the Caribbean region[122],

---

119 Most-favoured nation treatment "...is an obligation to treat activities of a particular foreign country or its citizens at least as favourably as it treats the activities of any other country. For example, if nation A has granted MFN treatment to B, and then grants a low tariff to C on imports from C to A, nation A is obligated to accord the same low-tariff treatment also to B and its citizens". Jackson, *supra* note 2 at 136.

120 "The concept of using a system of tariff preferences for imports from developing countries originated in 1964 at the first session of the United Nations Conference on Trade and Development (UNCTAD). The purpose of this system was to promote the development and diversification of the economics of beneficiary countries by applying lower duty rates, especially for manufactured and semi-manufactured goods." Eberhard Grabitz & Armin von Bogdandy, eds., *U.S. Trade Barriers: A Legal Analysis* (New York: Oceana Publications Inc., 1991) at 123.

121 19 U.S.C. s. 2701 (Supp 1992).

122 A well-known U.S. project to foster foreign investment and further development in the Caribbean region is Section 936 of the U.S. Internal Revenue Code. This section provides a tax exemption for U.S. firms operating in qualified Caribbean countries. Until now, Puerto Rico has been the nation most benefitted by the program. Indeed, "[b]esides providing direct employment for over 100,000 people, section 936 had led to the creation of a $14 billion pool of funds (936 funds) available

although potentially important, are outside the scope of this thesis.

SECTION I: The Caribbean Basin Initiative

The Caribbean Basin Initiative is directed towards Central America, the Islands of the Caribbean Sea, as well as some Latin American countries[123].

In the 1970s the rising price of imported oil adversely affected many of the Caribbean nations because of the fragile nature of their economies. At the same time, there was a decline in the demand and price of Caribbean exports, such as coffee, sugar and bauxite[124]. This economic situation, coupled with often inadequate monetary, fiscal and exchange rate policies at the domestic level[125], resulted in political unrest, high unemployment and trade imbalances in the region[126]. Thus, in order to correct the severe economic difficulties faced by the Caribbean Basin, President Reagan proposed a program called the "Caribbean Basin

---

for investments in Puerto Rico at fairly low interest rates." Ron H. Flax Davidson, "Tax-Exempt Investment for the Caribbean Basin Initiative Region" (1991) 25 International Lawyer 1021. Section 936 funds, however, had not promoted foreign investment in textiles and apparel. From 1987 to 1990, a total of US$358 million in 936 funds has been distributed for 15 significant projects in qualified Caribbean countries. None of those projects was related to the textile and apparel industry. U.S. International Trade Commission, *Annual Report on the Impact of the Caribbean Basin Economic Recovery Act on U.S. Industries and Consumers*, Sixth Report (Washington, 1991) at 4-4 [hereinafter *Sixth Report*].

123 "The Caribbean Basin, as defined by in the *Caribbean Basin Economic Recovery Act*, includes the chain of Caribbean islands from the Bahamas south to Trinidad and Tobago, plus Guyana and Suriname in South America and the seven Central American countries". U.S. Department of Commerce, International Trade Administration, *Caribbean Basin Initiative: 1989 Guidebook*, at 40 [hereinafter *CBI Guidebook 1989*].

124 Analisa G. Lunger, "The Caribbean Basin Initiative and the I.R.C. Section 936 Investment Program: A United States Answer to the Troubled Caribbean Region" (1987) 9 University of Pennsylvania Journal of International Business Law 741 at 749.

125 W. Charles Sawyer and Richard L. Sprinkle, "Caribbean Basin Economic Recovery Act" (1984) 18:5 Journal of World Trade Law 429.

126 Bruce Zagaris, "A Caribbean Perspective of the Caribbean Basin Initiative" (1984) 18 International Lawyer 563.

Initiative" (CBI)[127].

A. The Caribbean Basin Economic Recovery Act (CBERA)

The CBI was intended to bring a solution to the political and social instability in the Caribbean region through the implementation of more open and competitive markets in the area. The underlying objective of the project was to achieve the economic revitalization of the region through the adoption of more liberal economic policies[128].

The CBI was initially introduced to Congress on March 18, 1982[129]. At the core of the program was the implementation of market-oriented policies in the region through a duty-free treatment for Caribbean Basin products exported to the United States[130]. Apart from this exemption from duties, the original project contained three other major provisions: 1) the application of the U.S. investment tax credit to all new investment in the region; 2) increased foreign aid; and 3) technical assistance and private sector training[131].

However, the package was adopted in an amended form. It was exclusively centred on the duty-free treatment concession for Caribbean export products. The investment tax credit provisions, together with the provisions on private sector training, technical assistance and increase foreign aid were eliminated. In order to promote foreign investment and tourism, a provision to allow for the tax deductibility

---

[127] Address of President Reagan Before the Permanent Council of the Organization of American States, (24 February 1982) 18 Weekly Compilation of Presidential Documents 217 [hereinafter *Address of President Reagan*].

[128] John Pendleld, "The Caribbean Basin Initiative: A Welcome Remedy to the Ironic Turmoil" (1982) 12 California Western International Law Journal 466 at 475.

[129] Sawyer and Sprinkle, *supra* note 125 at 430.

[130] *Address of President Reagan*, *supra* note 127 at 220.

[131] Thomas L. Raleigh III, "The US Caribbean Basin Initiative" (1987) 15 International Business Lawyer 136.

of expenses incurred for conventions in the region was added[132]. The CBI, in its modificated form, went into effect on September 30, 1983 and was entitled the *Caribbean Basin Economic Recovery Act* (*CBERA*)[133].

The *CBERA* did not grant duty-free treatment to all Caribbean products. Textiles and apparel, footwear, handbags, luggage, flat goods, work gloves and leather goods, tuna, petroleum, or petroleum-derived products, watches and watch parts, were excluded from the *CBERA* product coverage[134]. Special restrictions were also introduced in relation to sugar and beef products[135].

In short, the *CBERA* was directed towards solving the economic and political crises in the Caribbean through the opening of the U.S. market for Caribbean exports. However, the concession of duty-free treatment for CBI eligible products came far short of what was actually needed to improve the situation of the targeted countries.

B. Operative Means and Regulation

1. Beneficiary Countries

In order to receive the benefits of the *CBERA*, a nation must be designated as a "beneficiary country". Only those countries specifically enumerated in the

---

132 19 U.S.C. s. 2701 (Supp 1992).

133 *Ibid.*

134 19 U.S.C. S.2703(b) (Supp 1992). The Caribbean region has been negatively affected by the CBERA limitation in the product coverage since most countries have a significant market in the production of the excluded goods. Bureau of Public Affairs, United States Department of State Background Note, El Salvador, November 1987; Bureau of Public Affairs, United States Department of State Background Note, Jamaica, January 1987; Bureau of Public Affairs, United State Department of State Background Note, Costa Rica, May 1986; World Almanac and Book of Facts 1987 (M. Hoffman ed. 1987) cited in Gema M. Pinon & Raul Javier Sanchez, "CBI II: Will United States Protectionist Tendencies Yield to Economic Development in the Caribbean Basin?" (1989) 20:3 University of Miami Inter-American Law Review 615 at 620.

135 19 U.S.C. s. 2703(c) and (d) (Supp 1992).

legislation are eligible for duty-free treatment[136]. To be eligible under the CBI, the country must have a number of specific characteristics: a non-communist government; no expropriation of any property belonging to either the Government of the United States or to any U.S. nationals; cooperation with the United States Drug Enforcement Agency; adequate protection of patents, copyright and trademark rights; recognition of the collective bargaining rights of workers; and the establishment of self-help measures[137]. In addition, there are some specific considerations that may be taken into account when designating a nation as a beneficiary country, such as the economic conditions of the country; the strength of the country's assurances to the U.S. that it will provide equitable and reasonable access to its markets and basic commodity resources; the country's commitment to the principles of the GATT; the degree to which the country uses export subsidies or imposes export performance and local content requirements which distort international trade; the degree to which the trade policies of the country, as they relate to other countries, contribute to the revitalization of the Caribbean region; and the willingness of the country to undertake self-help measures which promote economic development[138].

The *CBERA* gives the President of the United States the power to designate a nation as a beneficiary country[139]. Likewise, the President is empowered to

---

[136] The Caribbean nations that may be classified as "eligible countries" under the CBI are Anguilla, Antigua and Barbuda, the Bahamas, Barbados, Belize, Cayman Islands, Costa Rica, Dominica, Dominican Republic, El Salvador, Grenada, Guatemala, Guyana, Haiti, Honduras, Jamaica, Montserrat, Netherland Antilles, Nicaragua, Panama, St. Lucia, St. Christopher-Nevis, Suriname, Trinidad and Tobago, Turks and Caicos Islands, and the British Virgin Islands. 19 U.S.C. s. 2702(b) (Supp 1992).

[137] 19 U.S.C. s. 2702(b) (Supp 1992).

[138] 19 U.S.C. s. 2702(c) (Supp 1992).

[139] 19 U.S.C. s. 2701 (Supp 1992). As of December, 1991, only Anguilla, the Cayman Islands Suriname and Turks and Caicos had not formally requested *CBERA* designation. U. S. International Trade Commission, *Report on the Impact of the Caribbean Basin Economic Recovery Act on U.S. Industries and Consumers*, Seventh Report 1991 (Washington, 1992) at 1-3 [hereinafter *Seventh Report*]. The President was authorized to grant Nicaragua beneficiary status under the CBI and the

revoke any designation on the sole condition of adequate notification to Congress and to the respective country within sixty days before the termination[140].

2. Rules of Origin

The "one-way" free trade arrangement is applicable to those products of the eligible countries that meet the rules of origin[141] stipulated in the *CBERA*. Duty-free entry is granted to those articles that are grown, produced, or manufactured in a beneficiary country if they are imported *directly* into U.S. customs territory[142]. The *CBERA* establishes a requirement of thirty-five percent of local content, *i.e.* the total of the direct cost of processing operations plus the value of materials produced in one or more beneficiary countries must count for at least thirty-five percent of the appraised value of the article. The direct costs of processing operations performed in Puerto Rico or the U.S. Virgin Islands, and the cost or value of materials produced therein, may be included in the thirty-five percent figure[143]. Moreover, materials of U.S. origin may be counted for up to fifteen percent of the thirty-five percent of

---

Generalized System of Preferences (GSP) although it did not meet the designation criteria specified by the CBI and GSP. *Caribbean Basin Economic Recovery Act*, Pub. L. 98-67, s. 141 (1983) (codified as amended at 42 U.S.C. ss. 2701-2706 (1993), and in scattered sections of 19, 26 and 33 U.S.C.) [hereinafter *Caribbean Act*].

140 19 U.S.C. s. 2702(a)(2) (Supp 1992).

141 "The rules of origin are of paramount importance in the effective administration of any free trade agreement. They ensure that only goods with sufficient beneficiary country content will receive duty-free treatment, and they prevent the transshipping of non-beneficiary goods through beneficiary countries in an effort to take advantage of the preferences afforded under such agreements". David Serko, *Import Practice: Customs and International Trade Law* (New York: Practising Law Institute, 1991) at 315.

142 19 U.S.C. s. 2703(a)(1)(A) (Supp 1992).

143 19 U.S.C. s. 2703(a)(1)(B) (Supp 1992).

the product appraised value[144].

The *CBERA* disqualifies "pass-through" operations[145] by requiring that the product be wholly grown or manufactured in a beneficiary country or undergo a substantial transformation[146] which results in a new or different article[147].

3. Ordinary and Necessary Business Expense Allowance

The original intentions in the CBI involved the promotion of U.S. investment in the Caribbean Basin region. However, only a provision to allow for the tax deductibility of expenses incurred for conventions in the region was finally included in the *CBERA*[148]. A U.S. tax resident may deduct the reasonable business expenses of attending conventions held in a Caribbean Basin country if the following requirements are fulfilled: 1) the nation has been designated as a beneficiary country; 2) there is an exchange information agreement with the U.S.; and 3) there is no discrimination in the country's tax laws against conventions and similar meetings

---

144 *Ibid.* The CBI rules of origin differ from those established under the GSP in some significant aspects: 1) whereas the GSP establishes as a general rule that the article must be solely produced in the beneficiary country, the CBI permits the cost of materials and the direct costs of processing to be cumulative among all CBI beneficiary countries; and 2) under the GSP, U.S. materials do not account for a percentage of the appraised value of the finished article, while under the CBI up to 15 percent of the value-added may include the cost of U.S. content. Likewise, direct costs of processing in Puerto Rico and the U.S. Virgin Islands, as well as the cost of materials of those countries may not be applied toward meeting the 35 percent value-added figure under the GSP. 19 U.S.C. ss. 2461 (1993).

145 "[Pass-through operations are those] in which goods from foreign countries receive minimal processing or packaging before re-export." *CBI Guidebook 1989, supra* note 123 at 8.

146 "If the article contains or is made from materials originating from a non-CBI country, the final product must be an article of commerce 'new and different' from the foreign materials used in its manufacture". *Ibid.*

147 19 U.S.C. s. 2703 (a)(2) (Supp 1992).

148 Zagaris, *supra* note 126 at 580.

held in the U.S.[149].

The reasonable expenses that may be deducted are 1) the travelling expenses, when they are reasonable and necessary in the conduct of the business and are directly attributable to it, and 2) the admission fees at the convention, when it is sufficiently related to the taxpayer's business[150].

From an international tax perspective, the exchange of information requirement is the only significant provision of the *CBERA*. The tax information agreements refer to the data necessary to implement the tax law of the U.S. and the beneficiary country[151], including information that may otherwise be subject to nondisclosure provisions of the local law, such as provisions respecting bank secrecy and bearer shares[152]. In this respect, the information agreements are intended to go further than exchange information provisions of some U.S. tax treaties, "which may not impose an obligation to supply information not obtainable under local law or administrative practice"[153]. As of 1991, Barbados, Costa Rica, Dominica, the Dominican Republic, Grenada, Honduras, Jamaica, St. Lucia, Trinidad and Tobago, and U.S. Virgin Islands have signed Tax Information Exchange Agreements with the

---

149 *Caribbean Act*, s. 222, *supra* note 139.

150 IRC s. 274(h) (1954)

151 "The purpose of the [Tax Information Exchange Agreements] is to allow the United States and CBI Governments to share tax and other information that could lead to the arrest and conviction of drug traffickers, tax evaders, and other criminals. The rationale of the [Tax Information Exchange Agreements] is that it leaves such criminals without some of the protection otherwise afforded by foreign residency and relieves the confusion and jurisdictional problems encountered by law enforcement agencies when portions of an illegal enterprise occur in various countries". Davidson, *supra* note 122 at 1025. The geographic proximity of the Caribbean Basin countries and their development as tax havens has contributed to income tax evasion in the United States. Peter Beard, "Offshore Financial Centers in Caribbean Basin Secrecy Jurisdictions: Current Trends and Developments in United States Anti-Tax Haven Policy" (1986) 12 Syracuse Journal of International Law and Commerce 520.

152 *Caribbean Act*, s. 222(C)(i), *supra* note 139.

153 Zagaris, *supra* note 126 at 578.

U.S.[154]

C. Effectiveness

The effectiveness of the CBI can only be measured through an analysis of the beneficiary Caribbean countries' economic conditions "before and after" the promulgation of the *CBERA*[155]. Studies in this regard have demonstrated the failure or general ineffectiveness of the CBI[156]. For example, there has not been a foster of trade between the Caribbean and the U.S. On the contrary, the prevailing trend has been a reduction of U.S. imports from the CBI beneficiary countries[157]. The Caribbean Basin share of the U.S. market has fallen sharply. Whereas in 1984 Caribbean suppliers accounted for 2.8 per cent of total U.S. imports, their share of the U.S. market in 1991 was just 1.7 per cent[158].

The general decrease of Caribbean imports in the U.S. market during the period 1984-89 was mainly due to the drop of U.S. imports of petroleum and

---

154 *Seventh Report, supra* note 139 at 1-11.

155 John Cyril Malloy III, "The Caribbean Basin Initiative: A Proposal to Attract Corporate Investment and Technological Infusion Via an Inter-American System of Cooperative Protection for Intellectual Property" (1991) 23:1 University of Miami Inter-American Law Review 175 at 183.

156 See especially Edward John Ray, *U.S. Protectionism and the World Debt Crisis* (New York: Quorum Books, 1989). A clear reduction in trade between the Caribbean Basin and the United States was the tendency during the 1980s. "Mexico, Central American Countries Plan Free Trade Agreement to Be Reached by 1996" (1991) 8:3 International Trade Report 87.

157 "Significant increases in trade have been diluted by the adverse effects of declining commodity prices (especially petroleum), reduced U.S. sugar quotas, and declining tourism revenues in Central America. [However, in] a recently completed Department of Commerce study, it was determined that since the inception of the CBI program, 646 new foreign exchange generating investments have been undertaken, totalling an estimated $1.5 billion, and creating more that 116,000 new jobs". *CBI Guidebook 1989, supra* note 123 at 3-4.

158 *Seventh Report, supra* note 139 at 2-2. See Appendix A.

petroleum-related products from the Caribbean[159]. U.S. petroleum imports from *CBREA* nations decreased from US$4.7 billion in 1984 to US$1.0 billion in 1989. Note, however that since 1989, U.S. petroleum imports from the Caribbean region have partially recovered, reaching US$1.4 billions in 1991[160].

A number of reasons have been given for the disappointing outcome of the CBI: the inability to offer security to foreign investors[161], U.S. protectionism[162], the inadequacy fo the CBI's administration[163], and the lack of an authentic interests to assist the region in a meaningful way[164].

The study of the underlying reasons for the failure of the CBI are outside the scope of this thesis. However, there are two facts[165] that must be singled out since they unquestionably contributed to the CBI's outcome. First, even before the adoption of the *CBERA* over 93% of Caribbean exports entered the U.S. under duty-free treatment[166]. Therefore, since most of the CBI goods were already covered by other programs that permitted their entry into U.S. markets under free trade, the

---

159 The decrease in the annual value of U.S. imports from the Caribbean countries during the 1984-89 period accounted for "a significant portion of the decline in overall U.S. imports from the oil-exporting CBERA countries -Aruba, the Bahamas, the Netherlands Antilles, and Trinidad and Tobago-". *Ibid.* at 2-7.

160 *Ibid.* at 2-2.

161 Malloy, *supra* note 155 at 184.

162 Francis W. Foote, "The Caribbean Basin Initiative: Development, Implementation and Application of the Rules of Origin and Related Aspects of Duty-Free Treatment" (1985) 19 George Washington Journal of International Law and Economics 245 at 261-263.

163 Pinon and Sanchez, *supra* note 134 at 638.

164 *Ibid.* at 627-628.

165 Raleigh, *supra* note 131 at 137.

166 "The most-favoured nation provision, the Tropical Fruits and Vegetables Agreement negotiated in the General Agreement on Tariffs and Trade (GATT) and the Generalized System of Preferences (GSP) authorised by the Trade Act of 1974 (as extended by the Trade and Tariff Act of 1984) permitted such treatment." "The Caribbean Basin Policy", Hearings before the Subcommittee on InterAmerican Affairs of the House Committee on Foreign Affairs, 97th Cong. 1st Sess (1981) quoted by *ibid.*

CBI's focus on the opening of markets was futile[167].

On the other hand, the products specifically exempted from the *CBREA*'s one-way free trade provisions are those that represent the strongest Caribbean Basin industries, such as footwear, handbags, luggage, textiles and petroleum products[168]. Those industries[169] offer the greatest potential for growth in the economies of beneficiary CBI countries[170]:

> "Apparently, special interest groups in the United States were effective in influencing the eligibility criteria of the CBERA with respect to duty-free import access to U.S. markets in the direction of minimizing the exposure of domestic producers to foreign competition. Duty-free access to markets was biased toward areas of export in which the initial barriers were small and in areas in which competitive threats from potential beneficiary countries were minimal"[171].

The International Trade Commission has recognized the CBI's inability to grant new preferential access to *CBREA* products in the U.S. market. "Of the nonexcluded goods imported in 1988, $1.9 billion worth were already unconditionally

---

[167] "The limited impact of an approach based on tariff reductions was recognized as soon as the Act was articulated, for tariffs were not a major hindrance to trade between the Caribbean and the U.S." Mark B. Baker & Jaime E. Toro-Monserrate, "CBI v. Caricom: The Interplay between Two International Law Instruments" (1986) 11 North Carolina Journal of International Law and Commercial Regulation 1 at 12; see also Stuart K. Tuker, Desentrabamiento del Comercio: Evaluacion de la Iniciativa de la Cuenca del Caribe, Recuperacion y Desarrollo de Centroamerica, Ensayos del Grupo Especial de Estudios de la Comision Internacional para la Recuperacion y el Desarrollo de Centroamerica (San Jose: Trejos Hermanos Sucs., 1989) 361 at 365.

[168] Ray, *supra* note 156 at 201.

[169] The most promising area excluded from the CBI was trade in textile and apparel goods. Lazarus, *supra* note 68 at 145.

[170] "The reason for these exceptions is the protection of U.S. industries. Congress did not want the stronger Caribbean Basin industries to compete in these product lines with U.S. producers... Congress specifically excluded the industries that may prove most beneficial to the Caribbean development efforts". Abelardo L. Valdez, "Expanding the Concept of Coproduction Beyond the Maquiladora: Toward a More Effective Partnership between the United States and Mexico, and the Caribbean Basin Countries" (1988) 22:2 International Lawyer 393 at 409-500. "[Under the CBI] careful attention to the potential economic effects on domestic US industries has led to the exclusion of all products that are import-sensitive and countries that are too competitive". Grabitz & von Bogdandy, *supra* note 120 at 126.

[171] Ray, *supra* note 156 at 207.

free of duty under MFN tariff rates... The remaining $1.5 billion in imports represented CBERA-eligible products that would have been dutiable without the CBERA"[172]. Likewise, preferential access for Caribbean exports already subject to the Generalized System of Preferences (GSP) has not been improved by the CBERA[173].

Despite the disappointing results in terms of overall export earnings to the U.S., nontraditional exports, led by textiles and apparel, have increased significantly[174].

Apparel, being a non-eligible *CBERA* product, is the current leading category of U.S. imports from the Caribbean region. While imports entering the United States under *CBERA* duty free treatment amounted to US$1.1 billion in 1991[175], textile and apparel imports totalled US$2.5 billion in the same year[176].

A regional economic revitalization, primarily due to the performance of textile and apparel exports[177], is currently taking place in the Caribbean Basin[178].

---

172 U.S. International Trade Commission, *Report on the Impact of the Caribbean Basin Economic recovery Act on U.S. Industries and Consumers*, Fourth Report (Washington, 1989) at 1-12 [hereinafter *Fourth Report*].

173 "Although the CBERA does permit duty free entry for those products that lost GSP eligibility because their competitive-need limits were exceeded, the only item of significance in this category has been sugar imports from the Dominican Republic, which were redesignated as eligible for GSP treatment effective July 1, 1988". *Ibid.*

174 *Sixth Report*, *supra* note 122 at 2-9. See also Ray, *supra* note 156 at 200. See Appendix B.

175 See Appendix C.

176 *Seventh Report*, *supra* note 139 at 2-7.

177 "[The garment segment] has suddenly become the star of the manufacturing sector in several Caribbean nations. The value of regional apparel exports has soared from $90 million in 1985 to $1.073 billion by 1987". Bureau of National Affairs, International Trade Reporter No. 17 "Imports of Caribbean Garments Soar in Wake of CBI, Further Access Sought" (27 April 1988) at 625.

178 This export boom in the Caribbean Basin, however, is dominated by a few countries: The Dominican Republic, Costa Rica, Guatemala, Jamaica and Honduras. "Historically, the only other large CBERA apparel supplier has been Haiti. However, recent political turmoil in the country and a U.S.-supported trade embargo have kept most U.S. firms from considering Haiti as an attractive investment site." U.S. International Trade Commission, *Potential Effects of a North American Free*

However, this economic boom, is not due to the CBI, which, as we have seen above, expressly excludes textile and apparel articles from duty-free treatment[179].

D. Recent Developments: The CBI II

The *CBERA* was enlarged in the *Customs and Trade Act* of 1990. Nevertheless, it did not include the main proposed modifications that would have favored an increased access of Caribbean products to the U.S. market.

The CBI II legislation discarded Congressman Sam Gibbons' proposals for: the concession of duty-free treatment to Caribbean clothing and other articles manufactured from U.S. origin materials, and for the restoration of the Caribbean Basin sugar quotas to the amounts that prevailed before the CBI took effect[180].

Under that legislative project, those products originally excluded from the CBI would be permitted free entry to the U.S. under certain conditions[181]. However, this proposition was strongly opposed by U.S. apparel unions and domestic producers[182]. Likewise, the proposed changes in the quantity of sugar that could enter the U.S were rejected.

As passed, the CBI II extended its operation indefinitely, repealing the original

---

Trade Agreement on Apparel Investment in CBERA Countries (Washington, 1992) at 7 [hereinafter NAFTA Effects on Apparel Investment in CBERA Countries].

179 Pinon and Sanchez, *supra* note 134 at 627.

180 Bureau of National Affairs, International Trade Reporter No. 14 "Legislation to Expand Trade Preferences for CBI Beneficiaries Introduced in the House" (12 August 1987) at 1006.

181 Duty free entry will be allowed if the U.S. International Trade Commission determines that: (A) the articles within that category either (i) are not produced in the United States, or (ii) are not produced in the United States in quantities sufficient to meet the domestic demand for the product; and (B) no directly competitive articles are produced in the United States. H.R. Rep. No. 266, 98th Cong., 1st Sess, s. 4 (amending s. 213A(c)(1) of CBI) quoted by Pinon and Sanchez, *supra* note 134 at 637.

182 Committee on Ways and Means of the U.S. House of Representatives, *Written Comments on H.R. 1233: The CBER Expansion Act of 1989* (Washington, 1989).

1995 termination date[183]. However, it did not provide any major innovation that could had given Caribbean products easier access to the U.S. market[184]. The original purpose of increased trade relations between the Caribbean and the U.S. was hindered due to the narrow scope of the legislation.

SECTION II: U. S. Harmonized Tariff Schedule Subheading 9802.00.80

Item 9802.00.80 of the U.S. Harmonized Tariff Schedule (HTS) fits within the so-called offshore assembly provisions (OAPs). Although the OAPs vary in nature in each industrialized country, they are generally directed to the last stage in the manufacturing process -assembly- to be realized overseas. Usually, the goods are assembled with components from the country granting the OAPs. When the product is re-imported into the industrialized country, the import tariff is only applied on the value-added in the exporting country. Such products thus benefit from a reduction of the effective tariff. These OAPs derive from a principle of trade-neutral taxation according to which domestic products that are re-imported must not be taxed differently from those purchased and used solely within the country's borders[185].

The OAPs, which are built into the tariff schedules of the industrialized countries, have favoured developing countries through the creation of jobs in areas severely affected by unemployment. In fact, OAPs are incentives for multinational corporations to hive off the final processing stages of manufacturing and to relocate them at operating facilities in developing countries. OAPs, however, are not the primary factor encouraging outward processing. The low cost of labour in developing countries, which substantially reduces production costs, has been the basic reason for

[183] 19 U.S.C. ss. 2701-2706 (Supp 1992).

[184] *Ibid.*

[185] U.S. International Trade Commission, *The Use and Economic Impact of TSUS Items 806.30 and 807.00*, Report to the Subcommittee on Trade, Committee on Ways and Means, U.S. House of Representatives (Washington, 1988) at XXV [hereinafter *TSUS 806.30 and 807.00 Report*].

resorting to offshore assembly facilities[186].

Offshore assembly processing has grown rapidly in the last twenty years[187], and has benefited industrialized countries. First, as the OAPs promote the division of labour between developed and developing countries, the former experience an expansion of both exports and imports[188]. Second, the OAP-granting country will have more favourable costs than other, non-granting nations: offshore processing reduces production costs, thus increasing competitiveness. Finally, although offshore processing cause developed countries to lose sections in the manufacturing process, they improve the industry's competitiveness and therefore support the very existence of the industry in the near future[189].

U.S. OAPs are stipulated under HTS subheadings 9802.00.60 and 9802.00.80. Subheading 9802.00.60 provides tariff treatment for certain metals of U.S. origin processed abroad and returned to the United States for finishing. Subheading 9802.00.80 sets forth the tariff treatment for eligible imported goods that contain U.S.

---

186 See *infra* note 200.

187 "Exports of manufactures by developing countries which are covered by OAPs in industrialized countries appear to have grown even faster than totally developing countries exports of manufactures. For example, between 1970 and 1976 total manufactured exports of developing countries rose by 305 per cent, while such exports subject to OAPs in the United States alone rose by 530 per cent". Grimwade, *supra* note 38 at 325. "[In the United States] offshore assembly imports, excluding semiconductors, averaged an annual growth rate of 18.5 percent, or they grew approximately 2.5 times faster than the growth of total imports over the period 1980-1986" Khosrow Fatemi, ed., *The Maquiladora Industry: Economic Solution or Problem?* (New York: Praeguer, 1990) at 91.

188 "Hence their balance of payments need not suffer, while the total level of economic activity is likely to be raised". Grimwade, *ibid.*

189 "...U.S. industries that have a comparative disadvantage over time will be faced with increased import penetration in their domestic market. As a U.S. Tariff Commission study indicates, a major factor in the decision of a firm to conduct offshore operations was the need to respond to increasingly intense competition in the domestic market from foreign producers. Therefore, the more intense the import competition that this U.S. industry faces, the more likely it is that this particular industry will have a comparative disadvantage and therefore will engage in offshore assembly production." Fatemi, *supra* note 187 at 95.

formed components[190]. This section only deals with HTS 9802.00.80 which covers imports of textiles and apparel containing U.S.-made components[191].

Despite the growing importance of offshore assembly production, there has been little theoretical and empirical analysis of this topic.[192] Thus, the approach taken in this chapter does not intend to construct a general doctrine of offshore assembly production but only to address the decision of U.S. apparel companies to set up offshore facilities in the Caribbean Basin.

A. General Overview

Since the reasons which have prompted U.S. apparel companies to engage in processing in the Caribbean countries and Mexico are essentially the same, an initial reference relevant to both geographical regions will be made[193].

Faced with the increasing import penetration of Asian low-cost apparel and

---

[190] Imports under HTS 9802.00.80 alone represented 98 percent of the combined imports under HTS 9802.00.60 and 9802.00.80 in 1989, as well as 96 percent of the duty-free content of both provisions. U.S. International Trade Commission, *Production Sharing: U.S. Imports under Harmonized Tariff Schedule Subheadings 9802.00.60 and 9802.00.80*, 1986-1989 (Washington, 1991) at viii [hereinafter *Production Sharing 1986-1989*].

[191] The entry of an article under subheading 9802.00.80 does not relieve it from quantitative restrictions imposed under other provisions of law. Thus, textiles and apparel imports, which qualify for duty-free treatment on U.S. content, may be subject to quotas under the Multifiber Agreement.

[192] "The effects of OAPs on the trade balances of the United States, and other countries were examined in a series of papers by Finger in the mid-1970s. Since this series of papers, there has been surprisingly little ... work examining the offshore assembly industry, except for papers by Grossmann and Lee. In addition, the relevant literature concerning foreign direct investment, intrafirm trade, and intraindustry trade has touched on the issue but not dealt with it on detail...[P]eriodic descriptive reports have been issued by the U.S. International Trade Commission and the U.S. Department of Labour". Fatemi, *supra* note 187 at 92.

[193] *NAFTA Effects on Apparel Investment in CBERA Countries*, *supra* note 178 at 3; The most popular sites for foreign production for U.S. industries under HTS 9802.00.60 and 9802.00.80 are Mexico, the Caribbean Basin, Canada and East Asia. *TSUS 806.30 and 807.00 Report*, supra note 185 at 5-1.

textiles during 1972 and 1986[194], some U.S. apparel makers sought to improve their competitiveness through production-sharing operations in Mexico and the Caribbean Basin. These companies established manufacturing facilities or concluded subcontracting agreements with local interests to assemble U.S. components for re-export[195]. Offshore assembly, however, is not limited to the apparel industry. In general, over the last quarter century, competition from imported products in the U.S. market has required the development of strategies to improve U.S. competitiveness. Indeed, "[f]oreign competitors have increased their ability to market products in the United States because of factors such as implementation of efficient production techniques, low wages in certain countries, indigenous government support, and proximity to raw materials and components"[196]. Thus, U.S. industries were faced with the need of using offshore facilities. Whereas for some industries, offshore production represented the possibility of using new technology, for others, it allowed the use of low-cost production sites for labour-intensive goods[197].

In recent years, cost savings resulting from offshore assembly operations in Mexico and the Caribbean nations have usually been greater than those of producing in Hong Kong, the leading source of imported apparel[198]. Thus, most U.S. foreign

---

194 "It is estimated that by 1986 the Asian share of total U.S. apparel consumption was nearly 20 percent." *NAFTA Effects on Apparel Investments in CBI Countries, ibid;* see also Leslie Sklair, *Assembling for Development: The Maquila Industry in Mexico and the United States* (Boston: Unwin Hynan Inc., 1989) at 50-51.

195 Sklair, *ibid.* Offshore processing has been implemented either through export platform investment (requires direct investment) or through subcontracting (the assembled services are contracted in the developing country). Grimwade, *supra* note 38 at 234-235.

196 *TSUS 806.30 and 807.00 Report, supra* note 185 at 6-7.

197 Susan Walsh Sanderson, "Automated Manufacturing and Offshore Assembly in Mexico" in Cathryn L. Thorup, ed., *The United States and Mexico: Face to Face with New Technology* (Overseas Development Council, 1987) at 127 quoted in *ibid.* at 6-1.

198 U.S. International Trade Commission, *Production Sharing: U.S. Imports under Harmonized Tariff Schedule Subheadings 9802.00.60 and 9802.00.80*, 1985-1988 (Washington, 1989) at 6-4 [hereinafter *Production Sharing 1985-1988*]. See Appendix D.

assembly operations are currently located in those countries[199].

Performing the labour-intensive assembly operations in Mexico and the Caribbean is profitable for U.S. industries because of the abundant supply of low-cost labour[200]. Proximity to the United States adds to the advantage of outward processing since greater control over production and lower transportation costs are available[201]. Finally, the possibility of employing HTS item 9802.00.80 increases the firm's competitiveness since it allows for a tariff reduction when reimporting the finished products into the United States.

1. Subheading 9802.00.80: U.S. Components Assembled Abroad

Although item 807.00 of the Tariff Schedule of the United States (TSUS) has been replaced by item HTS 9802.00.80, the language and duty rates of the former were carried forward to the latter[202].

The origins of HTS item 9802.00.80 date back to 1954 when the *Customs*

---

199 *Production Sharing 1986-1989, supra* note 190 at 28. See Appendix F.

200 *TSUS 806.00 and 807.00 Report*, supra note 185 at 51. "Labour costs, according to most U.S. industry officials, are the leading source of production cost savings for firms assembling apparel in the CBERA countries and Mexico... Apparel industry wage rates in CBERA countries are reported to range between 58 cents and $1.10 per hour, while the wage rate in Mexico is generally higher." "The importance of labour costs in competitiveness comparisons relates, in large part, to the labour-intensive nature of the apparel-manufacturing process. Differences in technology rarely appear as a significant source of cost advantage or disadvantage for U.S. 807 firms operating in the CBERA countries and Mexico. Indeed, as new developments in sewing technology lead to new commercial applications, most U.S. firms are able to take advantage of them quickly, modernizing assembly facilities when necessary. The absence of differences in technological capacity among 807 firms highlights again the underlying importance of differences in labour costs" *NAFTA effects in Apparel Investment in CBERA countries supra* note 178 at 30.

201 *TSUS 806.30 and 807.00 Report, ibid.* at 5-5. Transportation costs from Mexico and the Caribbean are lower than those resulting from assembling in the Far East. *Production Sharing: U.S. Imports under Harmonized Tariff Schedule Subheadings 9802.00.60 and 9802.00.80, 1988-1991* (Washington, 1993) at 37 [hereinafter *Production Sharing 1988-1991*].

202 Conference Report on H.R. 3, the Omnibus Trade and Competitiveness Act of 1988, House Report 100-576, April 20, 1988 at 549-550 quoted in *Production Sharing 1986-1989, supra* note 190 at A-9.

Simplification Act[203] gave the Tariff Commission the authority to establish new tariff categories based on existing court decisions.

In *C.J. Tower & Sons* v. *United States*, the U.S. Customs Court concluded that marine engines sent to Canada to be installed into Canadian boat frames were exempt from duty on importation of the finished boat into the United States.[204] The principle established in this court decision was then codified into TSUS item 807.00 and, later, in HTS item 9802.00.80.

HTS 9802.00.80 provides beneficial tariff treatment to articles assembled abroad using U.S. components: the dutiable value of the finished product when reimported in the United States will be the value of the product less the value of the U.S. qualifying components[205].

Item 9802.00.80 refers to "[a]rticles assembled abroad in whole or in part of *fabricated components*, ... product[s] of the United States" [emphasis added]. The fabricated components must be exported in condition ready to assembly without further fabrication, should not lose their physical identity by change in form, shape or otherwise, and should not be increased in value or improved in condition abroad except by operations incidental to the assembly process.[206] Therefore, assembly, within the language of HTS item 9802.00.80, means "... no more than the actual physical process of fitting together components into a single finished product unaccompanied by any major process which would render the component different in kind, or fundamentally transformed, from the component first exported."[207]

---

[203] *Customs Simplification act of 1954*, Pub. L. No. 786, 83d Cong., 2d Sess. (1954) 68 Stat. 1163, 1137-1138 s. 202.

[204] 33 Customs Court 14 (1954).

[205] 19 U.S.C. s. 1202 (1983).

[206] *Ibid.*

[207] H.R. Rep. No. 342, 89th Cong., 1st Sess. 49 (1965) quoted by Al Watkins, "The Texas-Mexico Twin Plants System: Industry and Item 807.00 of the United States Tariff Schedule" (1985) 16:4 Texas Tech Law Review 963 at 966.

The U.S. Customs regulations define the term "fabricated component" as "a manufactured article ready for assembly in the condition as exported"[208]. An article qualifies as a fabricated component "product of the United States"[209] if it is "an article manufactured within the Customs territory of the United States"[210]. Thus, a fabricated component may be manufactured with imported raw materials without affecting its qualification as a "product of the United States"[211].

Articles assembled in offshore facilities using U.S. fabricated components are granted preferential duty treatment: they may be reimported into the United States with duty paid only on the value added abroad.[212]

2. The CBI Special Access Program

In February 1986, President Reagan announced the CBI Textile Program as a move to bring the textile and apparel trade within the context of the CBI from which it was originally excluded.[213] The proclaimed objectives of the program were: "[1]-to expand the manufacture of apparel in the Caribbean by providing

---

208 19 C.F.R. s. 10.12(d) (1991).

209 "Foreign-made articles or materials may become products of the United States if they undergo a process of manufacture in the United States which results in their substantial transformation. Substantial transformation occurs when, ... a new and different article emerges, having a distinctive name, character or use, which is different from that originally possessed by the article or material." 19 C.F.R. ss. 10.14(b).

210 19 C.F.R. s. 10.12(e) (1991).

211 "... a clear distinction must be made between assembly and fabrication in a foreign country because only components produced in the U.S. and exported in a condition ready for assembly are covered by that provision. Thus, a U.S. component subjected to further processing in a foreign country to put it into a condition ready for assembly (which constitutes fabrication as opposed to mere assembly and operations incidental to assembly) would fall outside the scope of item 807.00 TSUS [currently 9802.00.80 HTS]". Foote, *supra* note 162 at 332.

212 See *supra* note 205.

213 Peter Steele, *The Caribbean Clothing Industry* (London: The Economist Intelligence Unit, 1988) at 55.

guaranteed access to the US market for such clothing when produced under certain specific conditions; [2]-to help the US textile industry by ensuring that those conditions provided for the highest possible US inputs into the privileged categories of imports"[214].

This statement of objectives expressly recognizes the aim of making more competitive the U.S. textile industry through the development of the CBI Special Access Program: the expansion of the CBI to cover apparel manufacturing must ensure that the main categories of U.S. imports from the Caribbean will contain the maximum of U.S. fabrics.

The Special Access Program consists of the establishment of Guaranteed Access Levels (GALs) of specific textile categories from the Caribbean in the U.S. market. The GALs program, to be negotiated on a bilateral basis with each *CBERA* country, is a new form of quota[215] that only covers apparel assembly . The essential requirement in order to reach agreement in GALs is that the fabric be both formed and cut in the United States[216]. Hence, its Jamaican denomination as "All-American 807". This program is also familiarly known as "807A" or "Super 807"[217]. GALs are to be established in relation to the manufacturing capacity of the specific apparel categories of the *CBERA* country and may be increased by request of the

---

214 U.S. Department of Commerce, *Caribbean Basin Initiative Textile Program*, March, 1987 quoted by *ibid.*

215 Restraints to exports directed to the U.S. market may take the form of quotas or aggregate limits. Whereas quotas are directed to specific categories of products, aggregate limits may be imposed on all categories of exports to prevent sudden import surges in the U.S. market. Currently, aggregate limits are not applied to any of the major Caribbean textile suppliers. Quotas may take the following forms:
"- Designated Consultation Levels (DCLs). These are ceilings to which the importing country may request an increase. These are not subject to flexibility provisions(...).
- Specific Limits (SLs). These are limits fixed at a level for the duration of the agreement but, unlike the DCLs, are subject to annual growth provisions and flexibility (...). SLs tend to be used when the product is more sensitive in the US market." Steele, *supra* note 213 at 39-40.

216 "U.S. made fabric includes fabric woven or knitted in the USA from imported yarn, but excludes grey goods imported into the USA and finished there." *Ibid.* at 56.

217 *Ibid.*

government on the same basis. Thus, excepting the case of market disruption, access to the U.S. market is practically automatic and unlimited[218].

The current procedure followed by the United States Government is to negotiate specific limits[219] on apparel categories with *CBERA* beneficiary countries and, at the same time, to establish GALs for those categories.[220]

The Special Access Program does not contain duty preferences. Apparel products entered under GALs are remitted to HTS item 9802.00.80, and are thus dutiable only on the value added during the offshore assembly process. This program, however, allows apparel made of U.S. formed and cut cloth to be imported virtually free of quotas[221].

B. Textile and Apparel Imports under HTS Subheading 9802.00.80

The leading sources of textile and apparel imports under subheading 9802.00.80 are Mexico and several of the *CBERA* countries[222]. Indeed, they

---

218 This has been the situation with Costa Rican apparel suppliers who have had automatic approval when demanding increases of GALs limits. Interview with Luis Guillermo Elizondo, Consejo Nacional de Administracion de Cuotas Textiles y Ropa Confeccionada (18 December 1992) San Jose, Costa Rica. "...the action of the U.S. administration in granting a Gal merely guaranteed that qualifying products would be admitted to the U.S. market without being inhibited by the usual quantitative restrictions or the threat of these being imposed. It did not guarantee that there would be a market for those products". Steele, *supra* note 213 at 57.

219 Specific limits are defined in *supra* note 215.

220 Letter of H.J. Rosenbaum, Senior Policy Advisor, Office of the United States Trade Representative (27 January 1993).

221 *Ibid.*

222 "China emerged as the top supplier of all U.S. imports of textiles, apparel and footwear in 1991, as imports of China nearly tripled during 1988-91 ...China accounted for 16 percent of total U.S. imports of these products in 1991, followed by Korea (12 percent), Hong Kong (10 percent), and Taiwan (10 percent). However, only 3 percent of total textile, apparel, and footwear imports from these four Asian suppliers were from production-sharing operations in 1991". *Production Sharing 1988-1991, supra* note 201 at 37.

accounted for over 90 percent of such textile and apparel trade in 1991[223]. Mexico and the Dominican Republic were the top suppliers of nearly all apparel categories. To a lesser extent, Costa Rica was a significant source for trousers, slacks, and shorts; coats and jackets; and body- supporting garments. Jamaica and Guatemala were important sources for shirts and blouses, and the Philippines was a leading supplier of body-supporting garment.[224]

In general, imports from developing countries contain most of the U.S. fabricated components under subheading 9802.00.80 "reflecting the use of low-wage rate countries by U.S. firms seeking to reduce the costs of assembling labour-intensive products"[225]. The growth of Caribbean apparel exports, however, is not only due to low-cost labour but also to increased foreign investment seeking to avoid tight quotas imposed on textile and apparel exports from Hong Kong, Korea and Taiwan[226]. Indeed, "... producers in those countries as well as the United States have shifted their focus to the Caribbean region as a site for export-oriented production"[227].

Most of the Caribbean textile and apparel exports are directed to the U.S. market[228]. U.S. investment, which is dominant in the Caribbean Basin, is

---

223 See Appendix F-1 and F-2.

224 *Production Sharing 1988-1991, supra* note 201 at 37-41.

225 *TSUS 806.00 and 807.00 Report, supra* note 185 at 2-2.

226 *Production Sharing 1986-1989, supra* note 190 at 29. Imports from Hong Kong, Korea and Taiwan are limited to an average annual growth of one percent. *Production Sharing 1985-1988, supra* note 198 at 6-2.

227 *Production Sharing 1988-1991, supra* note 201 at 41. "Asian investment in the region have been largely influenced by rising costs of production in the Far East, as well as an experienced quota reduction to the US market for Singapore, South Korea, Taiwan and Hong Kong in 1989". Jennifer Hosten-Craig, *The Effect of a North American Free Trade Agreement on the Common wealth Caribbean* (Ontario: The Edwin Mellen Press, 1992) at 100.

228 "The countries of the Caribbean Basin were small suppliers of the international apparel market for many years but their exports increased substantially in the 1980s in both absolute terms and relative to other sources. Apart from the intra-regional trade of the CACM (Central American Common Market) and Caricom (Caribbean Community and Common Market) groupings which was

concentrated in production using item 9802.00.80[229]. On the other hand, Asian investment[230], which is also significant, is focused in cut, make and trim [CMT]. It usually employs Asian fabrics in preference of U.S. fabrics[231].

Asian CMT provides more opportunities for development of the Caribbean Basin than U.S. item 9802.00.80. Indeed, it requires more capital, produces higher value-added products, uses more labour, and promotes higher development of skill than does item 9802.00.80, which is limited to assembly. The CBERA countries, however, are not promoting these CMT operations. Asian investment is currently being discouraged in order to avoid frictions with the U.S. textile and apparel industry and a possible tightened of trade restrictions by the U.S. Government. This attitude acknowledges that Caribbean apparel made with Asian fabric is a threat to the U.S. manufacturers[232], and that Caribbean countries must keep the U.S. market open to their products.

Textiles and apparel represented the largest source of growth of U.S. imports from CBERA countries during the 1988-1991 period[233]. Although the main factor encouraging U.S. outward processing of textiles and apparel are the low Caribbean

---

always small in world market terms and has been reduced almost to insignificance in recent years, the main outlet for Caribbean apparel exports has been the USA". Steele, *supra* note 213 at 67.

229 *TSUS Items 806.30 and 807.00 Report, supra* note 185 at 5-5. In Costa Rica U. S. companies are responsible for 57.35 percent of total direct investment in the 10 principal export categories of the apparel sector. Ministerio de Comercio Exterior, *Costa Rica: Total Exports 1987-1991* (San Jose: Ministerio de Comercio Exterior, 1991).

230 "Jamaica has been particularly attractive to Asian investors because it is an English-speaking country and Jamaican exports receive preferential access to EC markets under the Lome Convention". *Production Sharing 1988-1991, supra* note 201 at 41.

231 *Production Sharing 1986-1989, supra* note 190 at 28.

232 *Ibid.* at 29. See also Steele, *supra* note 213 at 56.

233 *Seventh Report, supra* note 139 at 2-7.

wage rates[234], the use of HTS item 9802.00.80 is also an important source of cost savings for the apparel industry[235]. Indeed, the U.S. duty rates on imported apparel are higher than for most other products. As U.S.-origin content enters duty free under item 9802.00.80, there is a strong incentive to maximise its use in offshore apparel[236]. The significant quantities of U.S. content in apparel imports has allowed this industrial group to have the greater duty savings than any other[237]: "Unlike most products entered under subheading 9802.00.80, the duty-free, U.S. origin content of textile, apparel and footwear imports exceeds the dutiable portion of such imports. During 1988-91, the U.S.-made content averaged 54 percent for textiles, apparel, and footwear as opposed to 22 percent of all other product sectors combined."[238]

The apparel and textile industry accounted for 55 percent of the total duty savings under item 9802.00.80 in 1991, despite supplying only 16 percent of total

---

[234] See *supra* note 200 and accompanying text. "One of the principal attractions for foreign investment in the Caribbean is the relatively low cost of labour. Of the Caribbean suppliers, the Dominican Republic and Haiti offer the lowest hourly compensation, and the largest pools of available labour. Liberal social benefits and a better educated workforce account for Costa Rica's relatively higher wages. However, their higher wages are offset by the ability of firms in Costa Rica to handle a full range of production and frequent style changes. By contrast, firms in Haiti are more limited, producing budget articles with few style changes". *Production Sharing 1988-1991, supra* note 201 at 41.

[235] "The duty savings accrued from use of the production-sharing tariff provisions ($150 million for trousers, slacks, and shorts; $67 million for shirts and blouses; and $44 million for body-supporting garments) is an important consideration for the segment of the U.S. apparel industry that uses labour in Mexico and the Caribbean Basin to reduce their sewing costs". *Production Sharing 1988-1991, supra* note 201 at 37.

[236] "[T]he trade-weighted average nominal tariff for [the textiles, apparel and footwear sector] was 16.9 percent ad valorem versus an average of only 2.3 percent ad valorem for all other products in 1991". *Ibid;* see also *TSUS 806.30 and 807.00 Report, supra* note 185 at 4-3 and 4-4.

[237] *Production Sharing 1986-1989, supra* note 190 at 14.

[238] *Production Sharing 1988-1991, supra* note 201 at 37.

imports under that subheading[239].

C. U.S. "National Interest" Viewpoint

The U. S. International Trade Commission (ITC) has indicated the benefits of subheading 9802.00.80 for the U.S. market in a study conducted in 1988[240].

The ITC pointed out the increased use of U.S.-made components by foreign manufacturers, especially Canadian and Japanese firms, seeking to strengthen their position in the U.S. market:

> "The U.S. Department of Commerce anticipates that the Japanese in particular, will develop a large number of assembly operations in Mexico. Facing intense competition from producers in Korea and Taiwan of maturing and labour-intensive products, Japanese firms gain two advantages from these operations: lower labour costs and lower import duties, when U.S. components or materials are incorporated in the final product"[241].

Item 9802.00.80 has also promoted the use of U.S.-made components in U.S. offshore assembly operations. In many cases, the components necessary for global manufacturing are only available in East Asia and in the United States, but Asian-made parts and subassemblies are usually less expensive. Therefore, companies with operations only in the United States have increased their use of East Asian components, while companies with offshore assembly facilities have generally increased their purchases of U.S. components to obtain the duty savings of item 9802.00.80, thus favouring U.S. components suppliers[242].

Company surveys undertaken by the ITC have shown that the loss of

---

239 *Ibid.* "Apparel accounted for 80 percent of total subheading 9802.00.80 imports of textiles, apparel, and footwear in 1989. Footwear accounted for another 18 percent and textiles for the remaining 2 percent". *Production Sharing 1986-1989, supra* note 190 at 26.

240 *TSUS 806.30 and 807.00 Report, supra* note 185.

241 *Ibid.* at xxxii.

242 *Ibid.* at 6-7.

advantages under item 9802.00.80 would generate different consequences among U.S. industries manufacturing in the Caribbean. The most common response to such a loss would be to increase the industry's competitiveness by altering company cost structures. This would mean substituting foreign-made components, particularly from East Asia, for U.S.-made components. This would harm U.S. component suppliers more than the offshore assembly facilities, since "U.S. sources would become less cost competitive with lower cost Asian sources and would most likely experience significant sales declines ..."[243]. Other answers given by U.S. corporations facing the possibility of losing item 9802.00.80 were: a) continue with offshore operations using U.S. fabricated components but with a possible loss in market share because of the higher costs resulting from the tariff rates; b) go out of business altogether; c) shift operations overseas, thus harming U.S. suppliers and the local economies at plant locations; and d) drop product lines produced by assembly facilities and import finished products from lower cost sources. Moreover, there were two constant features present in the answers given by U.S. companies. First, each firm emphasized the need to reevaluate the company's cost structure due to the tariff imposition. On the other hand, U.S. firms recognized that U.S. component suppliers would probably sustain greater losses because of business closures, the switch to non-U.S. components, or the importation of finished products. This was further emphasized "by the choice of all the firms contacted not to move any assembly operations back to the United States"[244].

Finally, from a U.S. "national interest" viewpoint, the ITC has pointed out that item 9802.00.80 brings an important advantage to the U.S. economy. As noted

---

[243] "[A]ssembly manufacturing activities would most likely continue by using low cost foreign-made components. U.S. manufacturers are less likely to shift all operations overseas or import finish products, wanting to retain proximity to the U.S. ...and to avoid the cost inherent to plant closures". *Ibid.* at 6-24.

[244] *Ibid.* Likewise, in a report on items 806.30 and 807.00 realized by the U.S. Tariff Commission in 1970 it was concluded that few jobs would be saved or repatriated if those items were repealed. Sklair, *supra* note 194 at 49.

above, this provision promotes the use of U.S.-made components and materials in U.S. imports. Thus, the growth of 9802.80.00 imports results in an increase in U.S. product value[245]. In contrast, under the *CBERA*, which grants duty concessions to foreign exporters on foreign-origin content, imports growth results in an increase in the value of foreign-made content in U.S. imports. Therefore, U.S.-origin product value is not favoured by imports covered by the *CBERA*[246].

Offshore assembly processing has allowed U.S. industries which have a comparative disadvantage to improve their position by shifting labour-intensive production processes to low-cost developing countries[247]. Furthermore, HTS item 9802.00.80 has added to the costs savings of U.S. industries using outward processing, and, more importantly, this tariff provision has promoted the use of U.S. fabricated components. Since the elimination of item 9802.00.80 would certainly cause the substitution of foreign lower cost content for U.S.-origin content, one could foresee the negative consequences on U.S. suppliers[248]. The overall benefits of offshore assembly to the U.S. economy has, in consequence, promoted a change from neutrality to implicit support in the U.S. government's attitude towards the program[249].

---

245 Moreover, "use of foreign assembly facilities increases both U.S. exports and imports but has a minimal impact on the trade balance." Since item 9802.00.80 promotes the use of U.S.-origin instead of foreign-origin contents and materials, it reduces the trade deficit. *TSUS 806.30 and 807 Report, ibid.* at 6-14.

246 *Ibid.* at 4-1. Likewise, the imports growth under the GSP represents an increase of foreign value imports in the U.S. market. See *infra* note 144.

247 *Fatemi*, supra note 187 at 94.

248 *Ibid.*

249 The offshore assembly processing program has not been officially recognized by the U.S. government due to strong opposition from organized labour. Sklair, *supra* note 194 at 180.

CHAPTER III: RECENT DEVELOPMENTS IN INTERNATIONAL TRADE AND ITS EFFECTS ON THE CARIBBEAN TEXTILE AND APPAREL INDUSTRY

SECTION I: The Uruguay Round: Phasing Out the MFA

A. Liberalizing Textile Trade: A General Overview

The ministerial declaration for the Uruguay Round of multilateral negotiations under the General Agreement on Tariffs and Trade (GATT) established as one of its aims the formulation of "modalities that would permit the eventual integration of this sector [textiles and clothing] into GATT on the basis of strengthened GATT rules and disciplines, thereby also contributing to the objective of further liberalization of trade"[250].

The benefits of trade liberalization of textile and apparel trade has long been discussed in various studies. In particular, the costs and benefits of MFA protection have been analyzed in publications of the GATT, the Organization for Economic Co-operation and Development (OECD) and the World Bank, and in works by Cable[251], Hamilton[252], Sampson[253], Silberson[254], and Martin Wolf[255],

250 *Ministerial Declaration on the Uruguay Round*, GATT Doc. L/1396 (20 September 1986) reprinted in (1986) 25 I.L.M 1623 at 1627.

251 Vicent Cable, "Textiles and Clothing in a New Round of Trade Negotiations" (1987) 1:4 The World Bank Economic Review 304.

252 Carl B. Hamilton, "Follies of Policies for Textile Imports in Western Europe" (1985) 8 The World Economy 235; "Sampson Proposal: A Reply to Aubrey Silberston (1988) 11:2 The World Economy 301.

253 Gary Sampson, "Pseudo-economics of the MFA: a Proposal for Reform" (1987) 10:4 The World Economy 455; Gary Sampson & Wendy Takacs, "Returning Textile Trade to the Normal Worlings of GATT: a Proposal for Reform" in Carl B. Hamilton, ed., *Textile Trade and the Developing Countries: Eliminating the Multi-Fibre Arrangement in the 1990s* (Washington: The World Bank, 1990).

254 Aubrey Silberston, "Impracticalities of the Sampson Proposal for Phasing Out the MFA" (1988) 11:1 The World Economy 301.

among others. Recently, the OECD estimated that textile exports of developing countries could grow by around 80 percent and apparel exports by between 90 and 130 percent if trade in this area were liberalized[256]. We start, therefore, from the proposition that the MFA has had negative effects on consumers in importing countries since they had been forced to pay more for their clothing[257], and on the economic growth of developing countries since they had seen obstructed their potential export revenues and employment opportunities.

Apparel production is a labour-intensive industry. Automatation in this sector has not proved successful due to the constant variations inherent in clothing production. "The need for flexibility in the production process to meet the constantly changing fashions and large seasonal fluctuations in demand is the key factor behind a perpetuation of a labour-intensive production function in this industry"[258]. Thus, as low wages rates are generally present in developing nations, it is not difficult to conclude that those countries have comparative advantage in this labour-intensive industry. The clothing market, which is one of the most heavily protected markets in the industrialized world, presents the greatest trading opportunities for an important number of developing countries. Opening markets for developing countries' apparel products would stimulate significant growth in their industries. Apparel trade liberalization, although not the solution to problems of underdevelopment, could contribute to the economic growth of a significant part of the developing world. As Oxley has affirmed, "[n]o new conceptual work needs to be done or global commissions created to recommend it. It would not solve all problems of development. But it would make a big difference"[259].

---

255 Martin Wolf, "How to Unravel the Multi-Fibre Arrangement" (1985) 8:3 The World Economy 235.

256 Oxley, *supra* note 64 at 176.

257 See Chapter I, Section III:C, above, for a discussion of this issue.

258 Fatemi, *supra* note 187 at 103.

259 *Supra*, note 64 at 214.

Unlike apparel, the textile industry is at present highly mechanized. This automatation of the industry has given developed countries a comparative advantage in the sector without requiring excessive costs of protection[260]. Since textiles from developing countries do not currently represent a threat to industrialized nations[261], the need to resort to the MFA as a means of protection has disappeared[262]. Therefore, the textile sector should be liberalized to at least the same extent as apparel trade[263].

Traditionally, trade in textiles and apparel has not be subject to restraints with respect to industrialized countries[264]. By a gentleman's agreement[265], developed countries have avoided the mutual imposition of quantitative restrictions on their textile and apparel products. Thus, producers in industrialized countries are among the main beneficiaries of the MFA. Even the United States, not having a comparative advantage in the apparel industry, exported more clothing in 1987 than all the economies restrained under the MFA except for Hong Kong, Korea, Taiwan and India[266].

---

260 "[In 1986] U.S. consumer costs from protection in textiles amounted to only $2.8 billion annually, compared with $17.6 billion in apparel". William R. Cline, *The Future of World Trade in Textiles and Apparel,* 2nd ed. (Washington: Institute for International Economics, 1990) at 329.

261 From the U.S. total imports of textiles, apparel and footwear in 1989 under subheading 9802.00.80, textiles accounted for only 2 per cent while apparel imports accounted for an 80 per cent. *Production Sharing 1986-1989, supra* note 190 at 26.

262 The MFA was designed to be a temporary restraint on trade. Developed countries asked for the MFA as a means to allow time for the reorganization and adjustment of their textile industries. See Chapter I, Section I:B, *above.*

263 Cline, *supra* note 260 at 330.

264 "The determination to avoid restrictions on their own exports [by developed countries] and the corresponding evasions of the GATT discipline have been quite an important element in the textile history". Martin Wolf, "How to Cut the Textile Knot: Alternative Paths to Liberalization of the MFA" in Carl B. Hamilton, ed., *Textile Trade and the Developing Countries: Eliminating the Multi-Fibre Arrangement in the 1990s* (Washington: The World Bank, 1990) at 223.

265 See Chapter I, Section III, above.

266 Wolf, *supra* note 264 at 233.

Discrimination against developing countries has governed textile trade since the establishment of the STA. The protectionist mechanisms envisioned in the MFA, and the continued tightening of these mechanisms in subsequent renewals, have not only resulted in but have been maintained because of political pressures from the national industries[267]. An example of the political power of textile industries in modelling the international textile trade regime is found in the U.S. Jenkins Bill of 1985. Responding to the import surges of 1984, the Textile and Apparel Trade Enforcement Act of 1985 or Jenkins Bill was directed to the perpetuation of discriminatory treatment against developing countries by exempting only Canada and the European Community from restricting their textile exports. However, it would have favoured the Caribbean Basin Countries and Mexico since they were excluded from tighter restraints for sensitive products and from the graduation provisions[268]. President Reagan vetoed the bill and the House came within eight votes of the two-thirds vote needed to override the veto. The failure of the overriding vote was mainly due to the "preemptive protection" of the industry exerted by the administration. Indeed, the conclusion of new tighter bilateral agreements with principle suppliers and the adoption of a tougher position in the negotiations of extension of MFA IV, gave support to the presidential position. By the time of the override vote, the Protocol of Extension of MFA IV had already been approved with more complete product coverage and with new significant bilateral agreements in

---

267 For a discussion of this issue see above Chapter I, Section I. "The desire to persuade other industrial countries to liberalize was one reason for the American desire to create an international textile arrangement, but the most important aim was to protect both its own trade policy and the GATT from irresistible political pressure at a time when appearances still mattered a great deal. There was a belief that the GATT's safeguard clause (Article XIX) would explode if used as a container for the *pressures generated by textiles*. The greatest danger was thought to be congressional legislation in violation of the international obligations of the United States, leading to disintegration of the fabric of the GATT. The solution was an arrangement authorising discriminatory protection against 'disruptive' exporters, but one that also promised liberalization, if not yet." [emphasis added] *Wolf, ibid* at 219.

268 Cline, *supra* note 260 at 209. See also I. M. Destler "United States Trade Policymaking in the Uruguay Round" in Henry R. Nau, *Domestic Trade Politics and the Uruguay Round* (New York: Columbia University Press, 1989).

place[269]. This demonstration of broad political support for the textile sector has defined the general policies that have guided the MFA's evolution:

> "Conclusion of the important bilateral before renewal of the MFA meant in practice that the terms of the new MFA tended to follow those of the bilateral rather than viceversa as originally envisioned under the conception of the MFA as a moderating influence on concrete decisions."[270]

Since the MFA exists for political reasons[271] efforts to liberalize this industrial sector must also be approached politically[272]. The success of textile trade liberalization in the current multilateral trade negotiations depends in its acceptability to importing countries. Their domestic industries, having gained increased protection over time, will not easily accept a lowering of the current levels of protection[273] . If liberalization is to be reached, importing countries must make an irreversible decision to phase out the MFA[274].

The danger in not adopting a politically accurate scheme is that liberalization

---

269 Cline, *ibid.* at 210-214.

270 *Ibid.* at 214.

271 "But the legislative history of the past twenty-five years suggests that while the industry has not won *statutory* nontariff protection, it has held an effective veto power over broader trade legislation and the results of the multilateral negotiation. Kennedy had to appease the industry in 1962, Nixon in 1971-73, and Carter in 1979. It is not less powerful in U.S. politics today". Destler, *supra* note 268 at 203-204.

272 "[a]s it is evident that the reasons for keeping the MFA in place owe more to politics than to economics... a political gesture is necessary, in the form of mutual concessions between importing countries on one side, and exporting countries on the other". Marcelo Raffaelli "Some Considerations on the Multi-Fibre Arrangement: Past, Present and Future" in Carl B. Hamilton, ed., *Textile Trade and the Developing Countries: Eliminating the Multi-Fibre Arrangement in the 1990s* (Washington: The World Bank, 1990) at 272.

273 Bagchi, *supra* note 64 at 259. See also Raffaelli, *ibid.* at 272; Destler, *supra* note 268 at 204; Wolf, *supra* note 264 at 217.

274 "Such an approach would encounter domestic resistance in Canada as well as in the United States and the European Community; but if adopted by the major industrial countries it would provide a powerful inducement for some of the developing countries to participate more fully in the trading system." Murray G. Smith, *Canada's Stake in the Uruguay Round and the GATT System* (Ottawa: Institute Economics Program, 1988) at 16.

may become only a phase between two protectionist agreements:

> "This is no small danger. The price for liberalizing the MFA that will be demanded by the major importing countries will be 'strengthened rules and disciplines within the GATT'. This could prove to be a polite euphemism for the GATT's ruination, an attempt to introduce some of the most pernicious aspects of the MFA into the GATT itself"[275].

The problem that may arise in this attempt at liberalizing the textile sector is the insertion of the principles that govern international trade in textiles within the GATT system. That is, mainly, the legitimation of discriminatory treatment or selectivity in the application of the safeguard mechanism[276]. Liberalizing the MFA must imply primarily that nondiscriminatory treatment would continue to govern textile and apparel trade. Any scheme directed at integrating the MFA into the GATT system should aim to eliminate any restriction under the former, maintaining only those restrictions which would be fully GATT consistent[277].

Any modality to phase out the MFA should contain a transitional period for progressive liberalization in order to avoid shocks in importing[278] and less-efficient exporting countries. Likewise, it would be necessary to establish a predetermined and unchangeable date in which trade in textiles and apparel would be totally covered by the GATT, thus eliminating any quantitative restrictions agreed to under the MFA. Finally, a body would be required to provide effective surveillance of the transitional

---

275 *Wolf, supra* note 264 at 217.

276 "The 'low cost' brand, once imposed with regard to the textile sector, has been extended to other economic activities. If a new safeguard clause were approved in the Uruguay Round of GATT, allowing for selective safeguards, I fear its application would follow the MFA pattern, and that safeguards always would be applied selectively and only to countries already branded as 'low cost'". Raffaelli, *supra* note 272 at 272.

277 Bagchi, *supra* note 64 at 261. Wolf, *supra* note 264 at 225.

278 The MFA was adopted as a *temporary* instrument that would allow the adjustment of the textile industry in developed countries. See Chapter I, Section I: B, above.

period[279]. Compliance with the aforementioned requirements would guarantee the effectiveness of the liberalization process.

Different modalities for the liberalization of textile and apparel trade have been proposed by Cline[280], Sampson[281], Silberston[282], Raffaelli[283], and Wolf[284], among others. However, since the proposal adopted in the Dunkel Text for the phase-out of the MFA will be referred to in the following section, only some modalities will be noted:

Accelerated growth rates: Under this modality MFA growth rates should be increased significantly over the period of liberalization. This gradual process would attempt to reach a point in which all quotas cease to be binding even before the end of the process[285]. New restrictions would be permitted only in accordance with the GATT means of protection: the tariff[286].

Global quotas: This proposal relies on Article XIX of the GATT and calls for the replacement of the MFA bilateral agreements for global quotas. Under this system, discriminatory treatment would be immediately eliminated since all countries, including industrialized nations, would be covered by quotas. The quotas could be auctioned off or allocated (the former being a better way to comply with the nondiscrimination principle). In order to reach complete liberalization, a progressive elimination of the global quotas, during a established period of time, would be

---

279 Raffaelli, *supra* note 272 at 274-276.

280 Cline, *supra* note 260.

281 Sampson, *supra* note 253.

282 Silberston, *supra* note 254.

283 Raffaelli, *supra* note 272.

284 Wolf, *supra* note 255.

285 Bagchi, *supra* note 64 at 245. See also Wolf, *supra* note 264 at 226.

286 *Ibid.* at 246.

needed[287].

The global quotas system has been proven in the past by Canada and Norway. However, the quotas were discontinued either because of pressure exerted by other industrialized countries or because the MFA was found to be more convenient[288]. Particularly, the United States had reacted violently against decisions of other countries to introduce such quotas[289].

Tariffication: Under this scheme there would be a complete substitution of tariffs for the current quota system. In order to reach such agreement, tariffs should be high enough to allow the same protection afforded by quotas. This mechanism would provide a framework for a reciprocal tariff-cutting negotiation along traditional lines, would immediately reject discrimination, and would use tariffs as a means of protection[290].

Annual removal of quotas: After establishing a date for the completion of the phase-out process, the quotas' removal would be carried out on an annual percentage basis, *i.e.*, 10 percent of the existing quotas would be eliminated during a 10-year period[291].

Quota utilization: Under this proposal there would be a progressive elimination of quotas depending in the rate of quota utilization, *e.g.*, the reduction could start with all quotas filled up to 50 percent. An increasing percentage would

---

287 Wolf, *supra* note 264 at 227.

288 Bagchi, *supra* note 64 at 250.

289 Wolf, *supra* note 264 at 223. Interestingly enough, the modality of global quotas was proposed by the United States in the current Uruguay Round Negotiations. However, it was strongly opposed by the European Community which has not been subject to MFA restrictions due to a gentleman's agreement. Likewise, a number of less-efficient developing countries opposed the model since it would eliminate their current guaranteed access to some developed markets. Many developing countries feared that a global quota would take away their present market share when facing cheaper and more efficient exporters like China. Oxley, *supra* note 64 at 178.

290 Wolf, *supra* note 264 at 228.

291 Bagchi, *supra* note 64 at 247.

continue to govern the elimination on a progressive basis[292].

Removal of underutilized quotas: By this scheme underutilized quotas would be removed. Although this could be an important part of the liberalization process, it would be incomplete on its own.

Removal of quotas on small suppliers: The removal of quotas on small suppliers, like the preceding proposal, could also be a starting point of the liberalization process. However, it would not be enough to accomplish the phase-out of the MFA.

B. The Dunkel Text

Any comment regarding to the Dunkel Text in Textiles and Apparel must be preceeded by a consideration of the commitment adopted in the Punta del Este Declaration and in the Mid-Term Review of the Uruguay Round[293]. The Punta del Este Declaration establishes that negotiations in textiles shall aim to formulate modalities for the integration of this sector into GATT "*thereby* also contributing to the objective of further liberalization of trade" [emphasis added]. As written, the clause seems to imply that liberalization of trade will occur *per se* once modalities for the integration of the MFA into GATT have been implemented. In the *Mid-Term Review*, that objective was reinforced, and it was specified that "such modalities for the process of integration into GATT on the basis of strengthened GATT rules and disciplines should inter alia cover the phasing out of restrictions under the Multi-fibre Arrangement and other restrictions on textiles and clothing *not consistent with GATT rules and disciplines...* " [emphasis added]. As noted above[294], the danger of this type of commitment may be the introduction into the GATT of 'some of the most

---

292 *Ibid.* at 246-247.

293 General Agreement on Tariffs and Trade, *Decisions Adopted at the Mid-Term Review of the Uruguay Round*, (April 8, 1989), printed in 28 I.L.M. 1203 (1989) (hereinafter *Mid-Term Review*).

294 *Supra* note 275 and accompanying text.

pernicious aspects of the MFA'. Thereby, perpetuating the current protectionism of the textile and apparel sector, and possibly extending it to other trade sectors.

In examining the *Punta del Este Declaration* and the *Mid-Term Review* with respect to what the commitment amounted to in the textile sector, Oxley has affirmed that "[u]nlike the case with agriculture, there is no actual commitment to reduce the level of protection"[295]. Indeed, the Ministers' position on agricultural trade was more accurate than their reference to the textile sector. While the *Punta del Este Declaration* states that negotiations shall aim "to achieve greater liberalization of trade in agriculture", the *Mid-Term Review* adopted the precise compromise of ensuring that "tariff and non-tariff market access barriers in force at the date of this decision are not subsequently intensified in relation to imports of agricultural products nor extended to additional products...". Likewise, the adopted long-term objective in the latter agreement was "to provide for substantial progressive reductions in agricultural support and protection sustained over an agreed period of time, resulting in correcting and preventing restrictions and distortions in world agricultural markets".

The differences in the wording of the above-mentioned commitments suggest that liberalization of textile trade is a more difficult task than liberalization of the agricultural sector. While at the *Mid-Term Review* clear compromise was reached in order not to increase protection in agricultural products, this did not occur with respect to textile and apparel products. Moreover, after approval of the adoption of the Protocol Maintaining in Force the MFA from August 1991 to December 1992, the representative of India expressed disappointment in not having reached a commitment to refrain from invoking the MFA safeguard provisions during the extended period. Since the Uruguay Round negotiations were taking place in order to liberalize and integrate the textile sector into GATT a decision of such nature

---

[295] Oxley, *supra* note 64 at 177.

would have been compatible with the negotiations[296].

Keeping in mind that in the Uruguay Round negotiations there is no actual commitment to reduce the level of protection in textile trade, we will proceed to analyze the agreement on textiles and clothing in the Dunkel Text (ATC)[297].

1. The Integration Process

The integration process of the MFA into the GATT, as envisioned in the ATC, will be progressive. It will commence after the conclusion of the Uruguay Round and be finished in the year 2003, date by which the textiles and clothing sector should be fully integrated into the GATT[298].

The ATC only regulates the transitional period for the integration of the textiles and clothing sector into the GATT[299]. Once the transitional period is completed, the sector will be governed by the normal GATT instruments.

A Textiles Monitoring Body (TMB), whose members shall be designated by the GATT council, is established in the ATC. The TMB will supervise the implementation of the agreement[300], including the new restrictions to be imposed in accordance with the transitional safeguard mechanism discussed below. The TMB plays a significant role since its recommendations must be accepted by the parties. The ATC indicates that the parties shall *endeavour* to comply with the recommendations of the TMB. In case a party considers itself unable to accept *in full* those recommendations, it shall give its reasons to the TMB. The TMB, after

---

[296] GATT, Committee on Textiles, *Report of the Textiles Committee meeting held on 31 July 1991 adopted on 8 October 1991*, GATT, GATT Doc. COM.TEX/69, 38th supp. B.I.S.D (1992) 109 at 110.

[297] GATT, *Draft Final Act Embodying the Results of the Uruguay Round of Multilateral Trade Negotiations: Agreement on Textiles and Clothing* (Geneva: GATT, 1991) at 1 [hereinafter *ATC*].

[298] *ATC*, preamble and art. 9.

[299] *Ibid.* art. 1(1).

[300] *Ibid.* art. 8(1).

having heard the party's reasoning, shall issue the recommendations that it considers appropriate. However, if the matter remains unresolved it may be taken up by any party "before the GATT council and invoke Article XXIII:2 procedures or other dispute settlement procedures of the General Agreement"[301].

The integration process of the MFA into the GATT will start with the notification of the bilateral agreements under MFA Article 4 to the TMB within 60 days following the coming into force of the ATC[302]. Quantitative restrictions not notified shall be terminated forthwith[303]. The notified restrictions shall immediately be governed by the ATC[304]. Likewise, unilateral measures taken under Article 3 of the MFA shall remain in effect for the duration specified therein, but shall not exceed twelve months[305]. Any new restriction should be introduced in accordance with the transitional safeguard mechanism established in Article 6 of the ATC.

The transitional period for integrating textiles and apparel sector into the GATT system shall be done in four stages: on the first day of entry into force of the ATC, each party will integrate into GATT those products which, in 1990, accounted for not less than 12 per cent of the total volume of imports in 1990 of the products covered by the agreement, in terms of Harmonized Schedules lines or categories[306]; on 1 January 1996, each party will integrate into GATT those products which, in 1990, accounted for not less than 17 per cent of the total volume of 1990 imports of the products covered by the agreement[307]; on 1 January 2000,

---

301 *Ibid.* art. 8(10).

302 *Ibid.* art. 2(1).

303 *Ibid.* art. 2(4).

304 *Ibid.* art. 2(1).

305 *Ibid.* art. 2(5).

306 *Ibid.* art. 2(6).

307 *Ibid.* art. 2(8).

the parties shall integrate the products which, in 1990, accounted for not less than 18 per cent of the total volume of 1990 imports of the products covered by the agreement[308]; and, finally, on 1 January 2003 all restrictions under the ATC should be eliminated and the textile and clothing sector should be completely integrated into GATT[309].

The quantitative restrictions not eliminated in the first stage of integration shall be subject to the following requirements: the annual growth rate[310] will be the same provided in the bilateral agreements and increased by 16 per cent during the first stage of the agreement (from 1993 to 1995)[311]. During the second stage (from 1996 to 1999) the growth rate will be increased by 25 per cent[312]. Finally, during the third stage (2000 to 2003) the growth rate will be increased by 27 per cent[313].

Quantitative restrictions would continue to be governed by the exporting countries[314] and the flexibility provisions[315] will be the same as those provided in the MFA bilateral agreements when the ATC comes into force[316].

The ATC modality of phase-out of the MFA has been perceived as "end loaded" by the GATT negotiators since it is said that the removal of restraints and

---

308 *Ibid.* art. 2(8)(b).

309 *Ibid.* art 2(8)(c).

310 See Chapter I, Section II:B(1), above, for a discussion of this issue.

311 *Ibid.* art. 2(13).

312 *Ibid.* art. 2(14)(i).

313 *Ibid.* art. 2(14)(ii).

314 *Ibid.* art 4(1).

315 See Chapter I, Section II:B(1), above, for a discussion of this issue.

316 *Ibid.* art. 2(16).

increase of growth rates will mainly occur at the end of the transitional period[317]. However, according to economic studies conducted by Cline[318], it seems that the ATC model will not bring liberalization to the textile and apparel sector.

In order to reach textile liberalization, Cline has estimated that a minimum annual growth rate of 7 per cent for MFA quota, with a target of 9 per cent average growth[319], should be established. Lower quota growth rates would only induce "retrogression toward higher protection"[320].

The ATC maintains the quota growth rates established under the MFA. Periodical increases to those growth rates are set during the different stages of the integration process. However, as the current growth rates are generally very low[321], those increases seem not directed to achieving liberalization. For example, those growth rates of 1 per cent under the MFA will be increased by 16 per cent during the first stage, by 25 per cent during the second stage, and by 27 per cent during the last stage of integration. This means that at the end of the transitional

---

317 Interview with Louis Gionet, Ministry of External Affairs: International Trade (31 May 1993) Ottawa.

318 Cline, *supra* note 260 at 341.

319 *Ibid.*

320 *Ibid* at 332.

321 "Low, even extremely low growth rates have been diversely justified as: (a) a means to avoid recurrence of market disruption; (b) the result (in cases of wide-ranging Article 4 agreements) of a negotiation in which a lower growth rate was agreed in exchange for another feature more advantageous to the exporting country; c) the way to avoid endangering the maintenance of minimum viable production; and so on. One should not be distracted by these explanations, which are valid fewer times than they are invalid. Very low growth rates are employed in the case of large exporting countries (the so-called 'predominant suppliers', i.e., Hong Kong and Korea) even in relation to products of which they are medium or small suppliers and where recurrence of market disruption obviously could not take place even if the normal 6 percent growth rate of the MFA were granted. Very low growth rates have been and are still been employed by the Nordic countries, which claim that these rates are all they can afford if they are to maintain a minimum viable production of items for which their markets are entirely open when the supplier is developed country, ... Very low growth rates have also been uniformly applied by the United States in the case of wool products. Whatever the product, whatever the size of the quota, whatever the *status* of the exporting country, whatever the shape of the particular line of production affected, the United States has never granted to any wool product a growth rate higher than 1 percent." Raffaelli, *supra* note 272 at 277.

period the growth rate will be 1.84 per cent. Since the annual growth rate will never reach 7 per cent, but only a maximum of 1.84 per cent, according to Cline's estimations, the ATC mechanism will increase protectionism instead of leading to liberalization.

2. Transitional Safeguard Mechanism

Of special importance is the transitional safeguard mechanism which will allow the imposition of new export restrictions during the transitional period. As noted above, this mechanism will apply to all products covered by the ATC, except those integrated into GATT. Once integration has occurred, any restriction should be applied in accordance with the respective GATT provisions.

The safeguard action must not be applied to products that are already subject to restraint under the agreement[322] and it must be invoked on a country-by-country basis. The party[323] resorting to the safeguard action must demonstrate that a particular product is being imported into its territory in such increased quantities that it is causing, or threatening to cause, serious damage to the domestic industry[324]. Serious damage, or actual threat thereof, must be determined on the basis of a sharp and substantial increase in imports, the level of imports as compared with imports from other sources, and the price differential between the products offered in the domestic market and those offered by the supplier[325].

---

[322] *Ibid.* art. 6(4).

[323] "A customs union may apply a safeguard measure as a single unit, all the requirements for the determination of serious damage or actual threat thereof under this Agreement shall be based on the conditions existing in the customs union as a whole. When a safeguard measure is applied on behalf of a member State, all the requirements for the determination of serious damage, or actual threat thereof, shall be based on the conditions existing in that member State and the measure shall be limited to that member State." *Ibid.* art. 6 note 1.

[324] *Ibid.* art. 6(2).

[325] *Ibid.* art. 6(4).

The imposition of quantitative restrictions may proceed by agreement or by unilateral decision[326]. If the parties reach a mutual understanding that restraint is required in order to stop or avoid serious damage to the domestic industry of the party proposing it, the restriction should proceed. The base level of such restraint shall not be lower than the actual level of exports or imports from the party concerned during the twelve-month period terminating two months preceding the month in which the request was made[327].

The TMB must determine if the agreement is justified according to the factual data on which the importing party based its determination of actual threat or existence of serious damage. The TMB, after receiving the information required, may make recommendations that it considers appropriate to the parties of the agreement[328].

If agreements are not reached between the parties, the importing party may apply the restraints and at the same time refer the matter to the TMB. The TMB shall promptly examine the matter, "including the determination of serious damage, and its causes", and make the recommendations it deems appropriate to the parties concerned[329].

The quantitative restrictions invoked under the ATC may remain in place during three years without extension, or until the product is removed from the scope of the agreement[330].

The ATC, like the MFA[331], places some limits on the measures to be taken under the transitional safeguard mechanism in order to protect supplier countries.

---

326 *Ibid.* arts. 6(8) & 10.

327 *Ibid.* art. 6(8).

328 *Ibid.* art. 6(9).

329 *Ibid.* art. 6(10).

330 *Ibid.* art. 6(12).

331 See Chapter I, Section II:(B), above, for a discussion of this issue.

An annual growth rate of 6 per cent is established for those quantitative restrictions that should remain in force for more than one year[332]. On the other hand, the flexibility provision allows that when the supplier party has more than one product restrained under the agreement, the base level for each of the products may be exceeded by 7 per cent "provided that the total exports subject to restraint do not exceed the total of the levels for all products so restrained"[333].

Although the criteria for application of the transitional safeguard mechanism is not phrased identically to that of the MFA, it is very similar. While the transitional safeguard action is focused in the existence of serious damage to domestic producers or actual threat thereof, the MFA safeguard action is based in the concept of "market disruption". However, the MFA concept of "market disruption" is based on the existence of serious damage or actual threat thereof to the domestic industry[334]. Besides, in the MFA, like in the ATC, the serious damage or actual threat thereof is generally caused by a sharp and substantial increase or imminent increase of imports of the specific product, and a price differential between the products offered in the domestic market and those offered by the supplier[335].

Facing the similarity of the criteria for the application of safeguard measures in both agreements, the question of the utility of the transitional safeguard mechanism becomes unavoidable. Is this new provision going to be applied in the same manner as the MFA "market disruption" standard? If the answer is affirmative there seems to be no real possibility of reducing the actual level of protection of the textile and apparel industries in the domestic markets of industrialized countries: "By the 1980's, the key concept of 'market disruption', the MFA equivalent of Art. XIX

---

[332] *ATC*, art. 6(13).

[333] *Ibid.* art. 6(14).

[334] *MFA*, *supra* note 33 Annex A(I).

[335] *Ibid.* Annex A(II).

'serious injury' did not have any real meaning. It was never interpreted by the TSB, due mainly to the [importing countries'] unwillingness to report to a multilateral, supranational body"[336]. On the other hand, if the answer is negative, it will be necessary to count on the political will of importing countries to comply with the recommendations of the TMB referred to above[337]. However, such willingness seems difficult to attain since the provisions governing the TMB are quite similar to those governing the TSB[338]. If major importing countries have not in the past taken into account the TSB, what would make them submit to the TMB's recommendations, especially since commitment to lower protection on textiles and apparel was reached neither in the Punta del Este Declaration nor in the Mid-Term review of the Uruguay Round?

3. Treatment of Least Developed Countries, Small Suppliers, Small Wool Suppliers and Offshore Assembly Countries:

The ATC grants more favourable treatment to the least developed countries, small suppliers, small wool suppliers and offshore assembly countries.

Small suppliers are those whose total volume of textile exports is small in comparison with the total volume of exports of other countries and who account for a small percentage of the total imports of the specific product into the importing

---

336 Loretta Lundy, "The GATT Safeguards Debacle and the Canadian Textiles and Clothing Policy" (1988) 22:6 Journal of World Trade 71 at 80.

337 See *supra* note 300 and accompanying text.

338 "1. The Textiles Committee shall establish a Textiles Surveillance Body to supervise the implementation of this agreement...
4. In the absence of any mutually agreed solution in bilateral negotiations or consultations between participating countries provided for in this Arrangement, the Textiles Surveillance Body at the request of either party, ... shall *make recommendations* to the parties concerned...
8. Participating countries shall *endeavour to accept in full* the recommendations of the Textiles Surveillance Body...
9. If, following recommendations by the Textiles Surveillance Body, problems continue to exist between the parties, these may be brought before the Textiles Committee or before the GATT Council through the normal GATT procedures..." [emphasis added]. MFA, *supra* note 33 art. 11.

party. "[D]ifferential and more favourable treatment" shall be given to those suppliers when fixing the base levels and growth rates of the restrictions. Besides, consideration must be taken of "the future possibilities for the development of their trade and the need to allow commercial quantities of imports from them"[339].

When placing quantitative restrictions on wool exports from small wool suppliers, the quota levels, growth rates and flexibility must be established having special consideration for the export needs of such countries[340]. As for small wool suppliers, the agreement refers to developing countries whose textile trade is dependent, almost exclusively, on the wool sector, and whose volume of textile trade is comparatively small in the markets of the importing countries[341].

Least developed countries shall be given significantly more favourable treatment than that provided to small suppliers, small wool suppliers and offshore assembly countries. The preferential treatment must be granted in all its elements, that is, in quota levels, growth rate and flexibility provisions, or, at least, on overall terms[342]. Like the MFA IV, the agreement does not define the least developed country group. A clarification of this provision would permit a better interpretation of the rule.

Finally, more favourable treatment shall be granted to reimports into a country of textile products which that party has exported to another party for offshore assembly, when the products are re-imported from a country for which this type of trade represents an important proportion of its total textile and apparel exports[343].

---

[339] *ATC*, art. 6(6)(b).

[340] *Ibid.* art. 6(6)(c).

[341] *Ibid.*

[342] *Ibid.* art. 6(6)(a).

[343] *Ibid.* art. 6(6)(d).

C. Possible Effects of a Successful Uruguay Round in Textiles and Clothing on the CBI countries

1. Nature of the Caribbean Apparel Industry

a. Producing in the Caribbean

The apparel industry has become the largest exporter of the Caribbean Basin[344].

Economic analysis by Erzan, Goto, and Holmes[345] suggest that apart from the domestic producers of developed countries, the Caribbean countries have been some of the few developing countries to benefit from the emergence of the MFA. The study concludes that the market share gains in the apparel industry by the Caribbean countries might be associated with restrictions on major suppliers, although there is also the possibility that gains could have been due to shifts in comparative advantage[346].

Although the restrictions generated by the MFA on major suppliers may have encouraged Caribbean textile exports, there are other factors that have influenced this result, such as the existence of abundant low-cost labour[347]. Indeed, the Caribbean region has been developed as an offshore sourcing space for foreign

---

344 See *supra* note 233 and accompanying text.

345 Refik Erzan, Junichi Goto & Paula Holmes, "Effects of the MFA on Developing Countries' Trade" in H.W. Singer, Neelambr Hatti & Rameshwr Tandon, eds., *Trade Liberalization in the 1990s*, vol. 8 (New Delhi: Indus Publishing Company, 1990).

346 *Ibid.* at 746.

347 "Even Korean firms, which enjoyed low-cost production for a long time, currently find it advantageous to relocate some of their plants in [the Caribbean and] Mexico to take advantage of the lower cost of labour and the closeness to their ultimate markets, and to avoid the penalties of protectionism". Fatemi, *supra* note 187 at 229.

corporations, mainly U.S. corporations[348]. The wage differential between the Caribbean countries and the U.S. for apparel assembly is so substantial that producing in the Caribbean is sometimes essential to keeping the foreign industry competitive at the international level[349].

However, the use of low labour cost countries as assembly zones in order to reduce production costs is not new. As far back as the 1950s and 1960s, Asian countries were the processing sites of U.S. companies[350]. Moreover, the use of Asian instead of U.S.-origin materials[351] added to the profitability of the U.S. industries.

Over time, however, there has been a shift of U.S. companies assembling in Asia to the Caribbean Basin. The closeness of the region to the U.S.[352], the existence of abundant low-cost labour, the possibility of receiving preferential tariff treatment under TSUS 807[353] (later HTS item 9802.00.80) when using U.S.-origin materials, and not being subject to strict quantitative restrictions[354] gave the region a comparative advantage over its Asian counterparts[355].

---

348 Raffaelli, *supra* note 272 at 288. See also Chapter II, Section II:B, above.

349 See for a discussion of this issue Chapter II, Section II:A, above.

350 Sklair, *supra* note 194 at 9-10.

351 See Chapter II, Section II:C, above.

352 Sklair, *supra* note 194 at 8.

353 See Chapter II, Section II:A(1), above.

354 Raffaelli, *supra* note 272 at 288.

355 See Appendix D.

b. The Caribbean Apparel "Maquiladoras"

Most of the Caribbean apparel exports are directed to the U.S. market[356] and enjoy U.S. preferential tariff treatment under HTS item 9802.00.80[357]. Under this program, products assembled in the Caribbean region with U.S. components may be re-imported in the United States with duty payable only on the value-added in the processing country[358]. Particularly, in the case of apparel assembly, duty would be only payable on the labour costs, since this is usually the only value added in the Caribbean countries.

The Caribbean region is currently an apparel "maquiladora"[359] area. It has basically guaranteed the maintenance of profitability in the U.S. market[360] by promoting the use of U.S. components, granting low labour costs, and, in general, keeping the U.S. textile industry competitive.

The establishment of apparel maquiladoras in the Caribbean Basin has

---

356 Over 90 per cent of apparel exports from the five leading-apparel producers of the Caribbean Basin -that is Costa Rica, Dominican Republic, Guatemala, Honduras and Jamaica-, are directed to the U.S. market. *NAFTA Effects on Apparel Investment in the CBERA Countries, supra* note 178 at 14-23.

357 See Chapter II, Section II, above.

358 *Ibid.*

359 "The term 'maquiladora' comes from the Spanish word *maquila*, which in colonial Mexico was the charge that millers collected for processing grain. Today maquiladora stands as a generic term for those firms which 'process' (assemble and/or transform in some way) components imported into Mexico [or the Caribbean countries] which are then reexported. Alternatively it can be said that maquiladora is an economic unit for the production of goods or services based on the temporary importation of raw materials and equipment to be transformed in Mexico [or the Caribbean countries] and subsequently sold abroad." Norris C. Clement, "An Overview of the Maquiladora Industry" (1987) 18 California Western International Law Journal 55 at 56.

360 However, "[f]or the U.S. labour movement, any foreign competition based on cheap labour was unfair, and since the 1960s it has continually campaigned against offshore sourcing on the grounds that it caused the loss of U.S. jobs" Sklair, *supra* note 194 at 8.

favoured the region since it has provided jobs and foreign exchange[361]. However, the long term consequences of this program do not seem to be entirely beneficial for the regional economies.

Apparel is an enclave industry with minimal integration into the Caribbean economy[362]. The precut goods arrive, are assembled with imported threads, and are shipped back. Only the wages earned by the workers remain to be spent within the Caribbean economies. Given that most materials arrive in the form of precut pieces, the possible domestic inputs are the machinery and the thread. The Caribbean countries are not producing the machinery nor the thread. Moreover, under the maquiladora programs established in the Caribbean countries[363], inputs are allowed to be imported duty-free. This duty-free status substantially diminishes the incentive to substitute Caribbean inputs. There is little possibility for domestic substitution unless the Caribbean region institutes a coherent industrial policy to vertically develop its textile industry from cotton to the finished good, as it was done

---

361 The apparel industry has made a significant contribution to the economies of CBERA countries. For example, in the Dominican Republic there were already 262 apparel firms operating for export markets in 1991. Employment by these firms ranges from 25 to 2.000 employees per company, with the average firm employing between 300 and 500 workers. However, the unemployment rate near Santo Domingo and the Haitian border is still as high as 30 per cent. Investment Promotion Council of the Dominican Republic, Survey of Apparel Companies Established in the Dominican Republic, 1991, cited in *NAFTA Effects on Apparel Investment in CBERA Countries, supra* note 178 at 17. In Jamaica, "the industry employed some 23,000 people [in 1989]. As in other Caribbean countries, some 95 percent of those employed are women. The largest [Free Trade Zone] in Jamaica is the Kingston Export Free Zone which expanded from 200 employees in 1981 to 15,000 in 1989. In addition, income generated from apparel exports rose from $26 million to $50 million between 1984 and 1985. The US market accounted for 87 percent of Jamaica's exports in 1990, 58 percent of which fell under the 807 outward processing programme. Total garment exports from Jamaica to the US for 1990 stood at US $248 million." Statistics provided by JAMPRO International Operations, July 22, 1991, cited in Hosten-Craig, *supra* note 227 at 112.

362 In this comment on apparel and its effects in the Caribbean economies we follow the comments of Fatemi that, although referring to the Mexican apparel maquiladora industry, are completely applicable to the Caribbean apparel case.

363 Each of the five leading apparel producing countries of the Caribbean Basin has implemented a number of investment policies designed to encourage investment in export-oriented industries, thus, favouring the establishment of apparel maquiladoras. For a summary of these investment policies see Appendix G.

in Korea[364].

Apparel maquiladoras are at the low-technology end of the scale for maquiladora industries. They provide virtually no transfer of technology and very little in the way of training to the labour force. However, as mentioned above, they have contributed to the Caribbean economies through the creation of jobs and the generation of foreign exchange.

The U.S. preferential treatment programs such as item 9802.00.80 and the Caribbean Special Access program[365], which encouraged the development of the Caribbean apparel maquiladora industry, have been severally criticised since they seem to promote the creation of industrial areas in developing countries that do not provide for a relatively self-sustaining development on a local basis[366]. This kind of preferential treatment has been qualified as a "cynical form of generosity" which encourages small countries with major development problems to promote industries not able to compete by themselves on global scales[367]. U. S. Congressman Green declared that "Item 807.00 merely promotes competition between Hong Kong and Haiti for lower wage labour to serve this [U.S.] market without building markets worldwide"[368]. Finally, Steele, when referring to the Special Access Program[369] for Caribbean Textiles, affirmed:

> "[It] is the obvious intent of the U.S. administration to make it impossible for participating countries to build up substantial apparel industries which are not just offshore assembly operations for US contractors but self-sufficient manufacturing enterprises such as those developed in the Big Three and other major garment supplying

---

364 Fatemi, *supra* note 187 at 109.

365 See Chapter II, Section II:A(2), above, for a discussion of this issue.

366 Sklair, *supra* note 194 at 195.

367 Oxley, *supra* note 64 at 35.

368 Congressman Green "Statement" in U.S. Congress: Subcommittee on Multinational Corporations, Committee of Foreign Relations quoted by Sklair, *supra* note 194 at 49.

369 See Chapter II, Section II:A(2), above.

> countries. The program seems to have been so structured as to discourage the possibility of such development. To this extent, it is inimical to the wider economic good of the CBI countries."[370]

Without attempting to evaluate the overall advantages and disadvantages of the maquiladora apparel industry for the development of the Caribbean region, it is worth noting that in the long term the Caribbean economies would benefit more by the development of a well-integrated industrial policy: "[o]ne possibility... could be a vertically integrated domestic textile industry that starts with cotton production and ends with ironing the final garments and includes the whole range of intermediate production steps, including the generation of needed capital"[371].

Although such a proposal seems almost unrealistic for a region generally overwhelmed by economic, social and political crises, it could lead to the creation of a Caribbean textile industry directed not only at achieving economic growth but to regional development on a self-sustained basis[372].

2. The Uruguay Round and the Caribbean Apparel Industry

A. The Hypotheses

When referring to the Multilateral Trade Negotiations on textiles and apparel and their effects on the Caribbean apparel industry, we must consider two different hypotheses: 1) effective liberalization to be attained in the negotiation process; and 2) continuity of the current protectionist tendency in textiles and apparel.

If the level of textile and apparel protectionism is reduced and there is liberalization of this industrial sector, two possible results may be foreseen: the Caribbean countries would probably not be able to compete in the international

---

[370] *Supra* note 213 at 58.

[371] Fatemi, *supra* note 187 at 115.

[372] *Ibid.*

markets, facing more efficient producers such as China, Hong Kong, Korea and Taiwan[373]; or the Caribbean region could continue to assemble foreign fabrics as long as its rate wages were comparative lower than in other supplier countries. In this case, the assembly process would probably be done with the most price competitive foreign-origin material in order to reduce production costs.

On the other hand, if there is no liberalization of textile trade and the current protectionist regime continues to govern, the Caribbean region will probably carry on serving the U.S. market as long as low wages, preferential treatment and access to the U.S. market are guaranteed. Therefore, the prolongation of the present international trade regime would favoured, at least in the short term, the economies of the Caribbean countries.

B. The Dunkel Text

The ATC, presently being discussed at the Uruguay Round Negotiations, does not seem to provide for a reduction of the level of protection in textile trade. Neither the Punta del Este Declaration nor the Mid-Term Review of the Uruguay Round contain an actual commitment to phase out the protectionist trends in major importing countries. Indeed, even if there is an integration of the textile and apparel sector into the GATT system, the safeguard mechanism to be used during the 10 year transitional period seems to provide basically the same, or even greater protection[374] than the MFA. The continued use of discriminatory treatment and quantitative restrictions will probably not allow the liberalization of international textile and apparel trade.

If the transitional mechanism for the phase-out of the MFA is approved by the GATT Contracting Parties, it is possible that its safeguard mechanism be introduced into GATT in order to maintain the same protectionist standards. This implies that

---

373 See *supra* note 222.

374 See Chapter III, Section I:B, above.

discrimination and the use of quotas would be part of the GATT system, and as Wolf has pointed out, "[t]hat price would not be worth paying. There are things worse even than the MFA. One of them would be a trading system with the GATT's body and the MFA's heart"[375].

Apart from the apparent absence of liberalization of textile trade, the Dunkel text specifically addresses offshore processing operations of the HTS item 9802.00.80 type[376]. The ATC specifies that imports resulting from offshore assembly operations would be treated more favourably if this type of trade represents a significant proportion of the total exports of textiles and clothing of the processing country. Therefore, under the Dunkel text the Caribbean countries would likely continue to receive U.S. preferential treatment since 80 per cent[377] of their apparel production is the result of this type of outward operations. This conclusion is reinforced when looking at the U.S. policies dealing with the Caribbean and Mexico in apparel and textile matters. Thus, for example, the Jenkins Bill mentioned before[378], although directed at perpetuating discriminatory treatment against developing producers of textiles, was not going to affect Mexico and the Caribbean countries since they were explicitly excluded from tighter restraints for sensitive products and from the graduation provisions.

It is also worth noting that under the Dunkel text processing suppliers are in a more favourable situation than under the MFA itself. Indeed, while the latter only provides that *consideration* shall be given to special and differential treatment to re-imports which a nation has exported to another country for processing and subsequent reimportation[379], the former specifies that *more favourable treatment*

---

[375] *Supra* note 264 at 235.

[376] *ATC*, art. 6(6)(d).

[377] *NAFTA Effects on Apparel Investment in CBERA Countries, supra* note 178 at 4.

[378] See *supra* note 268 and accompanying text.

[379] *MFA*, art. 6, para. 6.

shall be given to the aforementioned re-imports.

If the Dunkel text agreement on textiles and clothing is approved by the Contracting Parties it seems that there will be an integration of this sector into the GATT. However, this process would probably not affect the present status in protection of the textile industry.

The intention of maintaining the current international textile trade structure seems to be present in the whole ATC of the Dunkel text. Therefore, the Caribbean countries will probably not be affected by its approval since no real change will be introduced into the current structure of international textile trade.

SECTION II: The North American Free Trade Agreement

This section focuses on the regulation of textile trade in the North American Free Trade Agreement (NAFTA) already approved by the Canadian Government and awaiting approval of the U.S. and Mexican governments[380].

Specific attention will be paid to the textile trade relation between the United States and Mexico since this is the centre of concern for the CBERA governments and the foreign firms operating in the Caribbean Region.

Since apparel trade between Mexico and Canada has not been significant -only 0.5 of Canadian apparel imports come from Mexico and Canadian apparel exports to the Mexican market are even smaller[381]- the trade and investment effects introduced by removal of Canadian import duties and quotas on Mexican-made apparel will not be discussed.

---

[380] NAFTA was approved by the Canadian Legislature on June 24, 1993.

[381] Steven Globerman & Michael Walker, eds., *Assesing Nafta: A Trinational Analysis* (Vancouver: The Fraser Institute, 1993) at 132.

A. Textile Trade under NAFTA

Trade in textile and apparel goods under the North American Free Trade Agreement [NAFTA] is regulated in Chapter III, Annex 300-B: "Textile and Apparel Goods", and Chapter IV Annex 401, Section XI: "Textiles and Textile Articles".

Textile trade among Canada, Mexico and the United States, once the NAFTA comes into force, will be ruled by this agreement. In case of any inconsistency among NAFTA and other agreement directed to regulate trade in textiles and apparel, the former "shall prevail to the extent of the inconsistency unless the parties agree otherwise"[382]. It is worth noting that not only is NAFTA given priority over the MFA, but also over any other "existing or future agreement" applicable to textile and apparel trade. This provision intends to guarantee the priority of NAFTA over any agreement in textiles and apparel trade that may be reached in the present Uruguay Round Negotiations of the GATT.

1. Rules of Origin

NAFTA establishes a "yarn forward" rule of origin for most textile and apparel products. Under this test, not only must fabrics be formed in North America but the yarns also must be sourced from the United States, Mexico or Canada if the final product is to be granted NAFTA duty treatment[383].

The NAFTA rules of origin for textiles and apparel goods are tighter than

---

[382] *North American Free Trade Agreement between Canada, Mexico and the United States,* Minister of Supply and Services, Canada, 1992, Annex 300-B, Sect. 1 [hereinafter *NAFTA*].

[383] *Ibid.*, Annex 401, Section B, Section XI. Under NAFTA there is no a generic rule of origin covering all the textile and apparel products, but the rule of origin is established specifically for each particular product in accordance with the Harmonized Commodity Description and Coding System as adopted and implemented by the Parties in their respective tariff laws. NAFTA, Annex 401, Section A(a). In certain cases, imported fabrics that the NAFTA parties agree are in short supply may be used to form the final product without hampering its preferential treatment.

those under the Canada-U.S. Free Trade Agreement [FTA][384]. Under the latter only the fabrics must be North American if textiles products are to receive FTA preferential rates. This "fabric forward" rule resulted from the pressure of the U.S. textile and apparel industries that, opposing the existence of the FTA, sought compensation through its inclusion in the final package. The harmful effect of this rule of origin on Canadian textile and clothing manufacturers, which depends more on foreign inputs than do their U.S. counterparts, was partially recognized with the introduction in the FTA of "tariff rate quotas" (TRQs)[385]. Under the TRQs system, certain annual quantities of apparel made from imported yarns and of non-wool fabrics made from imported yarns are allowed to enter the U.S. market at FTA rates of duty[386], thus giving some relief from the strict rule of origin[387].

The system of TRQs is also established in NAFTA but under the name of "tariff preference levels" (TPLs)[388]. Specific TPLs apply to particular goods between Mexico and the United States, Canada and Mexico, and the United States and Canada[389]. These TPLs were introduced in order to "alleviate the needs of the textile and apparel North American industry"[390], that is, essentially, the requirement of complying with the "yarn forward" rule.

Although Canada's efforts to avoid the new rule of origin for textiles and

---

384 *Canada-United States Free Trade Agreement*, 22 December 1987, Can. T.S. 1989 No. 3, 27 I.L.M. 1203 281 (1988) [hereinafter *FTA*].

385 Globerman & Walker, *supra* note 381 at 134.

386 *FTA*, Chapter III, Annex 301.2, Section XI: 17 & 18.

387 Interestingly enough, Canadian textile exports to the United States began to increase even before the FTA was in effect. "The reality of the FTA and the need to adapt acted as a psychological trigger and firms began to look beyond the domestic market ... In 1989 Canadian textile exports to the U.S. were $464 million. In 1992 they approached $900 million. In 1993 they will pass the $1 billion...". Globerman & Walker, *supra* note 381 at 146.

388 *NAFTA*, Annex 300-B, Appendix 6 (B).

389 *Ibid.*

390 *Nafta: An Overview and Description* (Ottawa: Government of Canada, 1992) at 3.

apparel in NAFTA were not successful, it achieved extended TRQs[391]. Indeed, under NAFTA the TRQs, current TPLs, are increased and provided with annual growth rates between 1 and 2 per cent for at least five years[392].

Apparel products that are assembled in Mexico as provided for in HTS item 9802.00.80 from fabric which is knit or woven outside the territory of the United States or Mexico, will also be subject to TPLs when re-imported into the United States[393]. However, not all U.S. apparel imports under this provision may enjoy TPLs. The exceptions are man-made fibre sweaters and apparel made from oxford cloth, denim and some circular knit fabrics[394]. This exception only applies between Mexico and the United States, forcing the importer to pay regular MFA rates.

2. Tariff Elimination

Tariffs in textiles and apparel products traded between the United States and Mexico will be progressively reduced over a ten-year period[395]. There will be immediate elimination of tariffs on textile and apparel products re-imported into the United States that are assembled in Mexico from fabrics wholly formed and cut in the United States[396].

Most tariffs on textiles traded between Canada and Mexico will be eliminated over an eight-year period. Apparel tariffs will be reduced over a ten-year period[397].

---

391 Globerman & Walker, *supra* note 381 at 136.

392 *NAFTA*, Annex 300-B, Appendix 6(B).

393 *Ibid.*

394 *Ibid.*

395 *Ibid.* Annex 300-B, Appendix 2.1 (B).

396 *Ibid.* Annex 300-B, Appendix 2.4.

397 *Ibid.* Annex, 300-B, Appendix 2.1 (C).

Tariffs on textiles and apparel traded between Canada and the United States will continue to be reduced as set out under the FTA[398].

Annex 300-B, section 4 establishes a transitional emergency action to be used when serious damage or actual threat thereof to the domestic industry of a party is being produced due to the increased quantities of imports of a textile or apparel product into the territory of another party as a result of the reduction or elimination of a duty provided for in NAFTA. In such a case the importing party may suspend any further reduction of the tariff or increase the rate of tariffs to certain specified levels[399].

3. Quantitative Restrictions

Canada and the United States are not subject to the MFA[400]. MFA quantitative restrictions are only applied to Mexico by the United States.

MFA quotas on apparel goods that are assembled in Mexico from fabrics wholly formed and cut in the United States that are reimported into the United States will be removed once NAFTA comes into effect[401]. Quotas covering non-originating[402] goods will be eliminated progressively during a transition period of ten years[403].

NAFTA establishes a transitional safeguard mechanism that allows the imposition of temporary quantitative restrictions in non-originating goods against any

---

398 *Ibid.* Annex 300-B Appendix 2.1 (A).

399 The rate of duty may be increased to a level not to exceed the lesser of "(i) the most-favored-nation (MFN) applied rate of duty in effect at time the action is taken, and (ii) the MFN applied rate of duty in effect on December 31, 1993". *Ibid.* Section 4 (b).

400 See *supra* note 100 and accompanying text.

401 *NAFTA*, Annex 300-B, Appendix 2.4 and Appendix 3.1 (B) (9:a) and (10).

402 *Ibid.* Annex 300-B, Section 2 (2) (a).

403 *Ibid.* Annex 300-B, Appendix 3.1 (B) (9).

of the contracting parties[404]:

> "If a Party considers that a non-originating textile or apparel good, including a good entered under a tariff preference ..., is being imported into its territory from a Party in such increased quantities, in absolute terms or relative to the domestic market for that good, under such conditions as to cause serious damage, or actual threat thereof, to a domestic industry producing a like or directly competitive good in the importing Party, the importing Party may request consultations with the other Party with a view to eliminating the serious damage or actual threat thereof"[405].

However, if the safeguard mechanism is to be applied between the U.S. and Canada, the action continues to be governed by Article 407 of the FTA, "which is commonly interpreted as precluding quantitative restrictions"[406]. This means that quotas will be not adopted between Canada and the United States, but only between Mexico and Canada, or Mexico and the United States.

Interestingly enough, although NAFTA establishes its priority status over the MFA or any future agreement in trade on textiles and apparel, it sets a prohibition on adopting or maintaining any quantitative restriction under the safeguard mechanism if the specific product has been integrated into the GATT as a result of commitments undertaken by the Party that wants to place the restriction[407].

Once the transitional period has expired, the safeguard measures will not proceed except with the consent of the party against whom the action will be taken[408].

---

[404] *Ibid.* Annex 300-B, Section 5. No safeguard measures are permitted on "originating" goods.

[405] *Ibid.* Annex 300-B, Section 5(2).

[406] Globerman & Walker, *supra* note 381 at 146.

[407] *NAFTA*, Annex 300-B, Section 5 (12).

[408] *Ibid.* Annex 300-B, Section 5 (13).

B. The Mexican Apparel "Maquiladora"

Although the general reasons that allowed the emergence of Mexico as an offshore processing location were discussed above when studying the Caribbean case[409], it has been said that it is a significant development of the U.S. offshore assembly provision[410], i.e. HTS item 9802.00.80.

The Mexican Maquiladora Program[411], established in 1966, not only has helped to solve the huge Mexican problem of unemployment, but it is also the second largest source of foreign exchange, thus being considered an important part of the economy[412].

Over the last decade one of the main objectives of the Mexican government has been to integrate the maquiladora industry into the national economy[413]. "Optimally, Mexico must contribute more than its labor, eventually increasing its input of raw materials, parts and components in the Maquiladora manufacturing process. To date, the highest integration achieved is an abysmal 2%."[414]

---

409 See Chapter II, Section III:A, above.

410 Cheryl Schechter, "The Maquiladora Industry and Free Trade", Mexico Trade Letter, Articles from Canada. Gottlieb & Pearson, March 12, 1992.

411 ". Mexico formulated the Border Industrialization Program, which became known as the maquiladora system, and launched the program in May of 1966. Americans always had some degree of investment in Mexico, and had located some processing and assembling in Mexico, but the Border Industrialization Program was something new. The program was specifically designed to attract labor intensive industries... During the next two decades maquiladoras experience great success... The future of maquiladoras is likely to be as bright as its past... Labor costs in Mexico are roughly one-seventh of what they are in the U.S.; the Mexican government supports the program; transportation between the countries is generally inexpensive, and the United States still only charges a value added duty on components assembled abroad." Gray Sanders, "Maquiladoras and the Yucatan" (1990) 5:3 Florida International Law Journal 523 at 527-529.

412 Hosten-Craig, *supra* note 227 at 102.

413 Norris C. Clement, "An Overview of the Maquiladora Industry" (1987) 18 California Western International Law Journal 55 at 63.

414 Schechter, *supra* note 410 at 7.

Exports from the Mexican apparel maquiladora account for a significant portion of total Mexican apparel exports. Mexico does not have a vertically integrated domestic textile industry. It is essentially a supplier of apparel made with foreign components[415]. U.S. trade with Mexico, like in the case of the Caribbean, largely has involved the assembly of garments from U.S. components, hence the significant role that U.S. firms have played in the development of the Mexican apparel export industry[416]. It is estimated that at least 80 per cent of total Mexican apparel exports go to the United States[417], and that U.S. apparel imports from that country under subheading 9802.00.80 accounted for 92 per cent in 1991[418].

Before 1989, U.S. apparel imports from Mexico under HTS item 9802.00.80 were only subject to MFA quantitative restrictions. However, in the MFA bilateral agreement signed by the United States[419] and Mexico in 1988[420], the United States introduced a new program called the "Special Regime".

The Special Regime is similar to the Special Access Program[421] for the Caribbean Region. Under the Special Regime apparel items assembled in Mexico from fabric parts formed (i.e. knit or woven) and cut in the United States receive

---

415 Fatemi, *supra* note 187 at 109.

416 *Ibid.*

417 *NAFTA Effects on Apparel Investment in CBERA Countries*, *supra* note 178 at 3.

418 *Ibid.* at 4.

419 "The United States had import-restraint agreements or quotas with some 40 countries in 1991. These countries supplied 83 per cent of total MFA imports by value for that year". U.S. International Trade Commission, *U.S. Imports of Textiles and Apparel under the Multifiber Arrangement: Annual Report for 1991* (Washington, 1992) at iii.

420 *Bilateral Textile Agreement Between the United States of America and the United Mexican States*, Mazatlan: February 13, 1988.

421 See Chapter II, Section II:A(2), above.

liberalize import quota treatment when entering the U.S. market[422].

Unlike the Special Access Program, which uses separate quotas (GALs), and permits virtually unlimited market access for such products, the Special Regime "combines products of U S. and foreign fabrics under the same quota and limits quota growth to 6 per cent annually"[423]. Under this program, quantitative restrictions on Mexican apparel items were increased from 50 to 90 per cent[424].

In February 1990 the Special Regime was renegotiated and the United States eliminated quotas in 52 apparel items. The remaining quantitative restrictions were enlarged by 25 per cent[425].

Before the current preferential system, Mexican apparel producers opposed the use of maquiladora plants by U.S. apparel manufacturers. They were concerned that U.S. manufactures would use the scarce quota allocations, thus hampering their access to the U.S. market. The Mexican government, in supporting their domestic industry, was reluctant to approve additional participation by U.S. apparel producers in the Maquiladora program[426]. Moreover, the application of MFA quotas to apparel imports into the United States, even though the textiles originated in the United States, was also *per se* an impediment to the growth of apparel maquiladoras

---

422 *NAFTA Effects on Apparel Investment in CBERA Countries, supra* note 178 at 2.

423 *Production Sharing 1985-1988, supra* note 198 at 6-7.

424 Gary Clyde Hufbauer, et al., *Prospects for North American Free Trade: Textiles and Apparel* (Ottawa: unpublished paper, 1989) at 10 quoted by Hosten-Craig, supra note 227 at 103.

425 *Ibid.*

426 Cheryl Schechter and David Brill "Maquiladoras: Will the Program Continue?" (1992) 23:3 St. Mary's Law Journal 679 at 717. "The mexican government encouraged existing U.S.-affiliated maquila operations that were exporting apparel to foreign markets to do so directly from Mexico rather than export maquila-sewn apparel from related facilities in the United States so that more room would be left in the quotas for production by Mexican companies". *Production Sharing 1985-1988, supra* note 198 at 6-7.

since most of the Mexican quotas were filled[427] .

Nevertheless, since the establishment of the Special Regime, which provides a more liberalized import quota treatment, the Mexican apparel maquiladora industry appears to have expanded[428].

C. Foreseen Consequences of NAFTA on the Caribbean Textile and Apparel Industry

As studied before, Mexico and the CBERA Countries had represented a competitive geographical area for U.S. offshore assembly processing and other foreign apparel firms. Low-labour costs, among other factors, have given this region a comparative advantage in the production of labour-intensive products such as apparel[429].

In the last decade, however, U.S. imports of apparel from Mexico had been stagnant since the U.S. firms had chosen to expand offshore assembly operations in the Caribbean rather than in Mexico, because labour costs have been even lower in the former[430]. While by 1991, Mexican workers in the apparel industry earned US$1.20 per hour[431], workers from the Dominican Republic, the leading CBERA

---

427 Norris C. Clement and Stephen R. Jenner, Location Decisions Regarding Maquiladora/In-Bond Plants Operating in Baja California, Mexico, Border Issues Series, No.3 (San Diego. San Diego States University, Institute for Regional Studies of the Californias, 1987) cited by Fatemi, *supra* note 187 at 106.

428 This seems to be the tendency when analysing the increase of Mexican apparel exports under item 9802.00.80 during the period 1987-1991. While from 1987 to 1989 those exports increased by 142 millions of U.S. dollars, from 1989 to 1991 there was an increase of 283 millions of U.S dollars.

429 See Chapter II, Section II (A), above, for a discussion of this issue.

430 *Production Sharing 1985-1988, supra* note 198 at XIX.

431 *Yearbook of Labour Statistics*, International Labour Office, 51st issue, Geneva 1992; and United Nations, Department of Economic and Social Development, *Monthly Bulletin of Statistics*, Vol XLVII No. 4, April 1993.

exporter of apparel to the United States, had an hourly wage of US$0.77[432]. The opposition of the Mexican apparel industry to the use of the maquiladora plants by U.S. manufacturers before the existence of the Special Regime, may also have contributed to the stagnation of Mexican apparel exports to the U.S.

The selection of the Caribbean region as the site for apparel outward processing has been reflected in the growth level of the Mexican textile and apparel industry. While the Mexican national economy grew at about 3 per cent annually in the 1987-1990 period, the textile and apparel industry only grew at about 1.5 per cent[433]. In contrast. the Dominican Republic increased apparel production by an estimated 150 per cent during that period[434].

Despite the preference of establishing outward operations in the Caribbean Region, Mexico was the second largest source of apparel exports to the U.S. market after the Dominican Republic during the period 1987-1991[435]. This strong position of the Mexican apparel Maquiladora has been favoured lately not only with the establishment of the Special Regime, but also with the more liberalized treatment that in general U.S. authorities have granted to Mexican apparel exports to the United States. Thus, in 1989, the U.S. Commerce Department extended some quotas under the Special Regime in order to receive the Mexican apparel surplus in the U.S. market[436].

The Mexican apparel Maquiladora is likely to be favoured even more with the approval of NAFTA to the detriment of its Caribbean competitors. Concerns have been expressed, by both the U.S. firms operating in the Caribbean Region and the governments of the CBERA countries, in relation to the possible disruptive effects

---

432 *NAFTA Effects on Apparel Investment in CBERA Countries, supra* note 178 at 16.

433 *Ibid.* at 25.

434 *Ibid* at 16.

435 *Ibid.* at 25.

436 Hosten-Craig, *supra* note 227 at 103.

of a NAFTA on the current patterns of apparel trade[437].

In examining such concerns, the U.S. International Trade Commission (ITC) reported on the potential effects that the granting of duty-free and quota-free treatment to U.S. imports of Mexican apparel under HTS item 9802.00.80 could produce in the Caribbean Region[438].

The ITC drew conclusions for the CBERA Region as a whole based on the five countries that currently account for the majority of Caribbean apparel exports to the United States, that is, Costa Rica, Dominican Republic, Guatemala, Honduras and Jamaica. The hypothesis in the ITC's study was that NAFTA would immediately eliminate quantitative restrictions and tariffs on U.S. apparel imports from Mexico.

The cost analysis[439] and the trade diversion economic model[440] used by the ITC allow it to affirm that "although duty elimination may not provide an absolute cost advantage for Mexico in many items, it will produce some change in Mexico's favour, even in cases where the effective duty is relative small"[441].

In general terms, the ITC identified low-labour and transportation costs as the primary determinants of competitiveness for U.S. firms operating in the Caribbean and Mexico:

> "The size of non-U.S. cost component for identical products in apparel production-sharing operations is similar in the CBERA countries and Mexico. Elimination of duties and quotas on imports from Mexico, therefore, will improve the relative cost competitiveness of Mexican producers compared with their counterparts in the Caribbean and Central America --particularly those products with a large foreign assembly cost component. The findings of the investment diversion analysis indicate that a NAFTA will introduce incentives that will tend to favour apparel investment shifts from the CBERA countries to

---

437 *NAFTA Effects on Apparel Investment in CBERA Countries*, *supra* note 178 at vii.

438 *Ibid.*

439 See Appendix H.

440 See Appendix I.

441 *NAFTA Effects on Apparel Investment in CBERA Countries*, *supra* note 178 at 72.

> Mexico. However, it was not possible to identify the magnitude of any shifts for any of the countries... because of the lack of data on specific investment flows."[442]

As mentioned before in its study the ITC assumed that with NAFTA there will be an immediate elimination of all duties and quotas of U.S. apparel imports from Mexico under HTS item 9802.00.80. However, the hypothesis of a "yarn forward" rule of origin in NAFTA was also considered. The ITC estimated that although such a rule may reduce the incentives for investment shifts from CBERA countries to Mexico, it will not offset them[443].

The current NAFTA includes the "yarn forward" rule of origin. Indeed, only those apparel products that have been assembled in Mexico with U.S. materials wholly formed and cut in the United States and exported from and reimported into the United States will receive immediate duty-free treatment and quota elimination. Those Mexican apparel products that, although entering the U.S. market under HTS item 9802.00.80, are assembled with U.S. fabricated components manufactured with imported raw materials are subject to a 10-year transitional period in order to be freed of quantitative restrictions[444]. These products, however, are not subject to a tariff reduction process since they are not "originating" goods, that is, they do not meet the "yarn forward" rule of origin.

Interestingly enough, the inclusion of the "yarn forward" rule of origin in NAFTA instead of the "fabric forward" rule, will not make any difference in the competitiveness of the Mexican apparel Maquiladora in relation to its Caribbean counterparts since U.S.-formed fabrics are usually either woven or knit using U.S.-made yarns[445].

The establishment of NAFTA "would eliminate advantages of the CBI and the

---

442 *Ibid.* at 69.

443 *Ibid.* at 70-73.

444 See Chapter III, Section II:A, above.

445 *NAFTA Effects on Apparel Investment in CBERA Countries, supra* note 178 at 71.

natural advantages of Mexico would put it in a better position"[446]. Mexican low wages, lower transportation costs[447], and reduced tariffs under NAFTA, are likely to create an investment advantage for Mexico in the apparel sector[448] and increased opportunities for trade.

NAFTA seems to render ineffective the Caribbean region's preferential access and duty reductions. The Mexican-U.S. free trade relations would probably draw future foreign investment away from the CBERA countries unless some action is taken to equalize the Mexican and Caribbean positions. Such action could be the expansion of NAFTA to cover the CBERA countries[449], or the development of a special program that would permit the importation in the NAFTA area of Caribbean apparel in the same favourable terms under which Mexican apparel is imported.

If the potential harmful effects of NAFTA in the fragile Caribbean economies are ignored, these countries will be forced to provide firms with even greater cost-savings if they wish to offset the NAFTA benefits [450]. This implies, essentially, reducing even more the already low wage rates. However, if such a policy is adopted, it seems that the benefits of additional foreign investment in the Caribbean Region would be significantly diminished[451].

---

446 Hosten-Craig, *supra* note 227 at 109

447 Since Mexico is separated from the United States by a land border, transportation costs are lower between those countries than from the Caribbean region to the United States

448 Hosten, *supra* note 227 at 112. It may be affirmed that even before the proposal of NAFTA, Mexican apparel was favoured by the United States, due to the Mexican policy reforms that have allowed its transition from a protectionist regime to a more liberalized economic model Thus, for example, although in 1989 Mexican apparel exports reached the full quota, the U S Department of Commerce allowed the enlargement of the Designated Consultation Levels in order to accommodate additional exports to the United States. *Ibid* at 103.

449 Lazarus, *supra* note 68 at 179.

450 *NAFTA Effects on Apparel Investment on CBERA Countries*, *supra* note 178 at 73.

451 *Ibid.*

CONCLUSION

The Caribbean apparel industry is an outgrowth of a provision of the U.S. Harmonized Tariff Schedule which gran
yts preferential treatment to U.S. imports that have been assembled with U.S. fabricated components. In order to benefit from such preferential treatment, foreign investment, mainly U.S. investment, has been directed to the Caribbean Basin to take advantage of the abundant existence of low-cost labour. The Caribbean Basin has then been a site for outward processing where low production costs have maintained the competitiveness of foreign textile and apparel industries at the international level.

In the long term, however, the development of the Caribbean Basin as an offshore assembly processing area seems to be not entirely beneficial for the economies of the Caribbean countries. Indeed, there is no vertically integrated Caribbean textile and apparel industry able to compete by itself on an international scale. The Caribbean apparel industry is completely dependent on the U.S. market and thus not able to contribute to the general development of the region on a self-sustained basis.

Although the evolution of the Caribbean apparel industry may not be the most appropriate strategy for development, it is evident that until now it has provided jobs and foreign exchange to a region generally overwhelmed by high rates of unemployment and various economic and political crises. These benefits may be affected by any new development in the international textile and apparel trade order especially when the dependence of this industry in the U.S. market is considered. The phase-out of the Multifiber Arrangement presently being discussed at the Uruguay Round of Multilateral Trade Negotiations and the North American Free Trade Agreement is one of the present international instruments that may affect the future of the Caribbean textile and apparel industry.

The mechanism contemplated for the phase-out of the Multifiber Arrangement in the current Multilateral Trade Negotiations of the Uruguay Round does not seem to liberalize textile and apparel trade. The transitional mechanism for the integration of this trade sector into the GATT is very similar to the actual rules of the MFA. As such, textile and apparel trade will likely continue to be one of the sectors most highly protected at the international level, without any major change in its international regulation. Therefore, it seems that the Caribbean apparel industry will continue serving foreign firms without being affected by any deal that may be reached at the Uruguay Round.

Unlike the Uruguay Round Negotiations, the North America Free Trade Agreement seems to affect the Caribbean apparel industry. The U.S. granted preferential treatment to the Caribbean Basin with the creation of the CBI Special Access Program. However, the establishment of the Mexican Special Regime and the preferential duty treatment that Mexican apparel exports would receive with the implementation of NAFTA, is likely to create an investment advantage for Mexico that is detrimental to the Caribbean Region. The U.S. International Trade Commission has affirmed that if the Caribbean countries wish to confront the negative effects of NAFTA on their apparel industry, they must enlarge the advantages for foreign investment. However, this implies that labour rates must be lowered even more, thus reducing the benefits of foreign investment in the Region. A less painful option for the Caribbean Basin would be to become a party to NAFTA, thus gaining the same preferential treatment granted to Mexico. This solution would give the Caribbean countries an opportunity to compete on more equal terms with their Mexican counterpart.

BIBLIOGRAPHY

BOOKS AND MONOGRAPHS

Balassa, Bela. *New Directions in the World Economy* (New York: New York University Press, 1989).

Bagchi, Sanjoy. "Textiles in the Uruguay Round: Alternative Modalities for Integration into GATT" in Carl Hamilton, ed.. *Textile Trade and the Developing Countries: Eliminating the Multi-Fibre Arrangement in the 1990s* (Washington: The World Bank, 1990).

Baldwing, Robert E. *Trade Policy in a Changing World Economy* (Chicago: The University of Chicago Press).

Bhagwati, Jagdish. *The World Trading System at Risk* (New Jersey: Princeton University Press, 1991).

Bloker, Niels. *International Regulation of World Trade in Textiles: A Lessons for Practice: A Contribution to Theory* (Boston: Kluwer Academic Publishers, 1989).

Castel, J.G., de Mestral, A.L.C. & Graham, W.C. *The Canadian Law and Practice of International Trade* (Toronto: Emond Montgomery Publications Limited, 1991).

Cline, William R. *The Future of World Trade in Textiles and Apparel,* 2nd ed. (Washington: Institute for International Economics, 1990).

Clubb, Bruce E. *United States Foreign Trade Law* (Boston: Little, Brown & Company, 1991).

Committee on Ways and Means of the U.S. House of Representatives, *Written Comments on H.R. 1233: The CBER Expansion Act of 1989* (Washington, 1989).

Curtis, Thomas B. & Vastine, John Robert. *The Kennedy Round and the Future of American Trade* (New York: Praeger Publishers, 1971)

Dam, Kenneth W. *The GATT: Law and International Economic Organization* (Chicago: The University of Chicago Press, 1970).

Destler, I. M.- Fukui, Haruhiro & Sato, Hideo. *The Textile Wrangle: Conflict in Japanese-American relations 1969-1971* (London: Cornell University Press, 1979).

Dunkel, Arthur et al. *Trade Policies for a Better Future. The 'Leutwiler Report', the GATT and the Uruguay Round* (Dordrecht: Martinus Nijhoff Publishers, 1987).

Fatemi, Khosrow (ed.). *The Maquiladora Industry: Economic Solution of Problem?* (New York: Praeguer, 1990).

Fernandez, Guillermo. *La Industria Textil y de Confeccion de Costa Rica* (San Jose: Camara Textil y de Confeccion, 1992).

Finger, J. Micheal & Olechowski, Andrzej (eds.). *The Uruguay Round: A Handbook on the Multilateral Trade Negotiations* (Washington: World Bank, 1987).

Glich, Leslie Alan. *Guide to United States Customs and Trade Laws* (Deventher: Kluwer L. & Taxation Publishers, 1991).

Globerman, Steven & Walker, Michael (eds.). *Assessing NAFTA: A Trinational Analysis* (vancouver: The Fraser Institute, 1993).

Grabitz, Eberhard & Von Bogdandy, Armin (eds.). *U.S. Trade Barriers: A Legal Analysis* (New York: Oceana Publications Inc, 1991).

Grimwade, Nigel. *International Trade: New Patterns of Trade, Production and Investment* (London: Routledge, 1989).

Hansen, Roger D. *Tariffs, Quotas and Trade: The Politics of Protectionism* (California: The Institute for Contemporary Studies, 1979).

Hilf, Meinhord; Jacobs, Francis G. & Petersmann, Ernst-Ulrich (eds.) *The European Community and GATT*, Vol. 4 (Deventer: Kluwer, 1986).

Hoda, Anwarul. *Developing Countries in the International Trading System* (New Delhi: Allied Publishers, 1987).

Hosten-Craig, Jennifer. *The Effect of a North American Free Trade Agreement on the Commonwealth Caribbean* (Ontario: The Edwin Mellen Press, 1992).

Hudec, Robert. *The GATT Legal System and World Trade Diplomacy* (New York: Praeger Publishers, 1975).

Jackson, John H. *Legal Problems of International Economic Relations* (Minnesota: West Publishing Co., 1977).

Jackson, John H. *Restructuring the GATT System* (New York: Royal Institute of International Affairs, 1990.)

Jackson, John H. *The World Trading System* (Massachusetts: The Massachusetts Institute of Technology, 1989).

Jackson, John H. *World Trade and the Law of GATT* (Indeanapolis: the Bobbs-Merrill Company, Inc., 1969).

Johnston, Charles R. *Law and Practice of United States Regulation of International Trade* (New York: Oceana Publications, 1987).

Loeb, Hamilton & Owen, Michael (eds.) *North American Free Trade Agreement: Summary and Analysis* (Washington: Paul, Hastings, Janofsky & Walker, 1993).

Long, Olivier. *Law and Its Limitations in the GATT Multilateral Trade System* (Dordrecht: Martinus Nijhoff Publishers, 1985).

Masaaki, Kotabe. *Global Sourcing Strategy: R & D, Manufacturing and Marketing Interfaces* (New York: Quorum Books, 1992).

McGaughey, William. *A U.S.-Mexico-Canada Free Trade Agreement* (Minneapolis: Thistlerose Publications, 1992).

Muhammad, V. A. *The Legal Framework of World Trade* (New York: Praeger, 1958).

Nau, Henry R. *Domestic Trade Politics and the Uruguay Round* (New York: Columbia University Press, 1989).

Oxley, Alan. *The Challenge of Free Trade* (New York: St. Martin's Press, 1990).

Patton, Boggs & Blow. *Memorandum: The Impact of Omnibus Trade Legislation on the Caribbean Basin Initiative*, 13 August 1987.

Petersmann, Ernst-Ulrich & Hilf, Meinhard (eds.) *The New GATT Round of Multilateral Trade Negotiations*, 2d. ed. (Deventer: Kluwer, 1991).

Raffaelli, Marcelo. "Some Considerations on the Multi-Fibre Arrangement: Past, Present and Future" in Carl B. Hamilton, ed., *Textile Trade and the Developing Countries: Eliminating the Multi-Fibre Arrangement in the 1990s* (Washington: The World Bank, 1990).

Raghavan, Chakravarthi. *Recolonization: GATT, The Uruguay Round and the Thirld World* (London: Zed Book Ltd., 1990).

Ray, Edward John. *U.S. Protectionism and the World Debt Crisis* (New York: Quorlum Books, 1989).

Rodriguez, Ennio, et al. *Analisis de las Oportunidades Brindadas por la Iniciativa de la Cuenca del Caribe* (Presentado a la Consideracion de la Secretaria de Integracion Centroamericana 1989).

Rom, Michael. *The Role of Tariff Quotas in Commercial Policy* (London: The Macmilian Press Ltd, 1979).

Rossides, Eugene T. *U.S. Customs Tariffs and Trade* (Washington: Bureau of National Affairs, 1977).

Ryan, K.W. *International Trade Law* (Melbourne: G.W. Green Printers, 1976).

Sampson, Gary & Takacs, Wendy. "Returning Textile Trade to the Normal Worlings of GATT: a Proposal for Reform" in Carl B. Hamilton, ed., *Textile Trade and the Developing Countries: Eliminating the Multi-Fibre Arrangement in the 1990s* (Washington: The World Bank, 1990).

Schott, Jeffrey J., ed. *Completing the Uruguay Round: A Results-Oriented Approach to the GATT Trade Negotiations* (Washington: Institute for International Economics, 1990).

Schott, Jeffrey J. *The Global Trade Negotiations: What Can Be Achieved?* (Washington: Institute for International Economics, 1990).

Serko, David. *Import Practice, Customs and International Trade Law* (New York: Practising Law Institute, 1991).

Stern, Robert M. (ed). *U.S. Trade Policies in a Changing World Economy* (Massachusettes: Massachusettes Institute of Technology, 1987).

Singer, H.W., Hatti, N. & Tandon, Rameshwr (eds.) *Trade Liberalization in the 1990s*, vol. 8 (New Delhi: Indus Publishing Company, 1990) 725.

Sklair, Leslie. *Assembling for Development: The Maquila Industry in Mexico and the United States* (Boston: Unwin Hynan Inc., 1989).

Smith, Murray G. *Canada's Stake in the Uruguay Round and the GATT System* (Ottawa: The Institute Economics Program, 1988).

Smith, Murray G. (ed.). *Future of the Global Trading System*, Part One (Halifax: The Institute for Research on Public Policy, 1990).

Steele, Peter. *The Caribbean Clothing Industry* (London: The Economist Intelligence Unit, 1988).

Stone, Frank. *Canada, The GATT and the International Trade System*, (Montreal: The Institute for Research and Public Policy, 1984).

Stowell, Alan (ed). *U.S. International Trade Laws* (Washington: Bureau of National Affairs, 1989).

Tuker, Stuart K. "Desentrabamiento del Comercio: Evaluacion de la Iniciative de la Cuenca del Caribe, Recuperacion y Desarrollo de Centroamerica" en *Ensayos del Grupo Especial de Estudios de la Comision Internacional para la Recuperacion y el Desarrollo de Centroamerica* (San Jose: Trejos Hermanos Sucs., 1989).

Tussie, Diana. *The Less Developed Countries and the World Trading System: A Challenge to the GATT* (NEW York: St. Martin's Press, Inc., 1987).

Waverman, Leonard (ed.) *Negotiating and Implementing a NAFTA* (Vancouver: Fraser Institute, 1992).

Winham, Gilber R. *The Evolution of International Trade Agreements* (Toronto: University of Toronto Press Inc., 1992).

Wolf, Martin. "How to Cut the Textile Knot: Alternative Paths to Liberalization of the MFA" in Carl B. Hamilton, ed., *Textile Trade and the Developing Countries: Eliminating the Multi-Fibre Arrangement in the 1990s* (Washington: The World Bank, 1990) at 223.

Yoffie, David B. *Power and Protectionism: Strategies of the New Industrializing Countries* (New York: Columbia University Press, 1983).

Zheng, Henry R. *Legal Structure of International Textile Trade* (New York: Quorum Books, 1988).

ARTICLES

Bannon, Pamela A. "Trade Relief: A Benefit or Burden for the Textile and Apparel Industries?" (1987) New York University Journal of International Law and Politics 701 at 706

Baker, Mark B. & Toro-Monserrate, Jaime E. "CBI v. Caricom: The Interplay between Two International Law Instruments" (1986) 11 North Caroline Journal of International Law and Commercial Regulation 1.

Beard, Peter. "Offshore Financial Centers in Caribbean Basin Secrecy Jurisdictions: Current Trends and Developments in United States Anti-Tax Haven Policy" (1986) 12 Syracuse Journal of International Law and Commerce 520.

Benedeck, Wolfgang. "The Caribbean Basin Economic Recovery Act: A New Preference in GATT?" (1986) 20 Journal of World Trade Law 29.

Cable, Vicent. "Textiles and Clothing in a New Round of Trade Negotiations" (1987) 1:4 The World Bank Economic Review 304.

Chemtob, Stuart. Book Review of *Liberal Protectionism: The International Politics of Organized Textile Trade* (1985) 19:3 George Washington Journal of International Law and Economis 915.

Clark, D. P.- Sawyer, W.C. & Sprinkle R. L. "Determinants of Industry Participation Under Offshore Assembly Provisions in the United States Tariff Code" (1989) 23:5 Journal of World Trade 123.

Clasen, Thomas F. "The Caribbean Basin Economic Recovery Act and Its Implications for Foreign Private Investment" (1984) 16 New York University Journal of International Law and Politics 715.

Clement, Norris C. "An Overview of the Maquiladora Industry" (1987) 18 California Western International Law Journal 55

Das, Bhagirath L. "The GATT Multi-Fibre Arrangement" (1983) 17 Journal of World Trade Law 99.

Das, Dilip K. "Dismantling the Multifibre Arrangement" (1989) 19 Journal of World Trade Law 67.

De Lima-Campos, Alusio. "Comments from a Brazilian Point of View on Trade in Textile Products and on the MFA" 19 Law and Policy in International Business 219.

Flax-Davidson, Ron H. "Tax-Exempt Investment fo the Caribbean Basin Initiative Region" (1991) 25 International Lawyer 1021.

Foote, Francis W. "The Caribbean Basin Initiative: Development, Implementation and Application of the Rules of Origin and Related Aspects of Duty-Free Treatment" (1985) 19 George Washington Journal of International Law and Economics 245.

Freud, Nicholas & Scown, Michael J. "Temporary and Proposed Regulations Detail Requirements for Qualified Investments in the Caribbean Basin Countries" 19 Tax Management International Journal 119.

Friman, Richard. "Rocks, Hard Places, and the New Protectionism: 3Textile Trade Policy Choices in the United States and Japan" (1988) 42 International Organization 689.

Giesse, Craig R. & Lewin, Martin J. "The Multifiber Arrangement: 'Temporary' Protection" (1987) 19 Law and Policy in International Business 51.

Gonzalez-Karg, Antonio. "On the Future of Trade in North America" (1991) 22 Revue Generale de droit 227.

Gosselin, Pierre. Remarks (1986) Proceedings American Society of International Law 292.

Graves, Harmon S. "Mexico's Maquiladora Program: Issues for Colorado Manufacturers" (1992) 21:8 Colorado Lawyer 1623.

Hamilton, Carl B. "Follies of Policies for Textile Imports in Western Europe" (1985) 8 The World Economy 235.

Hamilton, Carl B. "Sampson Proposal: A Reply to Aubrey Silberston (1988) 11:2 The World Economy 301.

Hufbauer, Gary C. & Schott, Jeffrey. "Options for A Hemispheric Trade Order" 22:2-3 University of Miami Inter-American Law Review 261.

Jacobs, Brenda A. "Renewal and Expansion of the Multifiber Arrangement" (1987) 19 Law and Policy in International Business 7.

Jenkins, Ed. "The Multifiber Arrangement: Its Shortcomings and Remedies" (1987) 19 Law and Policy in International Business 205.

Jones, Kent. "Voluntary Export Restraint: Political Economy, History and the Role of the GATT" (1989) 23:3 Journal of World Trade Law 125.

Khanna, Ram. "Market Sharing under Multifiber Arrangement: Consequences of No-Tariff Barriers in the Textiles Trade" (1990) 24:1 Journal of World Trade71.

Kassinger, Theodore W. Remarks (1986) Proceedings American Society International Law 287.

King, Peter. "Textiles and Apparel Trade in the 1990s: A Perspective from Jamaica" 16 (1992) The Fletcher Forum of World Affairs 27.

Koop, Barry. Remarks (1986) Proceedings American Society of International Law 290.

Landaw, Jared L. "Textile Trade Liberalization: The Need for a Strategic Change in Free Trade Arguments" (1989) Columbia Business Law Review 205.

Lazarus, David M. "Treading Water in the Caribbean: Recent Developments in United States Textile and Apparel Policy" (1992) 13:1 University of Pennsylvania Journal of International Business Law 141.

Lunger, Analisa G. "The Caribbean Basin Initiative and the I.R.C. Section 936 Investment Program: A United States Answer to the Troubled Caribbean Region" (1987) 9 University of Pennsylvania Journal of International Business Law 741.

Mandel, Irving. "U.S. Customs Defeated in 807 Ruling" (1981) 94 American Import-Export Bulletin 32.

Malloy, John Cyril. "The Caribbean Basin Initiative: A Proposal to Attract Corporate Investment and Technological Infusion Via an Inter-American System of Cooperative Protection for Intellectual Property" (1991) 23:1 University of Miami Inter-American Law Review 175.

Nehmer, Stanley. "The Multifiber Arrangement: Failure of an International Effort" (1987) 19 Law and Policy in International Business 235.

Pendfold, John. "The Caribbean Basin Initiative: A Welcome Remedy to the Ironic Turmoil" (1982) 12 California Western International Law Journal 466.

Pinon, Gema M. & Sanchez, Raul Javier. "CBI II: Will United States Protectionist Tendencies Yield to Economic Development in the Caribbean Basin?" (1989) 20:3 University of Miami Inter-American Law Review 615.

Raleigh, Thomas L. "The US Caribbean Basin Initiative" (1987) 15 International Business Lawyer 136.

Rolfe, Robert J. "Combining the Benefits of Possessions Corporations with the Caribbean Basin Initiative" (1990) 16 The International Tax Journal 5.

Sahai, P.S. "Textile Trade and MFA IV: A Comment" (1987) 19 Law and Policy in International Business" 223.

Sampson, Gary. "Pseudo-economics of the MFA: a Proposal for Reform" (1987) 10:4 The World Economy 455.

Sanders, Gray. "Maquiladoras and the Yucatan" (1990) 5:3 Florida International Law Journal 523.

Sawyer, W. Charles & Sprinkle, Richard L. "Caribbean Basin Economic Recovery Act: Export Expansion Effects" (1984) 18:5 Journal of World Trade Law 429.

Schechter, Cheryl. "The Maquiladora Industry and Free Trade" Mexico Trade Letter, Articles from Canada: Gottlieb & Pearson (12 March 1992).

Schechter, Cheryl & Brill, David. "Maquiladoras: Will the Program Continue?" (1992) 23:3 St. Mary's Law Journal 697.

Shostak, Richard. "The Evolution of Item 807.00 of the Tariff Schedules of the United States and the Resulting Revolution of the Customs Laws" (1980) 12 University of West Los Angeles Law Review 47.

Sierra, Ralph. "Funding Caribbean Basin Initiative Activities with Section 936 Funds" (1992) 18 The International Tax Journal 27.

Silberston, Aubrey. "Impracticalities of the Sampson Proposal for Phasing Out the MFA" (1988) 11:2 The World Economy 301.

Stempler, Robert Harlan. "Costa Rica: A Nirvana for Export Manufacturers?" (1991) 4 The Transnational Lawyer 201.

Stepp, David. "The 1984 'Country of Origin' Regulations for Textiles Imports: Illegal Administrative Action Under Domestic and International Law?" (1984) 14 Georgia Journal of International and Comparative Law 573.

Stewart, Michael T. "The Country of Origin Regulations: A Case Study in the Violation of the Multifiber Arrangement" (1985) 5:2 Journal of Law and Commerce 535.

Tang, Xiobing. "Textiles and the Uruguay Round of Multilateral Trade Negotiations" (1989) 23 Journal of World Trade 51.

Turro, John. "Congress Asks Why Section 936 Funds are not Reaching the Caribbean" (1990) 47 Tax Notes 133.

Tuttle, James C. "Multifiber Arrangement Phase-Out Prospects" (1987) 19 Law and Policy in International Business 249.

Valdez, Abelardo L. "Expanding the Concept of Coproduction Beyond the Maquiladora: Toward a More Effective Partnership between the United States and Mexico, and the Caribbean Basin Countries" (1988) 22:2 International Lawyer 393.

Walkins, Al. "The Texas-Mexico Twin Plants System: Industry and Item 807.00 of the United States Tariff Schedule" (1985) 16:4 Texas Tech Law Review 963.

Wolf, Martin. "How to Unravel the Multi-Fibre Arrangement" (1985) 8:3 The World Economy 235.

Zagaris, Bruce. "A Caribbean Perspective of the Caribbean Basin Initiative" (1984) 18 International Lawyer 563.

Zagaris Bruce. "Financing Participation in Caribbean Basin Investments and Trade" (1985) 17:1 Inter-American Law Review 122.

Zheng, Henry R. "The Fourth Multifibre Arrangement and the New Legal Regime for International Trade in Textiles" (1987) 25 Columbia Journal of International Law and Politics 301.

Zheng, Henry R. "The Legal Structure of the International Textiles Trade and the July 1986 MFA Renewal Negotiations" (1986) 4 B. U. Int'l L. J. 285.

LAWS AND OFFICIAL DOCUMENTS

LAWS

Caribbean Basin Economic Recovery Act, Pub. L. 98-67, s. 141 (1983) (codified as amended at 42 U.S.C. ss. 2701-2706 (1993), and in scattered sections of 19, 26 and 33 U.S.C.).

Customs Simplification Act of 1954, Pub. L. No. 786, 83d Cong., 2d Sess. (1954).

Reglamento de Exportacion de Productos de la Industria Textile y Confeccion de Ropa del Consejo de Cuotas, Decreto Ejecutivo No. 19481-CE, Gaceta No. 56 de 22 de marzo de 1990.

OFFICIAL DOCUMENTS

Addres of President Reagan Before the Permanent Council of the Organization of American States, (24 February 1982) 18 Weekly Compilation of Presidential Documents 217.

Bureau of National Affairs, International Trade Reporter No. 17 "Imports of Caribbean Garments Soar in Wake of CBI, Further Access Sought" (27 April 1988) 625.

Bureau of National Affairs, International Trade Reporter No. 14 "Legislation to Expand Trade Preferences for CBI Beneficiaries Introduced in the House" (12 August 1987) 1006.

"Mexico, Central American Countries Plan Free Trade Agreement to Be Reached by 1996" (1991) 8:3 International Trade Report 87.

Ministerio de Comercio Esterior. *Caribbean Basin Initiative: Exporter's Guide 1991* (San Jose: Comex, 1991).

Ministerio de Comercio Exterior, *Costa Rica: Total Exports 1987-1991* (San Jose: Ministerio de Comercio Exterior, 1991).

Ministerio de Comercio Exterior. *Estadisticas de las Exportaciones e Importaciones de Productos Textiles Realizadas por Costa Rica* (San Jose: CENPRO, 1990).

North American Free Trade Agreement: An Overview and Description (Ottawa: Government of Canada, 1992).

The NAFTA Manual (Ottawa: Government of Canada, 1992).

U.S. Department of Commerce, International Trade Administration, *Caribbean Basin Initiative: 1989 Guidebook.*

U.S. Department of Commerce, International Trade Administration, *Caribbean Basin Initiative: 1991 Guidebook.*

U.S. Department of Commerce, International Trade Administration, *Trade Balance Report*, Office of Textiles and Apparel, Data through November 1992.

U.S. Department of Commerce, *Latin America/ Caribbean Business Bulletin*, Vol. III No. 3, 1993.

U.S. Customs Service, *Foreign Assembly of U.S. Components: A Guide for Qualifying Imported Articles for the Partial Duty Exemption Under HTSUS subheading 9802.00.80* (Washington, 1992).

United Nations Conference on Trade and Development, *Uruguay Round: Further Papers on Selected Issues* (New York: United Nations, 1990).

United Nations, Department of Economic and Social Development, *Monthly Bulletin of Statistics*, Vol. XLVII No.4, April 1993.

U.S. International Trade Commission, *Annual Report on the Impact of the Caribbean Basin Economic Recovery Act on U.S. Industries and Consumers,* Second Report (Washington, 1987).

U.S. International Trade Commission, *Annual Report on the Impact of the Caribbean Basin Economic Recovery Act on U.S. Industries and Consumers,* Third Report (Washington, 1988).

U.S. International Trade Commission, *Annual Report on the Impact of the Caribbean Basin Economic Recovery Act on U.S. Industries and Consumers,* Fourth Report (Washington, 1989).

U.S. International Trade Commission, *Annual Report on the Impact of the Caribbean Basin Economic Recovery Act on U.S. Industries and Consumers,* Fifth Report (Washington, 1990).

U.S. International Trade Commission, *Annual Report on the Impact of the Caribbean Basin Economic Recovery Act on U.S. Industries and Consumers,* Sixth Report (Washington, 1991).

U.S. International Trade Commission, *Annual Report on the Impact of the Caribbean Basin Economic Recovery Act on U.S. Industries and Consumers,* Seventh Report (Washington, 1992).

U.S. International Trade Commission, *Potential Effects of a North American Free Trade Agreement on Apparel Investment in CBERA Countries* (Washington, 1992).

U.S. International Trade Commission, *The Use and Economic Impact of TSUS Items 806.30 and 807.00, Report to the Subcommittee on Trade, Committee on Ways and Means,* U.S. House of Representatives (Washington, 1988).

U.S. International Trade Commission, *Production Sharing: U.S. Imports under Harmonized Tariff Schedule Subheadings 9802.00.60 and 9802.00.80*, 1985-1988 (Washington, 1989).

U.S. International Trade Commission, *Production Sharing: U.S. Imports under Harmonized Tariff Schedule Subheadings 9802.00.60 and 9802.00.80*, 1986-1989 (Washington, 1991).

U.S. International Trade Commission, *Production Sharing: U.S. Imports under Harmonized Tariff Schedule Subheadings 9802.00.60 and 9802.00.80*, 1988-1991 (Washington, 1992).

U.S. International Trade Commission, *U.S. Imports of Textiles and Apparel under the Multifiber Arrangement: Annual Report for 1991* (Washington, 1992).

INTERNATIONAL DOCUMENTS

Arrangement Regarding International Trade in Textiles, GATT Doc. TEX.NG/1, 30th sess., 21st supp. B.I.S.D. (1973-1974) 3.

Bilateral Textile Agreement Between the United States and Costa Rica, Washington: 20 March 1992.

Bilateral Textile Agreement Between the United States of America and the United Mexican States, Mazatlan: February 13, 1988.

Canada-United States Free Trade Agreement, 22 December 1987, Can. T.S. 1989 No.3, 27 I.L.M. 281 (1988).

General Agreement on Tariffs and Trade, Geneva (30 October 1947) B.I.S.D., Vol. IV (1969).

GATT C.P. Dec. (19 Nov 1960), 19th supp. B.I.S.D. (1960)

GATT, *Decisions Adopted at the Mid-Term Review of the Uruguay Round* (8 April 1989), reprinted in 28 I.L.M. 1203 (1989).

GATT, Committee on Textiles, *Report of the Textiles Committee meeting held on 31 July 1991 adopted on 8 October 1991*, GATT Doc. COM.TEX/69, 38th supp. B.I.S.D. (1992) 109.

GATT, *Draft Final Act Embodying the Results of the Uruguay Round of Multilateral Trade Negotiations* (Geneva: GATT, 1991).

International Labour Office, *Yearbook of Labour Statistics*, 51st issue, (Geneva, 1992).

Ministerial Declaration on the Uruguay Round, GATT Doc. L/1396 (20 September 1986) reprinted in (1986) 25 I.L.M 1623 at 1627.

North American Free Trade Agreement between Canada, Mexico and the United States, Minister of Supply and Services, Canada, 1992.

Short-Term Arrangement Regarding International Trade in Cotton Textiles, GATT C.P. (21 July 1961), 18 & 19th sess., 10th supp. B.I.S.D. (1962) 18.

Long-Term Arrangement Regarding International Trade in Cotton Textiles, GATT C.P. (9 February 1962), 20th sess., 11th Supp. B.I.S.D. (1963) 25.

Protocol Extending the Arrangement Regarding International Trade in Textiles, GATT (14 December 1977), 33rd sess., GATT Doc. L/4616, 24th suppl B.I.S.D. (1977) 5.

Protocol Extending the Arrangement Regarding International Trade in Textiles, GATT (22 December 1981), 37th sess., GATT Doc. L/5276, 28th supp. B.I.S.D. (1981) 3.

Protocol Extending the Arrangement Regarding International Trade in Textiles, GATT (31 July 1986), 42nd sess., GATT Doc. L/6030, 33rd supp. B.I.S.D. (1986) 7.

Protocol Maintaining in Force the Arrangement Regarding International Trade in Textiles, GATT (31 July 1991), 47th sess., GATT Doc. COM.TEX/69, 38th supp. B.I.S.D. (1992) 113.

Protocol Maintaining in Force the Arrangement Regarding International Trade in Textiles, (Geneva: GATT, 1992).

Report of the Textiles Committee, GATT (22 March 1988), 44th sess., GATT Doc. COM.TEX/55, 35th supp. B.I.S.D (1989) 395.

Report of the Textiles Committee, GATT (7 November 1989), 45th sess., GATT Doc. COM.TEX/62, 36th supp. B.I.S.D. (1990) 464.

Report of the Textiles Committee, GATT (6 February 1990), 47th sess., GATT Doc. COM.TEX/67, 38th supp. B.I.S.D. (1992) 107.

INTERVIEWS

Interview with Francisco Chacon, Ministerio de Comercio Exterior (9 December 1992) San Jose.

Interview with Luis Guillermo Elizondo, Consejo Nacional de Administracion de Cuotas Textiles y Ropa Confeccionada (18 December 1992) San Jose.

Interview with Louis Gionet, Ministry of External Affairs: International Trade (31 May 1993) Ottawa.

Letter of H.J. Rosenbaum, Senior Policy Advisor, Office of the United States Trade Representative (27 January 1993).

APPENDICES

APPENDIX A

U.S. Trade with the Caribbean Basin countries, 1984-91

Year	U.S. exports[1]	Share of U.S. exports to the world	U.S. imports[2]	Share of U.S. imports from the world	U.S trade balance
	Million dollars	Percent	Million dollars	Percent	Million dollars
1984	6,300 2	2.9	8,896.5	2.8	-2,596.3
1985	5,996 4	2.8	6,849.9	2.0	-853.6
1986	6,292 2	2.9	6,186.8	1.7	105 4
1987	6,940.6	2.8	6,178.1	1.5	762 6
1988	7,666 3	2 5	6,172.3	1.4	1,494 0
1989	9,184.4	2.6	7,020.6	1.5	2,163.8
1990	9,698.2	2.6	7,601.3	1.5	2,097.0
1991	10,170.1	2.5	8,304.3	1.7	1,865.8

[1] Domestic exports, f.a.s. basis.

[2] Imports for consumption, customs value.

Source: Compiled from official statistics of the U.S. Department of Commerce.

APPENDIX B

U.S. imports for consumption from CBERA countries of goods not eligible for duty-free treatment under CBERA, 1987-91

(In thousands of dollars, customs value)

Product category[1]	*1987*	*1988*	*1989*	*1990*	*1991*
Textiles and apparel	1,148,432	1,488,812	1,753,055	2,006,348	2,558,240
Petroleum and petroleum products	1,376,662	1,058,524	1,044,432	1,340,317	1,399,607
Footwear	30,365	39,255	45,215	35,806	38,700
Certain handbags, luggage, and flat goods	20,215	20,410	16,669	18,264	26,651
Certain leather apparel	2,348	3,386	11,279	15,194	14,064
Work gloves	3,996	3,906	5,452	4,360	4,415
Tuna	117	14	2	111	0
Total	2,582,135	2,614,307	2,876,103	3,420,400	4,041,677

[1] Product categories are defined by HTS subheading in table B-3.

Note.—Figures for 1987-88 under the HTS classification system (see table B-3) are estimated.

Note —Because of rounding, figures may not add to totals shown.

Source: Compiled from official statistics of the U.S. Department of Commerce.

APPENDIX C

U.S. imports for consumption from countries designated under CBERA, by duty treatment, 1989-91

Item	*1989*	*1990*	*1991*
	Value (1,000 dollars, customs value)		
Total imports	6,637,440	7,525,208	8,229,366
Dutiable value[1]	2,101,839	2,573,813	2,869,880
HTS 9802.00.60 and 9802.00.80	504,882	520,107	691,052
HTS 9802.00.80.10	106,055	112,770	146,307
HTS 9802.00.80.50	398,241	406,235	544,695
Other	1,596,957	2,053,706	2,178,828
Duty-free value[2]	4,535,601	4,951,395	5,359,486
MFN[3]	1,854,400	1,968,007	1,912,824
CBERA[4]	905,762	1,020,717	1,120,697
GSP[4]	415,859	472,303	410,439
HTS 9802.00.60 and 9802.00.80	1,089,694	1,153,325	1,418,075
HTS 9802.00.80.10	286,437	318,108	410,905
HTS 9802.00.80.50	785,766	815,542	1,007,115
Other duty free[5]	269,886	337,04[illegible]	497,451
	Percent of total		
Total imports	100.0	100.0	100.0
Dutiable value[1]	31.7	34.2	34 9
HTS 9802.00.60 and 9802.00.80	7.6	6.9	8 4
HTS 9802.00.80.10	1.6	1.5	1 8
HTS 9802.00.80.50	6.0	5.4	6 6
Other	24.1	27.3	26 5
Duty-free value[2]	68.3	65.8	65 1
MFN[3]	27.9	26.2	23 2
CBERA[4]	13.6	13.6	13 6
GSP[4]	6.3	6.3	5 0
HTS 9802.00.60 and 9802.00.80	16.4	15.3	17 2
HTS 9802.00.80.10	4.3	4.2	5 0
HTS 9802.00.80.50	11.8	10.8	12 2
Other duty free[5]	4.1	4.5	6 0

[1] Reported dutiable value has been reduced by the duty-free value of imports recorded under HTS subheadings 9802.00.60 and 9802.00.80 and increased by the value of ineligible items that were reported as entering under the CBERA and GSP programs.

[2] The total duty-free value is calculated as total imports less dutiable value as defined above.

[3] Figures for MFN duty-free imports represent the value of imports which have a col. 1-general duty rate of zero

[4] Values for CBERA and GSP duty-free imports have been reduced by the value of MFN duty-free imports and ineligible items that were misreported as entering under the programs.

[5] The value for other duty-free imports was calculated as a remainder and represents imports entering free of duty under special rate provisions.

Note.—Because of rounding, figures may not add to totals shown.

Source: Compiled from official statistics of the U.S. Department of Commerce.

APPENDIX D

Cost comparison of producing selected apparel products among the United States, the Caribbean Basin, and Hong Kong under subheading 9802.00.80, 1987

Country	Materials: Fabric	Materials: Total	Labor and overhead: Cutting	Labor and overhead: Assembly	Freight, duty and related costs	Total costs
			Women's blouses[1]			
Domestic	$2.91	$3.33	$0.29	$4 75	$0 04	$8 41
Caribbean	2 90	13 33	.29	1 66	77	6 05
Hong Kong	2.10	12 53	09	2 20	1 41	6 23
			Men's sport coats[2]			
Domestic	$9.00	$14.90	$3.84	$15 66	$0 08	$34 48
Caribbean	9 00	14.90	3.84	5 44	3 49	27 67
Hong Kong	7 20	11.63	1 26	7 24	8 12	28 25
			Brassieres[3]			
Domestic	$0.55	$2.19	$0.18	$1 79	$0 01	$4 17
Caribbean	55	2.19	.18	73	45	3 55
Hong Kong	.43	1.65	.07	83	87	3 42
			Men's casual slacks[4]			
Domestic	$3.03	$3.59	$0.16	$4.46	$0.02	$8 23
Caribbean	3 03	3.59	.16	1.50	6.57	5 88
Hong Kong	2.51	2.93	.06	2.08	1 26	6 33

Long-sleeve blouses, not ornamented, of 55 percent cotton and 45 percent polyester.

[2] Men's sport coats, not ornamented, of 100 percent polyester.

[3] Manmade-fiber underwire brassieres. The 9802.00.80 cost assumes finishing in the United States The Hong Kong cost is for a finished package.

[4] Men's casual slacks, not ornamented, of 100 percent cotton canvas fabric.

Source: Compiled by the U.S International Trade Commission, Textiles Division, from industry sources.

APPENDIX E

Textiles, apparel, and footwear: Duty-free value of U.S. imports for consumption under HTS subheading 9802.00.80, by principal sources, 1986-8[illegible]

Source	1986	1987	1988	1989	Change in value of duty-free content, 1989 from 1986	Share of total duty free value 1986	Share of total duty free value 1989
	Million dollars				Percent	Percent	
Mexico	363	380	406	460	27	40	30
Dominican Republic	190	234	318	390	105	21	26
Costa Rica	84	92	131	172	104	9	11
Haiti	78	97	103	116	48	9	8
Jamaica	49	84	96	115	135	5	8
Colombia	26	30	50	57	122	3	4
Honduras	20	27	39	50	147	2	3
Guatemala	9	20	30	42	366	1	3
El Salvador	6	13	17	21	226	1	1
Philippines	17	15	17	15	-6	2	1
All others	64	73	104	73	15	7	5
Total	906	1,065	1,312	1,511	67	100	100

Notes —Table 22 corresponds to table 6-3 of the Full Report. Because of rounding, figures may not add to the totals shown

Source Compiled by the U S International Trade Commission from official statistics of the U S Department of Commerce

APPENDIX F

APPENDIX F(1)

Textiles, apparel, and footwear: Duty-free value of U.S. imports for consumption under HTS heading 9802.00.80, by principal sources, 1988-91

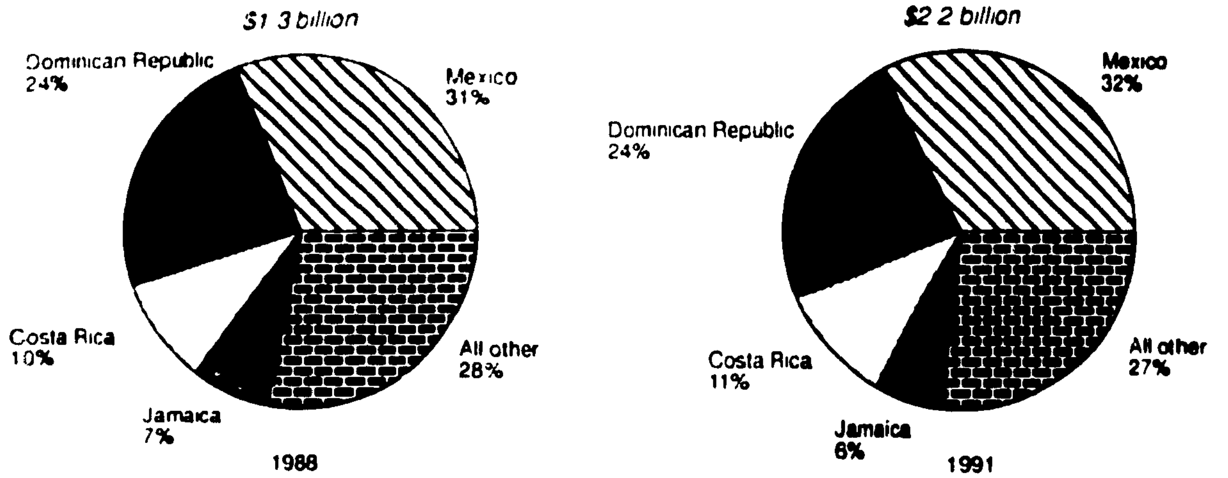
Source	1988	1989	1990	1991	Change in value of duty-free content, 1991 from 1988	Share of total duty-free value 1988	Share of total duty-free value 1991
	Million dollars				Percent	Percent	
Mexico	406	460	594	725	79	31	32
Dominican Republic	318	390	407	547	72	24	24
Costa Rica	131	172	205	254	94	10	11
Jamaica	96	115	119	131	36	7	6
Guatemala	30	42	60	117	290	2	5
Honduras	40	50	67	107	168	3	5
Haiti	103	116	110	101	-2	8	5
Colombia	50	57	63	82	64	4	4
El Salvador	17	20	25	44	159	1	2
Korea	27	9	26	23	-15	2	1
All others	94	80	87	106	13	7	5
Total	1,312	1,511	1,761	2,236	70	100	100

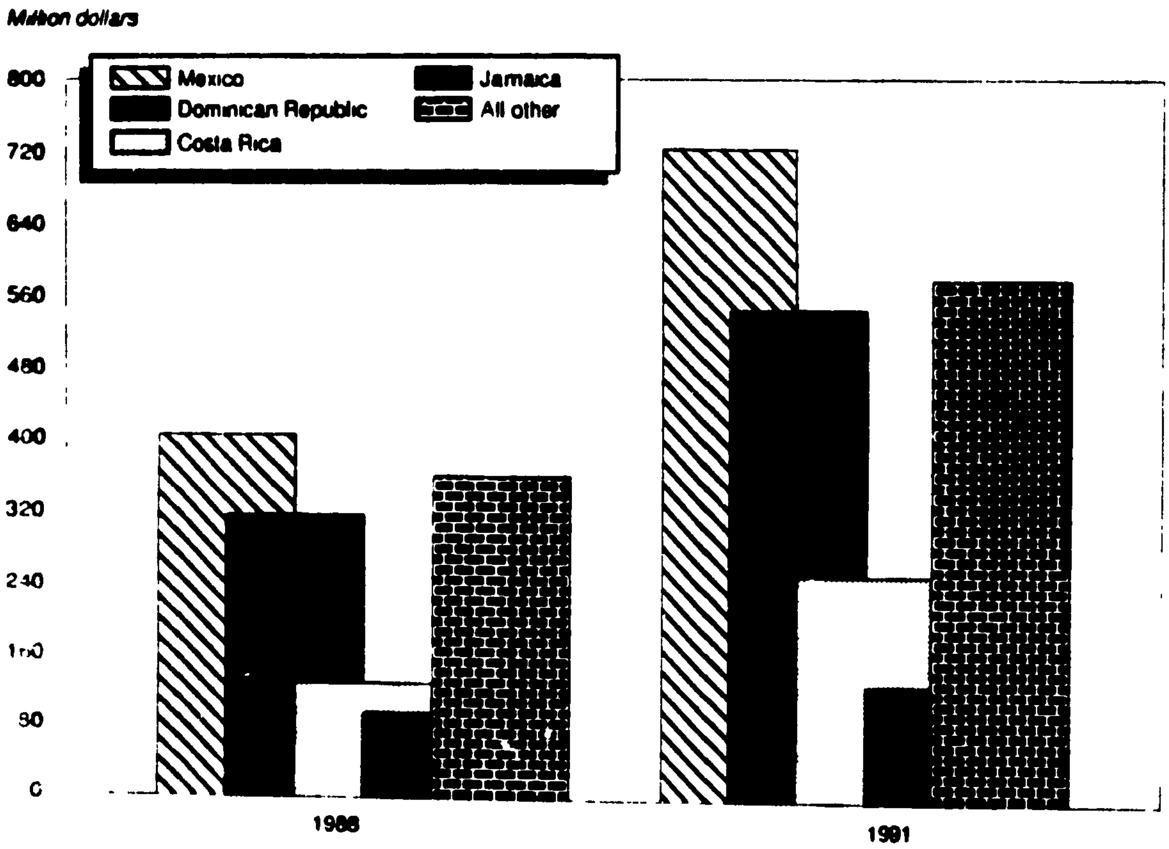
Note —Because of rounding, figures may not add to the totals shown.

Source Compiled by the U S International Trade Commission from official statistics of the U.S Department of Commerce.

APPENDIX F(2)

Textiles, apparel, and footwear: Value of U.S.-made components assembled in imports under heading 9802.00.80, by leading countries of assembly, 1988 and 1991





Source Based on official statistics of the U S Department of Commerce.

APPENDIX G

INVESTMENT POLICIES

	Costa Rica	*Dominican Republic*	*Guatemala*	*Honduras*	*Jamaica*	*Mexico*
INCOME TAX POLICY	• 100% exemption first 12 years, 50% next 6 years in designated areas of FTZs	• 100% exemption 15-20 years in FTZs	• 100% exemption for 12 years in FTZs • 100% exemption for 10 years for revenue obtained from goods exported outside Cen. America	• 100% exemption for perpetuity in FTZs[2]	• 100% exemption for perpetuity in FTZs	• Minimal tax paid in maquilas[1]
IMPORTS OF MACHINERY, EQUIPMENT AND INPUTS FOR PRODUCTION	• Duty-free in FTZs and under Temporary Admission System • Duty exemption proportional to export sales in the Export Contract Syst.	• Duty-free in FTZs	• Duty-free	• Duty-free in FTZs	• Duty-free in FTZs	• Duty-free in the maquiladoras
PROFIT REMITTANCES	• Unrestricted in FTZs	• Unrestricted in FTZs	• Unrestricted in FTZs	• Unrestricted in FTZs	• Unrestricted in FTZs	• Unrestricted
CAPITAL REPATRIATION	• No controls in FTZs	• No controls in FTZs	• No controls	• No controls in FTZs	• With prior approval, 100% permitted up to original investment without Central Bank intervention	• No controls
EXCHANGE RATE POLICIES	• Unrestricted currency conversion in FTZs	• Unrestricted currency conversion in FTZs	• Unrestricted currency conversion	• Unrestricted currency conversion in FTZs	• Unrestricted currency conversion	• Government requires conversions in the maquiladora operations, but at market rate
FINANCING ARRANGEMENTS	• Eligible for 936 funds[3]	• Eligible for 936 funds • FTZ operators eligible for preferential interest rates on Central Bank loans	• Availability of government-backed financing at preferential rates for certain projects	• Eligible for 936 funds	• Eligible for 936 funds	—
CUSTOMS PROCEDURES	• Expedited on-site in FTZs	• Expedited on-site in FTZs	• Expedited on-site in FTZs	• Expedited on-site in FTZs	• Expedited on-site in FTZs	• Government assistance in customs clearance in maquilas
EMPLOYEE TRAINING PROGRAMS	• Government-sponsored training at the Costa Rican National Training Institute and Technological Institute	• Government-sponsored training offered through the Instituto Nacional de Formacion Técnico Professional	• Training provided through the Guatemalan NonTraditional Product Exporters Association	• Limited	• Government-sponsored training offered	• Government-sponsored training offered • Some maquila-sponsored training offered
TAX EXEMPTIONS AND OTHER POLICIES	• 100% exemption from sales, export, local, and consumer taxes in FTZs	• 100% exemption from import, export, business license, municipal and production taxes • Industrial Development Corporation may offer lease space at subsidized rents in FTZs	• 100% exemption from taxes and other charges applicable to raw materials necessary to produce electricity in FTZs • 100% exemption from VAT, legal paper tax, stamp tax, property tax (5 years) in FTZs • Government guarantees of reimbursement in cases of inconvertibility or expropriation	• 100% exemption from import, export, local, sales and excise taxes in FTZs	• 100% exemption from property, import and export taxes in FTZs	• Government assistance in complying with registration requirements • 100% refund of VAT in maquilas if goods are re-exported
SALES TO LOCAL MARKET	• With government authorization, 40% of local production permitted with payment of import duties	• 20% of local production permitted with payment of import duties if 25% or more local value added, *or* if product not elsewhere [illegible]	• With government authorization, 20% of production permitted with payment of import duties	• Currently none permitted	• Currently none permitted	• With government authorization and payment of VAT and import duties, the lesser of (1) up to 50 percent of the prior year's production or (2) value of the current year's [illegible]

ient o t duti	local dded, if product not elsewhere manufactured in DR	with payment of import dut				of (1) up to 50 percent of the pric ; prod or (2) value of the current year's operating expenses to date

FOOTNOTES

[1] Taxable revenues for maquilas are calculated from sales of maquila services, e.g. assembly, which includes Mexican labor and overhead. Therefore, even under Mexico's federal corporate income tax rate of 35 percent, the taxes paid to the Mexican authorities tend to be minimal.

[2] Outside of the FTZs and industrial parks, companies are taxed at varying rates and are subject to limitations on profit remittances and capital repatriation.

[3] Under Section 936 of the U.S. Internal Revenue Code, qualified investors can borrow tax-deferred funds belonging to U.S. subsidiaries operating in U.S. possessions such as Puerto Rico. In 1986, modifications to U.S. and Puerto Rican tax laws allowed such funds deposited with Puerto Rican banks to be made available as loans to eligible borrowers for qualified projects at below-market rates. Financing using 936 funds is only available for investments in the Caribbean countries which have signed a Tax Information Exchange Agreement with the United States.

Sources: Compiled by USITC staff based on information provided by the Costa Rican Investment and Development Agency, Dominican Republic Investment Promotion Council; Embassy of Jamaica, Embassy of Honduras; U.S. Department of Commerce: U.S. Department of State; U.S. Department of the Treasury; U.S. Agency for International Development; U.S. apparel company officials; U.S. and Mexican attorneys.

APPENDIX H

MAJOR FACTORS AFFECTING COMPETITIVENESS OF CBERA AND MEXICAN INDUSTRIES

This chapter examines the changes in the relative competitiveness of the apparel industries of the CBERA countries versus Mexico. Four factors influencing competitiveness are analyzed in this chapter--production costs of U.S. companies operating in Mexico and in CBERA countries, fabric availability, quota availability and quality control.

U.S. apparel companies with assembly operations in the CBERA countries and Mexico usually cite low labor and transportation costs as the primary determinants of the region's competitive position. Duty eliminations under the NAFTA will influence the costs associated with sourcing in this region. The effects of a NAFTA on non-cost factors appear to be of secondary importance in comparison with the direct effects of duty eliminations on costs in evaluating changes in the relative competitiveness of these industries. Major differences in quality control between countries are usually overcome by companies with well-established and uniformly-applied management techniques. Fabric availability has been judged to have a relatively minor effect on the relative competitiveness of most CBERA and Mexican producers. Quotas have not been a major factor in determining the relative competitiveness of Mexico compared with the CBERA countries. For three of the four product categories in which quota levels on imports from Mexico were filled in 1991, the size of the adjustments made in the quota levels during the year suggests that these quantitative restraints were not binding. Therefore, these non-cost factors are discussed only to the extent that they are affected by the NAFTA. Accordingly, changes brought about by duty eliminations in the relative costs of fabric, assembly, transportation and miscellaneous costs are examined as the primary determinants of the relative competitiveness of the CBERA countries compared with Mexico. As the data in this chapter indicate, the removal of duties on U.S. imports of Mexican-made apparel is expected to reduce the costs of production for Mexican producers and improve their competitive position relative to the CBERA producers of apparel.

PRIMACY OF PRODUCTION COST FACTORS

U.S. apparel industry executives familiar with competitive conditions in the CBERA countries and Mexico frequently point out that literally hundreds of factors must be taken into consideration in deciding upon the most appropriate location for apparel manufacturing in the region.[75] Ultimately, however, U.S. companies with production-sharing facilities in the CBERA region and Mexico identify production cost differences as the single most important factor in deciding upon the best place to produce apparel. The cost elements most often cited are--

[75] See, for example, the testimony of Michael Rothbaum, President and CEO of the Harwood Companies, USITC hearing of Mar. 17, 1992, p. 49 of official transcript.

1. Labor costs (including base wages and fringe benefits); and

2. Transportation costs to and from major U.S. ports.

Labor costs, according to most U.S. industry officials, are the leading source of production cost savings for firms assembling apparel in the CBERA countries and Mexico. Ten out of fourteen U.S. companies interviewed by ITC staff indicated that wages were a critical factor in their decision to produce in a CBERA country or Mexico.[76] Wage rates can differ substantially between countries, reflecting in part differences in labor productivity and quality of workmanship. Apparel industry wage rates in CBERA countries are reported to range between 58 cents and $1.10 per hour, while the wage rate in Mexico is generally higher.[77]

Evidence suggests, however, that U.S.-owned 807 operations generally offer more attractive wage packages in order to attract and retain a high-quality workforce.[78] Moreover, U.S. companies maintain that variation in labor productivity and quality control standards result primarily from differences in company training policies and management techniques, rather than differences in the quality of the local workforce.[79] Thus, while sharp differences in wages and productivity may exist between countries, the size of these gaps tends to be smaller for 807 operations.

The importance of labor costs in competitiveness comparisons relates, in large part, to the labor-intensive nature of the apparel-manufacturing process. Differences in technology rarely appear as a significant source of cost advantage or disadvantage for U.S. 807 firms operating in the CBERA countries and Mexico. Indeed, as new developments in sewing technology lead to new commercial applications, most U.S. firms are able to take advantage of them quickly, modernizing assembly facilities when necessary. The absence of differences in technological capacity among 807 firms highlights again the underlying importance of differences in labor costs.

Transportation cost data collected by USITC staff indicate that both southbound and northbound ocean freight rates are quite similar for the major CBERA countries. Mexico does appear to possess a distinct cost advantage in this area.[80] This is reflected in the noticeable differences between CBERA and Mexican freight cost components in the production cost sheets for the six products that follow in the next section of the report. Six of the fourteen U.S. apparel companies contacted by ITC staff noted that transportation costs

---

[76] Out of 21 U.S. apparel companies surveyed, 14 responded. Of these, 10 specifically cited labor costs.

[77] For a survey of wages across the region, see individual country profiles in Chapter II and "1991 8th Annual 807/CBI Comparative Cost Analysis," Bobbin, Nov. 1991, p. 45.

[78] Regional variation in wage rates within a country can also exist, especially in large, economically-diverse countries like Mexico.

[79] U.S. apparel company official, telephone interview with USITC staff, Apr. 10, 1992.

[80] Analysis of CIF and FOB unit value data for key apparel items suggests that, at an aggregate level, Mexican operations can cut transport costs by as much as two-thirds over leading CBERA competitors.

were an important reason influencing their decision to produce in the Caribbean and Central American region.

PRODUCTION COST COMPARISONS

For the six representative apparel products selected for detailed analysis, production cost comparisons have been made between CBERA and Mexican producers. Cost analysis is performed for both 807 and 807A transactions--i.e., for apparel assembled with U.S.-cut fabric parts. Fabric costs represented in the column of tables 9-14 labeled "U.S.-Cut Fabric" apply to fabrics woven or knit outside of the United States but cut in the United States (807). The column labeled "U.S.-Formed and Cut Fabric," on the other hand, reflects the cost of fabrics both manufactured and cut in the United States (807A).

Mexican producers, in the absence of NAFTA benefits, currently have a competitive cost advantage in only one of the six products--blue jeans. Production costs for a second item, knit golf shirts, are approximately the same in Mexico and the leading CBERA supplier country. For the remaining four products, however, Mexican costs are currently higher. In some cases, the Mexican cost disadvantage is large (e.g., just under 20 percent for a typical ladies'. coat). (See tables 9-14 below).

As the product-by-product analysis below indicates, duty reductions brought about by NAFTA will have a noticeable effect on total production costs across the board. At a minimum, elimination of duties on imported Mexican apparel will * * * total costs for a typical Mexican producer by * * *. For one product--the suit-type coat--duty removal results in a * * * in total cost for Mexican producers.

In addition to the Mexican cost advantage in blue jean production, which can be expected to widen under a NAFTA, the duty-elimination effect will push Mexican producers into a position of overall cost advantage vis-a-vis their principal Caribbean competitors in the production of knit shirts and polyester blouses. For t-shirt producers, removal of the duty will improve the position of Mexican producers in comparison with CBERA competitors. With regard to women's suit-type coats and brassieres--two products with high labor cost-to-total cost ratios--Mexico will remain at a cost disadvantage even after the elimination of the duties. For these two products, relatively high labor costs in Mexico compared to leading CBERA producers will mitigate the cost savings achieved through a NAFTA duty elimination.

The calculated cost for items assembled in CBERA countries is a composite figure, compiled by taking a trade-weighted average of production costs in the leading Caribbean Basin supplier countries for each product. In some cases, limitations on the availability of reliable cost data have dictated the selection of only one CBERA country to be used as the regional benchmark in comparisons with Mexico. For all products, certain costs (fabric, trim, U.S. freight component) are assumed to be identical for both Mexican and CBERA production-sharing transactions. This is a reasonable assumption given the ability of U.S. firms to source fabrics and other U.S. components at similar prices, regardless of the assembly site. The crucial differences in costs, as the tables will show, are related to foreign assembly, transportation, and duties.

Production cost figures for Mexico and leading CBERA suppliers, as well as an analytical overview of expected NAFTA effects for the six products, are presented below.

Table 9
Men's cotton t-shirts[1]

(U.S. dollars per dozen)

Item	Mexico U.S.-formed and cut fabric	Mexico U.S.-cut fabric	CBERA[2] U.S.-formed and cut fabric	CBERA[2] U.S.-cut fabric
Fabric	11.99	13.67	11.99	13.67
Assembly[3]	***	***	***	***
Freight[4]	0.97	0.97	1.21	1.21
Duty[5]	1.06	1.06	0.66	0.66
Other[6]	***	***	***	***
Total cost (U.S. entry port)	19.81	21.49	17.74	19.42

[1] HTS subheading 6109.10.0005; MFA quota category 352.
[2] Based on data collected for t-shirt producers in Jamaica. U.S. imports of t-shirts from Jamaica represented 69.0 percent of total t-shirt imports from CBERA countries in 1991.
[3] Includes overhead costs.
[4] Includes both inland U.S. and non-U.S. freight costs. Duties are assessed only on the non-U.S. portion of this item.
[5] For 807 and 807A transactions, duties are assessed only on the non-U.S. value added.
[6] Includes miscellaneous trim, brokers' fees, etc.

All-Cotton T-shirts

Fabric availability and cost do not appear to be critical issues for U.S. apparel companies assembling cotton undershirts in the Caribbean Basin and Mexico. Indeed, U.S. industry sources have indicated that most cotton fabrics used to make t-shirts can be sourced easily and competitively from U.S. mills. Neither the "yarn-forward" nor "fabric-forward" rule of origin, therefore, would substantially affect the competitiveness of Mexican t-shirt assembly operations under a NAFTA.

* * *. The removal of a $1.06/dozen duty on imported Mexican t-shirts lowers the total cost of the product by 5.4 percent to $18.75 per dozen for firms using U.S.-formed and cut fabric. This reduction in cost would narrow the Mexican operation's cost disadvantage from 11.7 percent to 5.7 percent in comparison to a typical Caribbean Basin operation.

Quota liberalization for imported t-shirts does not appear to be a significant issue for U.S. 807 producers. Quota fill rates for cotton underwear and cotton knit shirts are both quite low.[81]

Table 10
Men's all-cotton knit golf shirts[1]

(U.S. dollars per dozen)

Item	Mexico U.S.-formed and cut fabric	Mexico U.S.-cut fabric	CBERA[2] U.S.-formed and cut fabric	CBERA[2] U.S.-cut fabric
Fabric	34.93	32.33	34.93	32.33
Assembly[3]	***	***	***	***
Freight[4]	1.87	1.87	3.60	3.60
Duty[5]	2.80	2.80	2.47	2.47
Other[6]	***	***	***	***
Total cost (U.S. entry port) . .	63.75	61.15	63.58	60.98

[1] HTS subheading 6105.10.0010; MFA quota category 338.
[2] Based on data collected for knit shirt producers in the Dominican Republic. U.S. imports of knit golf shirts from the Dominican Republic represented 25.7 percent of total golf shirt imports from CBERA countries in 1991. The Dominican Republic was the major CBERA supplier of knit golf shirts in 1991.
[3] Includes overhead costs.
[4] Includes both inland U.S. and non-U.S. freight costs. Duties are assessed only on the non-U.S. portion of this item.
[5] For 807 and 807A transactions, duties are assessed only on the non-U.S. value added.
[6] Includes miscellaneous trim, brokers' fees, etc.

All-Cotton Knit Golf Shirts

Assembly and freight costs together constitute * * * of the total landed production cost for both CBERA and Mexican producers exporting to the United States. Although dyed cotton fabric used in the construction of this item can be sourced readily in the United States, industry sources have indicated that fabric formed outside of North America can be purchased at more competitive prices--resulting in a savings of approximately $2.60 per dozen shirts (about 4 percent of total cost). A "fabric-forward" or "yarn-forward" rule of origin, therefore, might be expected to have a slight negative impact on the competitive position of Mexican producers who might otherwise reduce fabric costs under a "substantial transformation" rule.

---

[81] U.S. Department of Commerce data. The fill rate for Mexican underwear in 1991 was 20.3 percent. The fill rate for cotton knit t-shirts, category 338 (O) was 5.2 percent in 1991.

Under all rules of origin scenarios, however, the removal of the duty on golf shirts (21.0 percent on the foreign value-added) would place the typical Mexican producer in a position of marginal cost advantage over competitors in the Caribbean Basin. For example, a manufacturer using U.S.-formed fabric would see his bottom-line, landed cost fall by $2.80 per dozen shirts, from $63.75 to $60.95--a 4.4-percent reduction in total cost. * * *.

The removal of U.S. import quotas on Mexican-made cotton knit shirts would not, in all likelihood, have an important effect on competitiveness. In recent years the knit shirts quota for Mexico has not been highly utilized.[82]

Table 11
Men's blue jeans[1]

(U.S. dollars per dozen)

Item	Mexico: U.S.-formed and cut fabric	Mexico: U.S.-cut fabric	CBERA[2]: U.S.-formed and cut fabric	CBERA[2]: U.S.-cut fabric
Fabric	44.30	44.30	44.30	44.30
Assembly[3]	***	***	***	***
Freight[4]	1.86	1.86	3.20	3.20
Duty[5]	3.92	3.92	4.94	4.94
Other[6]	***	***	***	***
Total cost (U.S. entry port)	81.03	81.03	88.50	88.50

[1] HTS subheading 6203.42.4010; MFA quota category 347.
[2] Based on data collected for jeans producers in Costa Rica and Honduras. U.S. imports of blue jeans from Costa Rica and Honduras represented 64.3 percent of total imports of blue jeans from CBERA countries in 1991.
[3] Includes overhead costs.
[4] Includes both inland U.S. and non-U.S. freight costs. Duties are assessed only on the non-U.S. portion of this item.
[5] For 807 and 807A transactions, duties are assessed only on the non-U.S. value added.
[6] Includes miscellaneous trim, brokers' fees, etc.

Blue Jeans

Denim fabric used by U.S. apparel producers in the Caribbean Basin and Mexico can be sourced easily in the United States, and U.S. mills rank among the world's most cost-competitive producers of this type of fabric. This fact is reflected in the fabric cost data in table 11, which shows identical prices for U.S. and non-U.S. denim fabric. Most jeans producers appear to have little difficulty finding U.S. fabric. As a result, neither the

[82] U.S. Department of Commerce data indicate the 1991 fill rate for category 338 (S), cotton knit shirts other than t-shirts, was 41.8 percent.

"yarn-forward" nor "fabric-forward" rule of origin scenarios would detract from the competitiveness of Mexican assembly operations under a NAFTA.

Non-U.S. freight and assembly costs for blue jeans represent * * * of the total cost for Mexican-made jeans and * * * for trousers assembled in a typical CBERA facility. The large volumes of blue jean production in Costa Rica (a relatively high-cost supplier) influence assembly costs in the composite CBERA product. Lower assembly costs in Mexico, in relation to Costa Rica, help explain the lower pre-NAFTA cost figure of $81.03 per dozen--8.4-percent lower than the total cost for a typical CBERA assembly operation. Table 1 shows that removal of the duty lowers the total cost figure for Mexico by $3.92 (a 4.8 percent reduction), and widens the Mexican cost advantage to 12.9 percent over CBERA producers.

In addition to the duty-removal effect, elimination of quotas on Mexican-made jeans can be expected to enhance the competitiveness of producers in Mexico under the NAFTA. During the 1991 quota year, the fill rates for quotas on imported Mexican trousers were 88.2 and 99.3 percent.[83] However, U.S. import quotas for these items were increased significantly during that year.

Table 12
Women's polyester blouses[1]

(U.S. dollars per dozen)

Item	Mexico: U.S.-formed and cut fabric	Mexico: U.S.-cut fabric	CBERA[2]: U.S.-formed and cut fabric	CBERA[2]: U.S.-cut fabric
Fabric	76.08	71.28	76.08	71.28
Assembly[3]	***	***	***	***
Freight[4]	2.39	2.39	3.88	3.88
Duty[5]	5.23	5.23	4.66	4.66
Other[6]	***	***	***	***
Total cost (U.S. entry port) . .	119.64	114.84	118.40	113.60

[1] HTS subheading 6206.40.3030; MFA quota category 641.
[2] Based on data collected for blouse producers in Guatemala and the Dominican Republic. U.S. imports of polyester blouses from Guatemala and the Dominican Republic represented 47.8 percent of total polyester blouse imports from CBERA countries in 1991.
[3] Includes overhead costs.
[4] Includes both inland U.S. and non-U.S. freight costs. Duties are assessed only on the non-U.S. portion of this item.
[5] For 807 and 807A transactions, duties are assessed only on the non-U.S. value added.
[6] Includes miscellaneous trim, brokers' fees, etc.

[83] U.S. Department of Commerce data for category 347/348/647/648.

Polyester Blouses

Fabric availability appears to be a major issue for U.S. companies manufacturing blouses in the Caribbean Basin and Mexico. One U.S. apparel firm, for example, insists that the equipment necessary to spin the yarn used in the construction of the polyester fabric simply does not exist in the United States.[84] Informal surveys of U.S. sources revealed a price gap between certain U.S. and imported polyester fabrics used as inputs in these blouses. As a result, some U.S. companies find it difficult to assemble high-quality blouses under the 807A assembly program. Moreover, companies currently producing blouses with non-U.S. fabric would be expected to face higher fabric costs under either a "yarn-forward" or "fabric-forward" NAFTA rule of origin. Higher fabric costs would jeopardize the competitive position of post-NAFTA Mexican operations and reduce the likelihood of investment diversion away from competing blouse suppliers in CBERA countries.

For 807 assembly operations using high-priced polyester fabric of this kind, * * *. The duty reduction associated with the NAFTA, would have a notable effect on the bottom-line costs of Mexican producers. Removal of a $5.23 duty (4.4 percent of total cost) would give the typical Mexican 807A producer a 3.4 percent-cost advantage over a competing operation in the Caribbean Basin. This compares with a Mexican cost disadvantage of 1.0 percent prior to NAFTA.

The quota-fill rate for Mexican blouses surpassed 80 percent during the 1991 quota year.[85] This suggests that levels of Mexican production were lower as a result of U.S. import restraints than might otherwise have been the case.

[84] U.S. apparel company officials, interview with USITC staff, New York, Mar. 31, 1992.

[85] U.S. Department of Commerce data for category 341/641, cotton and manmade fiber non-knit blouses. The quota fill rate for 1991 was 80.8 percent.

APPENDIX I

DESCRIPTION OF THE TRADE DIVERSION MODEL

The appendix describes the economic model used in Chapter V to generate estimates of trade diversion under a NAFTA. It addresses two subjects relating to the economic analysis of U.S. apparel import demand. First, it presents the formal model used in the analysis and it shows how the model was applied to the analysis of apparel import demand. Second, it describes the data used in the formal model, including the sources for the elasticities.

A MODEL OF U.S. APPAREL DEMAND

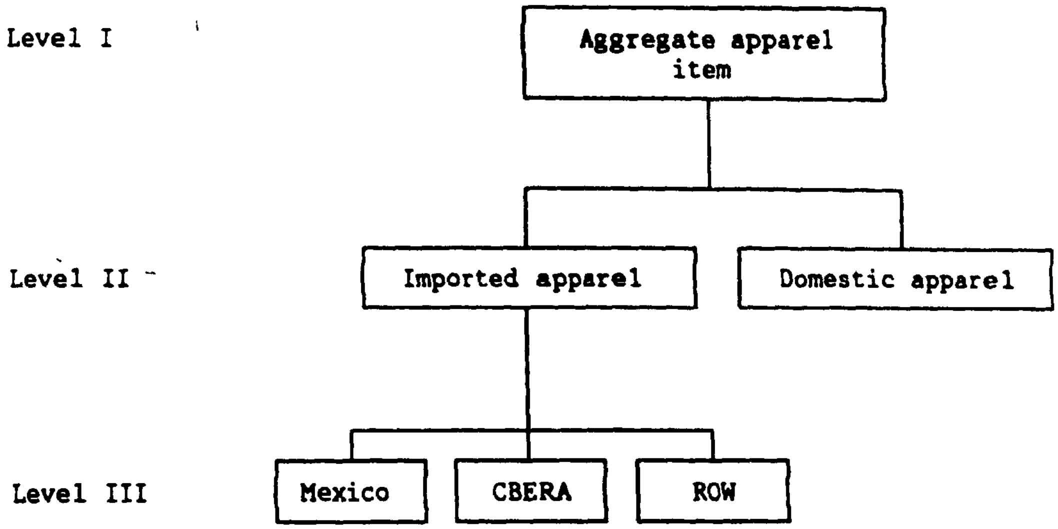
Basic Approach

The basic approach of the model is presented in graphical form in figure C1. At level I of the analysis, demand for the apparel item under consideration from both domestic production and import sources is represented by the box labeled "aggregate apparel item."[1] The demand for the aggregate apparel item varies inversely with a price index defined over imports as a whole and domestic production. That is, the lower the aggregate apparel item price, the more will be demanded.

---

[1] The term "aggregate" does not refer to an aggregation across apparel items, but rather to aggregation across domestic and imported varieties of the item. See next paragraph.

Figure C-1
Model structure



At level II of the analysis, demand for the aggregate apparel item under consideration is divided into two parts. The first part is imported apparel, which is, in turn, an aggregate of imports from all sources. The second part is domestic apparel. Domestic apparel and imported apparel are considered to be imperfect substitutes in the demand for the aggregate apparel item, and the division between these two parts is sensitive to their relative prices. For example, if the imported apparel component of the aggregate apparel item were to fall in price, there would be a tendency for the domestic component to become smaller and the imported component to become larger.

At level III of the analysis, the imported apparel item is divided among three import sources: the five CBERA countries as an aggregate, Mexico, and the rest of the world (ROW). Imports from these three sources are imperfect substitutes in total import demand for the apparel item under consideration, and the division of total imports into imports from these different sources is sensitive to their relative prices. For example, if imported apparel from Mexico were to fall in price, there would be a tendency for imports from other sources to fall and imports from Mexico to increase.

The application of this analytical framework to the question of the impact of the NAFTA on CBERA apparel exports is as follows. Implementation of the NAFTA will reduce the severity of U.S. restraints on imports from Mexico of the apparel item under consideration. The price of the item from Mexico to domestic importers in the United States will therefore fall. At level III in figure C-1, there will be a tendency for imports from Mexico to rise. Imports of the apparel item from the CBERA countries and the ROW would tend to fall. At level II, the price index for imports from all sources would fall. Therefore, there would be a tendency for the import portion of the aggregate apparel item to rise and the domestic portion of the aggregate apparel item to fall. Finally, at level I, the price index for the aggregate apparel item would fall slightly, and there would be a tendency for apparel demand to increase. This increase in demand would be transmitted down through levels II and III. The key effect, however, will be the potential reduction in imports of apparel from CBERA at level III.

The import demand system represented graphically in figure 1 is constructed as a standard economic model and is applied to a base year of 1991. The sensitivity of demands to prices at levels II and III in the model are governed by share parameters reflecting 1991 purchases and behavioral parameters reflecting responsiveness of producers and consumers to price changes. At level II of figure 1, a single behavioral parameter determines the degree to which consumers substitute between the imported and domestic versions of the apparel item under consideration in response to changes in their relative prices. At level III, a single behavioral parameter determines the degree to which importers substitution among import sources in response to changes in their relative prices. The use of a single parameter implies that imports from CBERA and the ROW are equally substitutable for imports from Mexico. These behavioral parameters are the price and import source substitution elasticities. Each elasticity has a low and a high level as described below.

Theoretical Model

Domestic production of the apparel item under consideration is modeled using a relation in which domestic supply (s_d) is positively related to the price of domestic apparel (p_d):

$$s_d = s_d(p_d;\ \varepsilon_s) \tag{1}$$

where ε_s is the elasticity of domestic supply.

Domestic demand for an aggregate of domestically-produced and imported apparel is modeled using a relation in which domestic demand (d_q) is negatively related to a price index of domestic and imported apparel (p_q):

$$d_q = d_q(p_q;\ \varepsilon_d) \tag{2}$$
$$p_q d_q = p_d d_d + p_m d_m \tag{3}$$

where ε_d is the elasticity of domestic demand, d_q is an constant elasticity of substitution (CES) aggregation of imports and the domestic good, d_d is the demand for domestic-produced apparel, p_m is the import price index, and d_m is the demand for a CES aggregation of imports from the different import sources.[2] The equations for d_d and d_m are CES demand functions:

$$d_d = d_d(p_d, p_m, d_q;\ \sigma_q) \tag{4}$$
$$d_m = d_m(p_d, p_m, d_q;\ \sigma_q) \tag{5}$$

[2] On the CES aggregation of imports and domestic goods, see K. Dervis, J. de Melo, and S. Robinson, *General Equilibrium Models for Development Policy*, Cambridge University Press, Cambridge, 1982, p. 222.

where σ_q is the elasticity of substitution between imports and domestic supply. The implication of equations (4) and (5) are that domestically-produced and imported apparel are imperfectly substitutable in the CES aggregate d_q.

Equilibrium in the domestic market for the apparel item requires that demand for domestic apparel equals domestic supply of domestic apparel:

$$d_d = s_d \tag{6}$$

Imports by source are given by the following CES demand functions:

$$m_{cb} = m_{cb}(p_{cb}, p_{mx}, p_{rw}, d_m; \sigma_m) \tag{7}$$
$$m_{mx} = m_{mx}(p_{cb}, p_{mx}, p_{rw}, d_m; \sigma_m) \tag{8}$$
$$m_{rw} = m_{rw}(p_{cb}, p_{mx}, , p_{rw}, d_m; \sigma_m) \tag{9}$$

where m_{cb} is imports of the apparel item from CBERA countries, m_{mx} is imports from Mexico, m_{rw} is imports from the rest of the world, p_{cb}, p_{mx}, and p_{rw} are the associated import prices, and σ_m is the elasticity of substitution among imports of the different sources. The implication of equations (7), (8), and (9) is that the degree of substitutability between any two of the three import types is the same.

The aggregate price of imports is given by:

$$p_m m = p_{cb}m_{cb} + p_{mx}m_{mx} + p_{rw}m_{rw} \tag{10}$$

Finally, the prices of the imported apparel items need to be specified. These are determined by world prices and protection levels as follows:

$$p_{cb} = (1+\tau_{cb})\mathbf{T}_{cb} \tag{11}$$
$$p_{mx} = (1+\tau_{mx})\mathbf{T}_{mx} \tag{12}$$
$$p_{rw} = (1+\tau_{rw})\mathbf{T}_{rw} \tag{13}$$

where τ_i is an *ad valorem* measure of the protection level on imports from source i and $\mathbf{T}_i$ is the world price of imports from source i where i = cb, mx, rw.

The endogenous variable to be determined by these equations are s_d, d_q, p_q, d_d, d_m, p_d, p_m, m_{cb}, m_{mx}, m_{rw}, p_{cb}, p_{mx}, and p_{rw}.

Elasticities

The equations presented above require information about four elasticities. These are the elasticity of domestic supply (ε_s), the elasticity of domestic demand (ε_d), the elasticity of substitution between domestic and imported apparel (σ_q), and the elasticity of substitution among imported apparel sources (σ_m). For each of these, a low and high value were adopted.

Elasticities of supply are notoriously difficult to estimate. For this reason, values of 1.0 and 10.0 were used as low and high elasticities. A great deal more information on elasticities of demand for apparel is available. Table C-1 presents the results of a few studies. Based on these estimates, values of -0.30 and -0.60 were used as low and high elasticities.

The elasticity of substitution between domestic and imported apparel was estimated by Reinert and Roland-Holst at a value of 0.45.[3] This estimate was used as a low value and 1.50 was used as a high value.

The elasticity of substitution among imported apparel sources was estimated directly for this study, following a methodology developed by Reinert and Shiells.[4] The rest of this appendix describes this estimation and the results.

The preparation of the data for estimation began with the concordance of the relevant HTS number to the corresponding TSUSA numbers for each of the quarters during the 1978-1988 period. This necessitated expanding the apparel items considered by a very small amount for a few of the HTS numbers. Next, a time series of quarterly import data for the 1978 to 1988 period was extracted from U.S. Department of Commerce data tapes for the 7-digit TSUSA items corresponding to each HTS number separately for the three suppliers: the five CBERA countries as a whole, Mexico, and the ROW. Series of quantities and c.i.f. values were assembled, yielding a full time series for each HTS number except for HTS 6109.10.0005, Mens' and boys' all white, cotton t-shirts. For this item, imports into the United States did not begin recently enough to support estimation. For all items, unit values were calculated to be used as prices.[5]

---

[3] K.A. Reinert and D.W. Roland-Holst, "Disaggregated Armington Elasticities for the Mining and Manufacturing Sectors of the United States," *Journal of Policy Modeling*, vol. 14, No. 5, (1992). This study addressed apparel as a whole, but it would be difficult to obtain domestic price and quantity series to estimate an elasticity of substitution between disaggregated domestic and imported apparel items.

[4] K.A. Reinert and C.R. Shiells, "Trade Substitution Elasticities for Analysis of a North American Free Trade Area," unpublished working paper, July 1991.

[5] Given the changing nature of the concordance between any given HTS item and the corresponding TSUSA numbers, it was not possible to create a Laspeyres price index over the TSUSA numbers as in Reinert and Roland-Holst (1992) and Reinert and Shiells (1991).

Table C-1
Elasticities of Demand for Apparel

Study	Estimated Elasticity
Blanciforti and Green (1983)	-0.57
Eastwood and Craven (1981)	-0.55
Houthakker and Taylor (1970)	-0.57
Phillips (1972)	-0.30
Maki (1988)	-0.37

Source: L. Blanciforti and R. Green, "An Almost Ideal Demand System Incorporating Habits: An Analysis of Expenditures on Food and Aggregate Commodity Groups," *Review of Economics and Statistics*, vol. 65, No. 3, (Aug. 1983), pp. 511-515; D.B. Eastwood and J.A. Craven, "Food Demand and Savings in a Complete, Extended, Linear Expenditure System," *American Journal of Agricultural Economics*, vol. 63 (Aug. 1981), pp. 544-549; H.S. Houthakker and L.D. Taylor, *Consumer Demand in the United States: Analyses and Projection*, (Harvard University Press, Cambridge, 1970); L. Phillips, "A Dynamic Version of the Linear Expenditure Model," *Review of Economics and Statistics*, vol. 54, (1972), pp. 450-458; A. Maki, "The Estimation of a Complete Demand System Using the Marginal Rates of Substitution: An Indifference Map Interpretation of the Houthakker-Taylor Model," *Economic Studies Quarterly*, vol. 39, No. 1, (Mar. 1988), pp. 64-76.

Table C-2
Estimated Elasticities of Substitution by Import Source

Items	HTS Numbers[1]	Elasticity[2]	t Statistic[3]
Men's and boy's cotton trousers, not knit . . .	6203.42.4005 6203.42.4010 6203.42.4025 6203.42.4045 6203.42.4015 6203.42.4035	1.11	1.71
Men's and boy's cotton t-shirts, all white[4] . .	6109.10.0005	-	-
Men's and boys' cotton knit shirts	6105.10.0010 6105.10.0020 6105.10.0030	0.99	1.15
Brassieres MMF woven . . .	6212.10.2020	1.37	1.42
Women's MMF woven blouses .	6206.40.3030	0.10	17.84
Women's, girls', and infants' suit-type jackets of manmade fibers, not knit	6204.33.10 6204.39.20 6204.33.20 6204.39.30 6204.33.40 6204.33.50	1.04	7.95

[1] In those cases where there are more that one HTS number, the additional numbers were necessitated by the concordance to TSUSA numbers for the generation of time series.
[2] Elasticity of substitution between imports from the five CBERA countries as a group, Mexico and the rest of the world.
[3] Given the sample size and using a one-tail test, a t statistic greater than 1.30 indicates the estimated elasticity is significant at the 10 percent level. A t statistic of greater that 1.68 indicates the estimated elasticity is significant at the 5 percent level.
[4] Data availability was too limited to support estimation.

The estimation technique used was the second of three techniques employed by Reinert and Shiells in a study of trade substitution elasticities for modeling the NAFTA.[6] This technique estimates the elasticity of

[6] Reinert and Shiells, p.   for further details.

substitution based on the CES functional form and utilizes the true CES price aggregator rather than the simple, log-linear price aggregator. The resulting equations are nonlinear in parameters and are therefore estimated using a nonlinear, maximum-likelihood procedure. The technique abstracts from problems of simultaneity and distributed lags, but corrects for first-order and, where necessary, second-order autocorrelation.[7]

The results of the estimation procedure are given in table C-2. Each estimate has the correct sign, ranging from 0.10 to 1.37. For items 1, 3, 4, and 6, the estimates from table C-2 were used as low values and 3.00 was used as high values. There is strong evidence that quotas were binding for item 5, women's MMF woven blouses, over the sample period. This is the likely cause of the very low estimate of 0.10 for this sector and brings into question the validity of the estimation procedure for this sector. Therefore, for items 2 and 5, a low value of 0.90 and a high value of 3.00 were used.

Effective Tariff Rates

The apparel items considered are produced abroad under offshore assembly arrangements and therefore are subject to duty discounts. Larger portions of imports from Mexico and the selected CBERA countries are eligible for these duty discounts than imports from the rest of the world. Consequently, the effective tariff rates for imports from the selected CBERA countries and Mexico are lower than for those from the rest of the world. Additionally, the effective tariff rates on imports from the rest of the world are only slightly lower than the official rates in the tariff schedule. Effective ad valorem tariff rates for imports from each of the three sources are presented in table C-3.

---

[7] The Reinert and Shiells study found that, in general, accounting for simultaneity and distributed lags did not substantially effect the estimation results. In practice, correcting for these problems requires using the log-linear price aggregator in place of the correct CES price aggregator. Commission staff felt that maintaining the CES price aggregator was more important.