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## **ON THE IMPLEMENTATION OF THE DOMINICAN REPUBLIC- CENTRAL AMERICA FREE TRADE AGREEMENT**

### **WRITTEN TESTIMONY BEFORE THE U.S. HOUSE COMMITTEE ON WAYS AND MEANS**

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Oxfam is an international development and humanitarian relief agency committed to developing lasting solutions to poverty, hunger and social injustice. We work in over 120 countries around the globe, including the five Central American countries and the Dominican Republic that are party to the free trade agreement with the United States, known as DR-CAFTA.

Oxfam believes that trade can be an important means to achieving sustainable development and poverty reduction. Trade and development are intimately linked. A global system that has fair trade rules and practices has the potential to lift millions of people out of poverty. For this reason, Oxfam has focused on making global trade rules fair and consistent with development goals, as an integral part of our work to improve livelihoods and reduce poverty in developing countries.

Trade agreements present both opportunities and risks, especially when they involve developed and developing countries. The DR-CAFTA is the first such agreement the US has negotiated with some of the poorest countries in the hemisphere, two of which have annual per capita incomes below \$1,000. The U.S. trading partners in the DR-CAFTA, with a population of 42.5 million, have high levels of poverty and very unequal distributions of income and wealth. They depend heavily on agriculture for the livelihood of significant portions of their populations. These countries are ravaged by curable diseases due to poverty and inadequate health-care coverage. They sorely lack public infrastructure and, in several cases, are highly indebted.

In order for a trade agreement to be fair for these countries and promote their development, it must ensure that governments are able to provide for the food security needs of their people. And for an agreement to contribute to their poverty reduction, it must not prevent citizens from being able to access life-saving drugs they desperately need to effectively combat contagious diseases like HIV/AIDS or prevalent illnesses like diabetes. Trade agreements inevitably have winners and losers. Oxfam believes that those who stand to lose in the DR-CAFTA are the ones who are already disadvantaged in these highly unequal societies, where the majority of poor people live in rural areas, rely on income from agriculture and must pay for medicines out-of-pocket.

There has been much public debate about what the passage or rejection of the DR-CAFTA will mean for the U.S. trade agenda. Oxfam, however, believes that the DR-CAFTA must be judged only on the basis of what this particular agreement will mean specifically for the seven countries involved. Congress should look carefully at the terms of the DR-CAFTA to understand their implications in a region of high geo-political importance to our country. On balance, Oxfam believes the agreement, in its current form, will do more harm than good. It will threaten the livelihoods of millions in Central America and the Dominican Republic and may contribute to increased insecurity and instability in that region.

Oxfam wishes to focus attention on provisions in the DR-CAFTA involving agriculture, intellectual property and investment. As a result of our analysis in these areas, Oxfam believes the DR-CAFTA is a bad deal for millions of farmers, workers, and consumers in Central America and the Dominican Republic and should therefore be rejected.

### *Agriculture*

Agriculture currently comprises between 10 to 23 percent of GDP in the six DR-CAFTA trading partners, while it represents less than two percent of GDP in the U.S. Nearly a third of employment in these six countries depends on agriculture, much of which involves food essentials for consumption in the region, and most of these workers are poor and low skilled.

There are two major reasons why Oxfam believes many farmers in Central America and the Dominican Republic are at significant risk of losing their livelihood under DR-CAFTA. Market access rules for agriculture in the agreement deny developing country governments the ability to adopt measures to ensure domestic food security and promote rural livelihoods. Under DR-CAFTA, countries must eliminate import tariffs on virtually all agricultural goods, including those food essentials that are most important for small farmers' incomes - rice, yellow corn, beans and dairy products.

At the same time, the agreement requires Central American countries and the Dominican Republic to open the door for dumping of highly subsidized US agricultural exports at prices below their cost of production. This situation is not only profoundly unfair, but it risks creating poverty and economic dislocations among the 5.5 million farmers and farmworkers in the region.

Although DR-CAFTA provides for longer tariff elimination periods for some basic commodities in Central America and the Dominican Republic, duty-free quotas are immediately created or expanded beginning in the first year of the agreement. These duty-free quotas are nearly equal to current US exports to these markets (quotas begin to surpass current US export levels starting in the second year of DR-CAFTA) and will immediately drive down prices for local producers. The region's small farmers – who receive no subsidies, lack access to credit and depend on the income from each year's harvest for their subsistence – will be unable to compete with subsidized US exports. And as more local farmers go out of business each year, the region's grain imports in following years are likely to surpass the annual quota increases, as occurred in Mexico under NAFTA, making the longer tariff phase-out periods irrelevant.

The case of corn in Mexico under NAFTA is illustrative. An extended 15-year period for tariff elimination was instead reduced to little more than 30 months, and real corn prices in Mexico fell more than 70 percent in the first eight years under NAFTA, without benefiting Mexican consumers. It is estimated that since NAFTA's passage, 1.7 million Mexican peasants working in the agricultural sector have lost their jobs. In addition, 15 million small farmers have lost significant income because they could not compete with subsidized US exports, such as corn. Many left their land and fled to urban areas. It is no coincidence that the number of Mexicans crossing the US border without authorization seeking employment and a better life more than doubled between 1990 and 2000 – with most of that growth occurring after NAFTA went into effect in 1994 – and has continued to increase in this decade.

A similar outcome can be expected under the DR-CAFTA for producers of basic grains such as rice. In fact, the experience of the rice sector in Honduras in the 1990s offers a case study of the likely impact on small farmers in the region. In 1991, the Honduran government cut tariffs on rice imports to make up for a shortage due to drought, and a flood of imports at harvest time equivalent to the country's annual consumption left local producers without a market. Rice prices fell by more than 28 percent in one year and, as a result, areas under rice cultivation decreased by 35 percent the following year. Over a decade, the number of rice producers dropped from 25,000 to fewer than 2,000, and the jobs generated from rice production fell from 150,000 to 11,200. As a result, rice production was reduced by 86 percent between 1991 and 2002, and the amount of foreign exchange spent on rice imports increased 20-fold (from \$1 million in 1989 to \$20 million in 2003). At the same time, the price of rice to consumers rose 140 percent in nominal terms, or 12 percent in dollar terms, over the decade.

The market access rules for agriculture in the DR-CAFTA deny developing country governments the policy flexibilities necessary to promote rural development, protect livelihoods, and provide food security to their citizens. The agreement negates the principle governing multilateral trade negotiations for the past 50 years that developing countries are not required to make reciprocal commitments to reduce trade barriers if these are inconsistent with their individual development needs. Instead, the DR-CAFTA does not incorporate pro-development concepts, such as special and differential treatment, and precludes use of flexibilities available to developing countries at the WTO. It does not allow developing countries to use differentiated tariff reduction formulae or designate special products eligible for more flexible treatment. It prohibits the use of the WTO safeguard, and the safeguard mechanism provided under DR-

CAFTA is weak and temporary: a price drop could render it useless since it is linked to volume instead of prices of imports, and it can only be applied until the tariff is completely phased out.

This will have a devastating impact on the 5.5 million Central Americans who depend on agriculture for their livelihoods. What will the US gain at the expense of the loss of livelihoods of small farmers in Central America and the Dominican Republic? According to the US International Trade Commission, US grain exports can be expected to expand by 1.2 percent annually once tariffs are fully eliminated under DR-CAFTA. Overall, the market access provisions are expected to increase US GDP by less than 0.01 percent annually. Considering the cost in terms of increased poverty and social problems for our neighbors, not to mention the potential increase in immigration to our borders, the DR-CAFTA is not only a bad deal for development in the region, but it provides no appreciable benefits to US citizens.

### ***Intellectual Property***

The rules on intellectual property in DR-CAFTA are another serious area of concern for Oxfam. All of the Central American countries and the Dominican Republic are WTO members and are therefore bound to implement the intellectual property provisions in the WTO's Agreement on Trade-Related Intellectual Property Rights, known as "TRIPS". But the DR-CAFTA goes well beyond the existing TRIPS provisions, imposing new so-called TRIPS-plus provisions related to pharmaceuticals. Most of these provisions are aimed at delaying the introduction of generic competition, thereby prolonging a patent holder's monopoly over the marketing of a medicine. When generic drugs cannot enter the market to compete with brand-named products, drug prices are higher and fewer people have access to medicines.

At the heart of intellectual property rights systems is a balance between the rights of patent holders and the public interest. In particular, determining the appropriate balance between protections related to pharmaceuticals and public health is a complex task still being debated in the United States -- for example, the "drug re-importation" debate in Congress. Oxfam does not believe that there is one "size" of intellectual property protection that fits all, however. The appropriate balance depends upon a variety of factors, such as the level of poverty in a country, the likelihood that protections will generate innovation, and the real-world effects from higher medicine prices resulting from protections.

Many public health and intellectual property experts have warned that TRIPS-plus provisions may undermine public health in poor countries, without generating any appreciable gains in innovation. This concern became a major issue at the WTO, and the importance of preserving public health was affirmed in the 2001 Doha Declaration on TRIPS and Public Health in 2001 by all WTO members, including the United States. The Doha Declaration confirmed that WTO Members may use "flexibilities" built into TRIPS to modify intellectual property rules to address public health needs, and constitutes a commitment to favor public health over intellectual property rights.

In 2002, Congress endorsed this commitment as part of Trade Promotion Authority, under which DR-CAFTA was negotiated, by instructing the US Trade Representative to respect the Doha Declaration in trade negotiations (Section 2102(b)(4)(C) of the Trade Act of 2002). Yet USTR has ignored the direction of both the WTO and Congress by forcing the governments

of Central America and the Dominican Republic to adopt some of the highest levels of intellectual property protections for drugs in the world. This completely undermines the protections for public health laid out in the Doha Declaration. Oxfam believes that many of these provisions are not suitable for the small, poor developing economies in Central America and will result in reduced access to needed medicines and therapies, with no appreciable benefit in innovation or research and development spending.

Many of the intellectual property provisions in DR-CAFTA tip the balance of intellectual property protections in favor of the short-term commercial interests of US pharmaceutical companies, at the expense of public health. These provisions:

- Extend patent protection beyond the 20-year period required under TRIPS. Contrary to US law, no upper limit is placed on such extensions. Twenty years of patent protection is more than an adequate monopoly for patent holders to recover investments and generate profits. Extending this monopoly period unfairly favors patent holders to the detriment of the broader public interest in accessing affordable medicines.
- Require test data protection for periods of up to 10 years. These rules will delay for up to 10 years the introduction of generic medicines, even in the absence of patent barriers.
- Effectively eliminate the ability of Central American countries and the Dominican Republic to use compulsory licensing, a key tool available to governments to meet their citizens' public health needs. Compulsory licenses provide an important safeguard to governments to counterbalance the monopoly rights granted to patent holders. Both developing and developed countries – including the United States – have used compulsory licenses or the threat of them to bring down medicine prices.
- Force national drug registration authorities to serve as patent police, which prevents these authorities from granting marketing approval for generic versions of drugs until after the patent expires. This could prevent or delay access to affordable generic versions of new medicines, as well as undermine the use of compulsory licenses. Furthermore, this goes beyond US law, which places the burden on the patent owner to enforce its own rights. DR-CAFTA forces the government to bear the cost, expense, and delay of enforcing private patent rights.

When the DR-CAFTA was signed on August 5, 2004, a side letter or “understanding” on intellectual property and public health was included in response to criticism that the intellectual property restrictions in the agreement could undermine public health. However, this “understanding” does nothing to allay Oxfam’s concerns with these provisions. In reality, it merely states that CAFTA provisions “do not affect a Party’s ability to take necessary measures to protect public health by promoting access to medicines for all” or from “effective utilization” of the WTO decision on TRIPS. This clause is virtually meaningless from a legal standpoint because it is just a declaratory statement, similar to a preamble or an objective. It is not a legally binding exception to the very clear obligations in the Agreement but at best has interpretive value. USTR has studiously avoided describing the “understanding” as a legally binding exception.

Oxfam believes that TRIPS-plus provisions relating to pharmaceuticals should not be included in a trade agreement with Central America and the Dominican Republic. Central America has the second highest death rate from communicable diseases in Latin America. Over 165,000 people are living with HIV/AIDS and more than 30,000 cases of full-blown AIDS have been reported in the region. Resources for public health in the DR-CAFTA countries are extremely limited. Medicines sold at monopoly prices are too costly for these countries to provide through their public health systems and too expensive for poor people to pay for out-of-pocket. These countries should be able to use the TRIPS public-health safeguards to the fullest to protect public health and promote access to medicines for all, as affirmed by the Doha Declaration.

DR-CAFTA is often described as a “cutting-edge” trade agreement that will serve as a model for future trade agreements. Oxfam feels this is a grim prospect. Imposing new intellectual property burdens on developing countries that increase the cost of medicines for poor people is a very bad model indeed, particularly looking towards the other countries with which the US is currently negotiating trade agreements.

### ***Investment***

Investment rules in the DR-CAFTA are another important concern for Oxfam in this trade agreement. These rules are clear and strong on the rights of foreign investors, but say little about the rights and obligations of governments to ensure that investors behave responsibly and that investment serves the public good. Specifically, DR-CAFTA restricts governments’ ability to regulate foreign investment through the use of measures such as performance requirements, technology transfers, and capital controls. Oxfam believes that prohibiting pro-development measures such as these will reduce the positive impact that investment in the region can have and may create large new financial and policy burdens for already over-stretched governments.

In Central America and the Dominican Republic, increased investment is critical to achieving sustainable development. Yet several recent studies show that trade and investment agreements themselves do not stimulate additional foreign investment. Rather, macroeconomic and political stability, as well as market size, are determining factors. Furthermore, Oxfam believes that the quality – not just quantity – of investment is key in promoting development. Positive incentives to direct investment can help distribute wealth and promote economic growth, which can result in improved livelihoods. By setting performance requirements, governments can ensure the use of local inputs, which helps create backward linkages to the domestic economy. Through technology transfers, governments can help establish valuable linkages between foreign and domestic producers.

However, DR-CAFTA will forbid governments from using local content rules and technology transfers. Without the flexibility to utilize these measures, governments are powerless to direct investment so that it benefits the rest of the domestic economy. This will lead to a scenario in which a limited number of investors may prosper without contributing more broadly to sustainable growth in the countries where they operate. This defies the spirit of the DR-CAFTA agreement, which claims to have the development of Central America and the Dominican Republic as one of its goals.

Much of the foreign direct investment recently flowing into the region has been directed towards *maquiladora* factories or export processing zones, mostly for garments manufacturing. While these factories do provide some badly needed jobs, they usually contribute little to the overall economy because of the enclave nature of their production. Moreover, jobs in these factories are increasingly at risk with the removal of global quotas for textiles and apparel.

Oxfam is also concerned that DR-CAFTA forbids restrictions on the repatriation of profits and limits governments' ability to impose controls on highly speculative investments. This means that foreign investors in the region will have unrestricted ability to bring capital into and out of countries, while governments will have little recourse to deal with economic instability, should investors suddenly pull their money out of the country. While a stable business climate is important, so too is ensuring that investment contributes to domestic growth and broad-based sustainable development. Unregulated capital flight can have devastating consequences, especially in case of a financial meltdown, such as occurred in Argentina in 2001.

Also of serious concern is the investor-state dispute settlement mechanism in the DR-CAFTA, which, similar to NAFTA, will enable foreign investors to bring suits before international arbitral tribunals when they believe their business interests have been impaired by government regulatory actions. Investment rules in the DR-CAFTA broadly define what constitutes an expropriation and leave open the possibility that these ad-hoc tribunals will interpret social and environmental regulations as an "indirect expropriation." Thus, foreign investors will be able to challenge laws or regulations at the national, state or local levels, even if these are enacted for legitimate public interest objectives, including public health, safety, and environmental protection.

These special international tribunals are neither open to the public nor accountable to democratic processes. They lack the transparency generally afforded by normal judicial proceedings, yet are empowered to order governments to directly compensate investors for regulations that hurt them, regardless of the public good that the regulations might serve. Claimants are not required to exhaust domestic judicial remedies before bringing investment claims to these international tribunals, thus allowing foreign investors to bypass domestic legal systems. Although the DR-CAFTA was intended to strengthen and support democratic institutions in Central America and the Dominican Republic, it may actually undermine the judiciaries in the region.

This dispute settlement mechanism has been used to challenge important regulations that are expressly designed to protect public health, safety, the environment, and other public interest objectives that enhance social welfare. To date, over 40 suits have been filed by corporations under NAFTA's investment rules in special tribunals, seeking \$28 billion in claims from the US, Canadian and Mexican governments. If NAFTA is any indication, the investment provisions of DR-CAFTA could create large new liabilities for the governments of Central America and the Dominican Republic. Perhaps more problematic is the chilling effect the threat of litigation by investors could create on policy-makers interested in generating new environmental, public-health, and pro-development safeguards.

Highlighting this problem is a bitter dispute between Canadian-owned Glamis Gold, Ltd., which is seeking to construct a mine in San Miguel, Guatemala, and the local citizens who oppose the project. Backed by the Catholic Church, local residents fear that the mining project will wreak havoc on the local environment. They successfully pressured the Guatemalan government to agree to freeze issuance of future mining permits. However, under DR-CAFTA, foreign investors will be able to challenge local measures like this one, claiming discrimination as foreign investors. At risk will be governments' ability to provide effective regulation to protect workers, health and safety, and the environment. Any agreement that contains investment rules that limits governments' ability to protect the health and well-being of its citizens should be opposed.

## **Conclusion**

CAFTA is likely to increase inequality and exacerbate poverty in a region that is still struggling to recover from the devastation of wars, hurricanes and droughts. Under the Caribbean Basin Initiative (CBI), Congress established trade preferences to facilitate the economic development and export diversification of the Caribbean Basin economies. These benefits were permanently extended in 1990, and in 2000 the list of products eligible for duty-free access to the US market was expanded, in part in response to the devastation wrought by Hurricane Mitch. Nevertheless, the region continues to suffer from serious problems of poverty and inequality.

Oxfam believes it is in the interest of the United States to promote economic development in the region, including increased development assistance, institution-building, and increased trade. However, the DR-CAFTA is, at best, a mixed bag. The agreement provides very modest and incremental trading opportunities for our poorer neighbors, while it imposes major new obligations and restrictions in the process.

In general, Oxfam believes that the US trade negotiation strategy has set the wrong priorities. With limited resources, the USTR has pursued numerous smaller bilateral and regional trade agreements even while a much bigger, and more important, trade agreement has stalled. For both the US and the world, the WTO Doha Round offers potential benefits that are orders of magnitude larger than those in free trade agreements with small countries such as DR-CAFTA. While negotiating trade agreements at the global level is certainly a messy and cumbersome process, the alternative is a very scattered and asymmetrical trading scheme that adds complexity and increases entry costs. This is not good for the US, but it is far worse for developing countries, many of which are already very marginal players in global trade. And while the US is likely to have to make more concessions – particularly in agriculture – at the multilateral level, than in bilateral agreements, this is where the US can demand concessions from other rich countries like Europe and Japan. Investing in, rather than neglecting, the WTO and the Doha Round, will help build a more common, rules-based system that provides more opportunity and stability for both the US and developing countries.

The rules set forth in the DR-CAFTA on agriculture, intellectual property, and investment add up to a bad deal for farmers, workers, and consumers in Central America and the

Dominican Republic. Rather than setting out provisions that will foster broad-based economic growth and sustainable development, DR-CAFTA will put millions of poor people at risk of losing their livelihood. The US should do better if it wants to promote peace, political stability, and economic security in this region that has struggled with poverty and inequality, and the resulting instability, for so long. Unfortunately, the DR-CAFTA is wrong way to achieve these goals, which is why Oxfam urges Congress to vote no.