Central American Export Processing Zones:
Industrial Policy vs. Trade Liberalization in Multilateral and Regional Trade Agreements

by

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List of Acronyms

ADB	Asian Development Bank
AFTA	ASEAN Free Trade Area
AGOA	African Growth and Opportunity Act
AHM	Asociación Hondureña de Maquiladores (Honduran Manufacturers Association)
APHD	Asia Partnership for Human Development
ASCM	Agreement on Subsidies and Countervailing Measures
ASEAN	Association of Southeast Asian Nations
ATC	Agreement on Textiles and Clothing
ATPDEA	Andean Trade Promotion and Drug Eradication Act
AZOFRAS	Asociación de Empresas de Zonas Francas (Association of Free Zones)
BCH	Banco Central de Honduras (Honduran Central Bank)
BIT	Bilateral Investment Treaty
BPO	Business Process Outsourcing
C.A.	Central America
CA-4	Central American Four (Guatemala, Honduras, El Salvador, and Nicaragua)
CAMTEX	Cámara de la Industria Textil, Confección y Zonas Francas (Chamber of the Textiles, Clothing, and Free Zones)
CBI	Caribbean Basin Initiative
CBTPA	Caribbean Basin Trade Partnership Act
CLC	Commission for Labor Cooperation
CLS	Core Labour Standards
CNZF	Comisión Nacional de Zonas Francas (National Free Zone Commission)

CNZFE	Consejo Nacional de Zonas Francas de Exportación (National Free Zones Council)
CoC	Codes of Conduct
CSR	Corporate Social Responsibility
DDA	Doha Development Agenda
DR-CAFTA	United States-Dominican Republic-Central America Free Trade Agreement
DSM	Dispute Settlement Mechanism
DSU	Dispute Settlement Understanding
ECLAC	Economic Commission for Latin America and the Caribbean
EEC	European Economic Community
EOI	Export-Oriented Industrialization
EPA	Economic Partnership Agreement
EPZ	Export Processing Zone
EU	European Union
FDI	Foreign Direct Investment
FTAA	Free Trade Area of the Americas
GATS	General Agreement on Trade in Services
GATT	General Agreement on Tariffs and Trade
GSP	Generalized System of Preferences
GSTP	Global System of Trade Preferences
GUF	Global Union Federation
IDB	Inter-American Development Bank
IEL	International Economic Law
IFA	International Framework Agreement

IIAs	International Investment Agreements
IILS	International Institute of Labour Studies
ILC	International Labour Conference
ILO	International Labour Organization
IMF	International Monetary Fund
ISI	Import-Substitution Industrialization
ISO	International Organization for Standardization
ITO	International Trade Organization
ITR	International Trade Regime
LCCBM	Labor Cooperation and Capacity Building Mechanism
LDCs	Least-Developed Countries
MFA	Multi-Fibre Arrangement
MFN	Most Favored Nation
MNC	Multinational Corporation
MSMEs	Micro, small, and medium enterprises
MTA	Multilateral Trade Agreement
MTN	Multilateral Trade Negotiations
MTS	Multilateral Trading System
NAALC	North American Agreement on Labor Cooperation
NAFTA	North American Free Trade Agreement
NAO	National Administrative Office
NICs	Newly Industrialized Countries
ODECA	Organización de Estados Centroamericanos (Organization of Central American States)

OECD	Organisation for Economic Co-operation and Development
RTA	Regional Trade Agreement
SAFTA	South Asian Free Trade Agreement
SDT	Special and Differential Treatment
SICA	Sistema de la Integración Centroamericana (Central American Integration System)
TPP	Trans-Pacific Partnership
TPR	Trade Policy Review
UN	The United Nations
UNCTAD	United Nations Conference on Trade and Development
UNIDO	United Nations Industrial Development Organization
U.S.	United States
USTR	United States Trade Representative
VER	Voluntary Export Restraint
WB	World Bank
WBCSD	World Business Council for Sustainable Development
WCO	World Customs Organization
WRAP	World Responsible Accredited Production
WTO	World Trade Organization
ZIP	Zona Industrial de Procesamiento (Industrial Processing Zone)

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Introduction

The evolution of the international economic law (hereinafter the IEL) and the creation of new international trade regimes (hereinafter ITRs) to enhance trade liberalization have limited the policy space of developing countries that want to implement industrial policies to stay competitive in the international trade arena. ITRs are defined in the present study as international processes and collection of rules on tariff and non-tariff barriers and export incentive schemes aimed at strengthening the competitiveness of countries. They may be exemplified through multilateral trade agreements (hereinafter MTAs), regional trade agreements (hereinafter RTAs), economic partnership agreements (hereinafter EPAs), bilateral trade agreements (hereinafter BITs), and Transpacific Partnership (hereinafter TPP). The policy space limitation that occurs with the ITRs has given place to clashes between trade liberalization rules and industrial policies implemented by the countries around the world.

The multilevel IEL provisions, i.e. provisions in the multilateral and regional level, have limited the policy space of developing countries that want to implement industrial policies to enhance their own economies. Industrial policy can be defined as "government policies directed at affecting the economic structure of the economy."[1] The IEL provisions in the multilateral and regional levels that constrain countries' sovereignty are shaped and borne from the negotiations and voluntary signing of these countries. This means that policy space erosion voluntarily takes place and is agreed among the states. The reason for developing countries to relinquish their own policy space by signing cumbersome agreements is to remain competitive in the international trade arena and to gain preferential market access especially in developed countries' markets.

[1] Stiglitz, Lin, and Monga, "The Rejuvenation," 1.

Considering the existing rules in the different levels of the IEL, and to remain competitive in the globalizing world economy, developing countries need to optimize their comparative advantages and pursue outward export-led growth with some degrees of protectionism and industrialization. To reach such development paths, countries need to use their policy space to implement appropriate industrial policies that can adjust to their own domestic needs while they still achieve compliance with rules provided by the IEL.

The dynamics of the provisions provided in the multilateral and regional levels of the IEL can be analyzed in light of the export processing zones (hereinafter EPZs). EPZs are industrial polices implemented by countries all over the world. The World Bank (hereinafter the WB) defines EPZs as "fenced-in industrial estates specializing in manufacturing for exports that offer firms free trade incentives and a liberal regulatory environment."[2] Baissac defines them as "demarcated geographic areas within a country's national boundaries where the rules of business and customs procedures are different from those that prevail in the national territory".[3]

As industrial policies, governments grant specific fiscal and regulatory incentives to attract investors in setting up EPZs. Fiscal incentives are granted in the form of import and export tariff exemptions, tax holidays, tax breaks, among other specific fiscal benefits. Regulatory incentives are several, among them flexibilities in labor regulations for investing companies. Waters describes EPZs as a *quid pro quo* between host governments and investing companies. [4] This means that the investing companies, many of them multinational corporations (hereinafter MNCs), can benefit from the fiscal and regulatory incentives granted by the host governments, whereas host governments can benefit from the companies

[2] The World Bank, *Export Processing Zones*, 1.
[3] Baissac, "Brief History of SEZs," 23.
[4] Waters, "Achieving World Trade Organization Compliance," 481.

because EPZs increase investment, alleviate unemployment, give place to technology transfers, and increase foreign exchange earnings, among other developmental benefits. In this way, EPZ schemes involve mainly three actors: the host governments, the investing companies, and the labor force engaged in the activities.

As aforementioned, governments grant specific fiscal and regulatory incentives to promote investment in EPZs. However, these incentives may clash with provisions in the multilateral and regional levels of the IEL. Firstly, the fiscal incentives granted by host governments to the investing companies in EPZs may constitute export subsidies that are prohibited by the World Trade Organization (hereinafter the WTO) Agreement on Subsidies and Countervailing Measures (hereinafter the ASCM). Secondly, the regulatory incentives granted to investors in the form of flexibilities in labor law may lead to violations of core labor standards (hereinafter CLS) provided by the International Labour Organization (hereinafter the ILO) and domestic labor law of countries that have recognized and adopted the CLS in their domestic organs.

The clashes that take place when governments that implement EPZs, as industrial policies, grant fiscal and regulatory incentives in relation with the multilateral and regional levels of the IEL are exemplified in the context of the Central American EPZs. The focus on the region is based on the fact that EPZs have been significant industrial policies that have benefited from the special treatment granted in the WTO. EPZ Central American host governments have enacted flexible laws that offer fiscal and regulatory incentives to attract EPZs and at the same time countries in the region pursue export-oriented trade liberalization policies. Thus they are in need to comply with the IEL, even in an era in which no more special treatment will be granted for some of the countries. Moreover, the single-ever labor case that has been brought to a dispute settlement of an RTA and that has requested an arbitral

panel, has taken place within the United States-Dominican Republic-Central America Free Trade Agreement (hereinafter DR-CAFTA) context. The fiscal and regulatory incentives granted in EPZs as industrial policies, the policy space erosion that takes place when countries voluntarily sign multilateral and regional trade agreements, and the need of EPZ host countries to comply with the IEL will be fully analyzed in the present thesis.

Chapter 1. History of the Post-war Global Trading System

The first part of the present chapter provides a historical review of trade liberalization waves taking place in a second post-war period. It starts from the signing of the General Agreement on Tariffs and Trade (hereinafter the GATT), failures to establish the International Trade Organization (hereinafter the ITO), insight on the ministerial rounds of the GATT, and the creation of the WTO that led to policy space erosion of countries around the world.

The second part of the chapter discusses the phenomenon of proliferating RTAs as part of trade liberalization and development paths countries want to pursue to enhance their economies. It provides a discussion on regionalism and its place in multilateralism. It confirms the trade convergence that RTAs can create, hence the coexistence that is possible between multilateralism and regionalism.

1.1. Multilateralism: The GATT, Trade Preferences, and Differential Treatment of Developing Countries

The most notable contribution by the developed countries after the Second World War in relation to the international economic system was multilateralism. Multilateralism is the rule setting through international organizations based on the fundamental principle of non-discrimination. According to Rodrik, this came to reflect the U.S. preference for legalism over *ad hoc* relationships.[5] In this context multilateralism means that "Rule of enforcement and belief systems would work henceforth through international institutions – the International Monetary Fund (hereinafter the IMF), the WB, and the GATT – rather than through naked power politics or imperial rule."[6] They neither became truly autonomous from the U.S. or other major economic powers, nor they represented a pure extension of these powers. They

[5] Rodrik, *The Globalization Paradox*, 70.
[6] Ibid.

played important rulemaking, rule enforcing, and legitimating roles. Multilateralism was thought to give smaller and poorer nations a voice and protect their interests in an unprecedented way.

Based on the ideal of multilateralism, in the middle of the 20th century, during a second post-war period, many countries around the world with capitalism ideals, such as (and led by) the U.S., sought ways to revive economies by enhancing global trade and setting rules that would lower tariff and non-tariff barriers. The institutional embodiment of this multilateralism in trade during the fifty years subsequent to the Bretton Woods Conference was the GATT. The GATT was signed by 23 nations in Geneva on October 30, 1947 and took effect on January 1, 1948. The GATT is considered to be "the fountainhead of international trade law."[7] It had as a purpose the "substantial reduction of tariffs and other trade barriers and the elimination of preferences, on a reciprocal and mutually advantageous basis."[8]

The GATT achieved its objective to promote trade liberalization mainly through its four legal commitments, sometimes referred to as the four pillars of the GATT: 1) the most-favored-nation (hereinafter MFN) obligation that prohibited signing parties from discriminating against or giving preferences to any other signing party, regardless of whether the latter had made any trade concessions to the former; 2) the national treatment obligation, which required that imports be treated in the same as the domestic like product in so far as domestic taxation; 3) binding obligations to reduce import tariffs; and 4) the general elimination of quotas. These commitments were to be followed equally among all signing parties, with no special treatment to any member, regardless of their development status. The principle of reciprocity ensured to all the signatory countries benefits to ease restrictions, regardless of their participation momentum or economy sizes.

[7] Bhala and Kennedy, *World Trade Law: The GATT-WTO System*, 1.
[8] GATT full legal text, at https://www.wto.org/english/docs_e/legal_e/gatt47_01_e.htm.

The non-discrimination principles are embodied in the GATT Article I providing that "a product made in one member country cannot be treated less favorably than a like product originating in any other country" and in Article III providing that "having once passed the border, foreign goods cannot be treated less favorably than similar domestic goods in terms of internal indirect taxation and non-tax policies."

The GATT became the forum for multilateral trade negotiations (hereinafter MTNs). In fact, the GATT only represented a part of a more ambitious organization, the ITO. The ITO was to include provisions on commodity price stabilization, international antitrust, and fair labor standards. The ITO never came into existence, as it is said "it was embodied in domestic politics."[9] As a result, the GATT was never constituted formally into an organization, as the Bretton Woods institutions were in the IMF and the WB, but it counted with a small secretariat in Geneva. This allowed it to become a *de facto* multilateral forum overseeing global trade liberalization.

During its era, between 1947 and 1995, eight negotiating Rounds took place.[10] Each round had the objective of liberalizing trade by reducing tariffs on trade. Later rounds had additional objectives of formalizing the existing trade rules, expanding GATT's scope of coverage, and eliminating non-tariff barriers. In general, all of the rounds successfully managed to eliminate a substantial part of the import restrictions. Table 1 illustrates the eight GATT Rounds and subjects covered in each.[11]

[9] Rodrik, *The Globalization Paradox*, 71.

[10] Kennedy, "Introduction to the GATT-WTO System," 5 and Jackson, "Structure of the WTO/GATT System," 292-293.

[11] Kennedy, "Introduction to the GATT-WTO System," 5-6.

Table 1. GATT Rounds

Year	Place/Name	Subjects covered
1947	Geneva Round	Tariffs
1949	Annecy Round	Tariffs
1950-1951	Torquay Round	Tariffs
1955-1956	Geneva Round	Tariffs
1961-1962	Dillon Round	Tariffs
1964-1967	Kennedy Round	Tariffs and Antidumping
1974-1979	Tokyo Round	Tariffs, non-tariff measures, framework agreements
1986-1994	Uruguay Round	Tariffs, non-tariff rules, services, intellectual property, dispute settlement, textiles, agriculture, creation of the WTO

Source: Author, adapted from Kennedy (1998), 5-6.

The main focus from the Geneva Round in 1947 to the Dillon Round in 1961 was the progressive reduction of tariffs and the elimination of quotas. The Geneva Round of 1947 achieved 45,000 tariff concessions affecting one-fifth of world trade.[12] In the sixth round, the Kennedy Round, existing customs duties were reduced an average of 35 percent.[13] World trade grew at an average annual rate of almost 7 percent between 1948 and 1990, considerably faster than anything experienced to date.[14] Rodrik recognizes that "If there was an era of globalization, this was it."[15]

However, as signatory countries included both developed and developing countries, all of them living in a same-conditioned post-war world reality, the developing countries began to show their dissatisfaction with the world trade pattern. Trade liberalization was only

[12] Ibid.
[13] Ibid.
[14] Ibid.
[15] Rodrik, *The Globalization Paradox*, 71.

felt in some areas of the world, while other areas were completely left out of the multilateral agreements. Within the GATT, some sectors were likewise left out of the trade liberalizing provisions, such as agriculture and most service sectors, including insurance, banking, construction, utilities, and the like. The manufacturing sector was liberalized. Nonetheless, this sector began to be affected when low-cost, highly productive exporters obtained protection from existing trade rules. Industrial policies began to be felt contentious; soon they were to be tackled in a serious ways on the GATT.

Baldwin recognizes the "pragmatic approach which was not closely tied to basic GATT principles and which proved to be successful in contributing to long-run trade liberalization."[16] This was the acceptance by GATT of the Generalized System of Preferences (hereinafter GSP) for developing countries. This scheme emerged as a serious proposal in the first United Nations Conference on Trade and Development (hereinafter the UNCTAD) in 1963 as part of the efforts at that time to narrow the then widening income gap between developed and developing countries. The proposal called upon developed countries to set import duties at lower rates on manufactured goods if they were produced in developing countries in contrast to developed countries. The GSP template to allow the preferential treatment was established under UNCTAD auspices in 1968.

The main role of unilateral preferences was to support infant industry policies. The increase in manufactured exports due to preferential access to markets was argued to be one element to support industrialization. A number of developed countries promptly agreed to introduce the scheme for a selected number of products. The EU and the U.S. passed legislation establishing their GSP schemes in 1971 and 1974 respectively. Japan, Canada, Australia, and several other countries implemented their own GSP schemes. Under the GSP,

[16] Baldwin, "Pragmatism Versus Principle in GATT Decision-Making," 37.

developed countries offer preferential treatment on a non-reciprocity basis, e.g. none or low import tariffs, to products imported from developing countries. The developed countries that grant this preferential treatment determine the countries and conditions to be included in their schemes.

To implement GSP in the GATT, a waiver was needed. This was because it was inconsistent with the non-discrimination principle provided in GATT Article I. To allow such waiver, the GATT system, in its Tokyo Round (1973-1979), enacted "the differential and more favorable treatment reciprocity and fuller participation of developing countries."[17] Also known as the Enabling Clause (L/4903), this decision allowed members of the GATT to derogate from the MFN in favor of developing countries. Developed countries would be able to grant special treatment to developing countries.

The Enabling Clause gave permanent legal cover to the GSP and to the Special and Differential Treatment (hereinafter SDT) under the GATT. It also covered issues related to regional and global preferential agreements and to the special treatment granted to least-developed countries (hereinafter LDCs). According to Keck and Low,

> "The Enabling Clause restated the principal of non-reciprocity and further stated that developing countries, according to their capacities, could make contributions and negotiate to gradually improve their situations and lead in this way to progressive development. This was the notion of graduation."[18]

At present, the developed countries still grant GSP programs. For instance, the most important development in unilateral preferential treatment since the establishment of the U.S. GSP is the implementation of special programs destined to specific regions, such as the

[17]The Enabling Clause, at https://www.wto.org/english/docs_e/legal_e/enabling1979_e.htm.
[18] Keck and Low, "Special and Differential Treatment in the WTO," 4.

Caribbean Basin Initiative (hereinafter the CBI) (1984),[19] the Caribbean Basin Trade Partnership Act (hereinafter the CBTPA) (2000),[20] the Andean Trade Promotion and Drug Eradication Act (hereinafter the ATPDEA) (1991),[21] and the African Growth and Opportunity Act (hereinafter the AGOA) (2000),[22] among others. The EU GSP scheme is considered more complex than the U.S. regime but with the same preferential principles. Non-compliance of GSP rules leads to unilateral suspension of trade benefits to the developing countries. The Enabling Clause represents the main WTO legal basis for the GSP schemes. It also serves as the legal basis for RTAs among developing countries and for the Global System of Trade Preferences (hereinafter GSTP), which promotes preferential treatment in trade among developing countries.

Besides the Enabling Clause, an agreement that would also deviate GATT main principles was the Multi-Fibre Arrangement (hereinafter the MFA). The MFA, introduced in 1974, consisted of a set of bilaterally negotiated quotas on exports from developing nations. Its purpose was mainly to impose quotas on the amount of textiles and garments that the developing countries could export to developed countries. Professor Matsushita discusses the welfare effects of quotas as follows:

> "The welfare effects of quotas for domestic countries would be essentially identical to tariffs. A quota increases the welfare of domestic producers and causes deadweight losses. A quota, by its nature, is more certain than a tariff because the importing country controls the number of imports."[23]

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[19] CBI available at: https://ustr.gov/issue-areas/trade-development/preference-programs/caribbean-basin-initiative-cbi

[20] CBTPA available at: http://www.cbp.gov/trade/priority-issues/trade-agreements/special-trade-legislation/caribbean-basin-initiative/cbtpa

[21] ATPDEA available at: http://web.ita.doc.gov/tacgi/eamain.nsf/6e1600e39721316c852570ab0056f719/53018ab5e2d8426a852573940049684c?OpenDocument

[22] AGOA available at: http://trade.gov/agoa/

[23] Matsushita, Schoenbaum, and Mavroidis, "Tariffs, Quotas, and other Barriers," 270.

The MFA allowed developed countries to adjust to imports from the developing countries establishing selective quantitative restrictions when surges in imports of particular products caused damage. Textile and garment EPZs could ensure specific quotas to be exported to developed countries' markets and thus competition was not as fierce. The 1980s witnessed the spread of voluntary export restraint (hereinafter VER), arrangements whereby typically Japanese exporters of autos, steel, and some other industrial products undertook to keep their exports within specific quotas.

In this way GATT rules, trade preferences, and differential treatment allowed developing countries to pursue their industrial policies. The GATT sought the most possible amount of trade among the countries, unlike the WTO, which currently seeks trade liberalization at its maximum. Developing countries could recourse to various GATT clauses that allowed them to resort to limitations on imports, virtually on a permanent basis. During this period, developing countries could focus on national efforts directed at fostering industrialization and economic growth. There was no external discipline, as the GATT lacked a real enforcing body and power. The developing countries, either inward or outward looking type, were free to deploy a vast range of industrial policies to transform their economies.

It is said that the "GATT's purpose was never to maximize free trade. It was to achieve the maximum amount of trade compatible with different nations doing their own thing."[24] Rodrik refers to it as "spectacularly successful."[25] Thomas and Trachtman identify three important factors linked to trade liberalization and development in the GATT, particularly in the evolution of the concept of SDTs. The authors identify the factors as follows: "1) non-reciprocity for developing countries (after the Enabling Clause), 2) permissive protection for developing countries against the promotion of domestic

[24] Rodrik, *The Globalization Paradox*, 75.
[25] Ibid.

liberalization and institutional reform, and 3) increased market access for developing country products and services in developed country markets."[26] However, with the establishment of the WTO, the situation for developing countries changed.

1.2. The Establishment of the WTO and Policy Space Erosion of Countries

Following the Tokyo Round, the GATT Uruguay Round launched in 1986 gave birth to the WTO in 1995. The WTO did not replace the GATT; rather it institutionalized it as an international organization. The establishment of the WTO is considered to be the greatest reform in international trade since the Second World War and the establishment of the GATT. Rodrik states, "the WTO marks the pursuit of a new kind of globalization that reversed the Bretton Woods priorities: hyperglobalization, economic globalization, the international integration of markets for goods and capital (but not labor), became an end in itself, overshadowing domestic agendas."[27]

Globalization became an imperative, requiring all nations to pursue a common strategy. The WTO, besides maintaining the GATT principles and the agreement *per se*, included a package of agreements. This package of agreements was characterized by a Single-Undertaking of "take it all or leave it all". This meant that every item of the negotiation was part of a whole and invisible package and could not be agreed separately item by item. In other words, "nothing would be agreed until everything was to be agreed."[28] These conditions would represent "a list of burdensome and strict obligations that the developing countries would have to comply with within the system."[29]

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[26] Thomas and Trachtman, *Developing Countries in the WTO Legal System*, 3-10.

[27] Rodrik, *The Globalization Paradox*, 76.

[28] For the Single-Undertaking, see "How the negotiations are organized under the WTO", at https://www.wto.org/english/tratop_e/dda_e/work_organi_e.htm.

[29] Janow, Donaldson, and Yanovich, *The WTO: Governance, Dispute Settlement & Developing Countries*, 196.

The Single-Undertaking resulted in a "grand bargain for the developed and developing countries."[30] The Uruguay Round was based on such a grand bargain. "Developing countries accepted a set of new disciplines in a package that contained many areas: services, investment, and intellectual property. Developing countries' gain in the grand bargain was the elimination of the MFA, the outlawing of VERs, the inclusion of agriculture into the WTO, market access and institutional reforms which were to be carried out by the developed countries."[31]

With such aggressive pursuit of trade liberalization as a common strategy, the WTO brought a problem in differences of priorities and capacities across the WTO Membership. There were large differences in terms of resource capacity constraints and national trade policy and investment priorities. Hoekman recognizes that the "adjustment burden of new rules that the establishment of the WTO brought, mainly fell in developing countries, as such rules reflected the *status quo* in industrialized countries, a best practice."[32] The author also emphasizes that the "WTO was not established to provide development for countries, but to pursue trade liberalization."[33]

As aforementioned, at the time of the GATT, the Enabling Clause allowed for GSP schemes and SDT for the developing countries. This gave developing countries preferential market access and limited reciprocity in negotiating rounds considering their development situations. It also gave developing countries more freedom to use industrial policies that would otherwise have been prohibited. The premise behind SDT in the WTO had the same purpose. Like in the GATT, they were couched on the belief "that trade liberalization under MFN auspices does not necessarily help achieve growth and development in so far as

[30] Ostry, "The Uruguay Round North-South Grand Bargain," 282.
[31] Hoekman, "Operationalizing the Concept of Policy Space in the WTO," 410.
[32] Ibid.
[33] Ibid.

industries in developing countries need to be protected from foreign competition for a period of time."[34]

Therefore, the WTO did recognize the SDT but "the notion of SDT was largely reduced to transitional periods for developing countries."[35] The Doha Round granted longer transition periods for developing countries' SDT. Nonetheless, this same approach used in the Uruguay Round "is now recognized as an inadequate response, as they were imposed arbitrarily and did not consider, nor did they remain open for the possibility to consider, the specific context of each developing member country."[36]

Singh reaffirms that the concept of SDT was radically changed with the establishment of the WTO. SDT under the GATT allowed nations to follow a different path toward development that did not necessarily require each nation follow the rules. The WTO was established with a Single-Undertaking that required nations to endorse and comply with every single agreement under the WTO. "The SDT was reconceptualized to be a special treatment to make sure that nations comply with the Single-Undertaking, rather than special treatment to steer clear of certain provisions until a certain level of development is reached."[37]

The pursuit of trade liberalization at its maximum, the Single-Undertaking that countries needed to follow in order to become members of the WTO, and the new terms from which SDTs were to be possible created a significant change in the nature of developing country involvement in the system. At this point, the term "policy space was coined."[38] Policy space means "letting countries do what they want, while in some unspecified way allowing these countries to benefit from binding commitments of others."[39] The policy space debate

[34] Ibid., 406.
[35] Bhagwati, "Fifty Years: Looking Back, Looking Forward," 58.
[36] Hoekman, "Operationalizing the Concept of Policy Space in the WTO," 406.
[37] Singh, "Special and Differential Treatment," 233-234.
[38] Janow, Donaldson, and Yanovich, *The WTO*, 197.
[39] Ibid., 198.

encapsulates the concern that the Single-Undertaking, combined with the extension and deepening of trade rules, "has led to the adoption by many developing countries of obligations that are less than development friendly."[40] Unlike the GATT, which allowed countries to implement freely developmental policies, the WTO came to impose restrictions on certain policies that would hinder trade liberalization and that would not comply with the MFN principle of the GATT. Concerns on the WTO's right to regulate for development arose. Main concerns were the constraints that now developing countries had to face in their freedom to implement industrial policies.

Rodrik recognizes such constraints by stating that "all successful cases of development in the last fifty years had been based on creative policy innovations. The creativeness combined trade policy with industrial policy."[41] He reaffirmed that "trade liberalization was to be a gradual process."[42]

As can be understood, GATT obligations did not restrict freedom of developing countries to implement industrial policies. This changed in the Uruguay Round and with the creation of the WTO. With the WTO, developing countries have greater commitments, standing, and stronger dispute settlement that would make them comply with the new set of rules.

The Uruguay Agreements that the WTO offered decreased the special treatment granted in the GATT. The WTO commitments and rules came to deny many developing countries access to policies that foster economic and industrial development. The rules under the WTO represented binding obligations that the developing countries had to comply with. The Dispute Settlement Understanding (hereinafter DSU) would make the WTO obligations

[40] Ibid., 197.
[41] Rodrik, "How to make the Trade Regime Work," at http://ksghome.harvard.edu.
[42] Ibid.

binding, enforceable, and judicially applicable. Therefore, the substantive changes brought with the WTO were to be enforceable by the DSM. The obligations limited developing countries' policy space and less flexibility was encountered.

The Sao Paulo Consensus, forged in the summer of 2004 at the eleventh meeting of the UNCTAD, explicitly recognized the policy space erosion under various international agreements and calls on nations to "take into account the need for appropriate balance between national policy space and international disciplines".[43] Developing countries have willingly signed many of these agreements. However, the concerted efforts that developing countries are conducting to make sure that no further erosion takes place and that some space can be restored is evidence of the fact that many countries feel that mistakes were made during the last trade round.

In relation to subsidies, which would have a direct impact on EPZ schemes implemented by developing countries, the ASCM extended the prohibition of export subsidies on trade in goods, and introduced a prohibition on import substitution subsidies. The import substitution subsidies are the ones governments pay contingent upon the use of domestic over imported goods.[44] Likewise, the Agreement on Textiles and Clothing (hereinafter ATC) that put an end to the GATT-MFA would also have a direct effect on textile EPZs. The ATC gave a transitional period of ten years for the ultimate removal of textile quotas. With the end of the ATC in 2005, developing countries highly dependant on textile exports would need to seek ways to stay competitive with other strong exporters to enter developed countries' domestic markets.

[43] UNCTAD, *Sao Paulo Consensus*, 3.

[44] Chapter 5 of the present dissertation provides deeper insights on the ASCM provisions, export subsidy prohibition, and SDT for developing countries.

1.3. The Rise of Regionalism and its Place in Multilateralism

While multilateralism was reflected in the GATT and WTO provisions and trade liberalization was pursued at its maximum, especially after the establishment of the WTO in 1995, regionalism was another phenomenon that was in parallel gaining momentum. Regionalism addresses challenges similar to those faced by the multilateral trading system (hereinafter the MTS) and if agreements are ratified within regionalism, they may have impact on the multilateral process. There is in fact a high degree of interaction between the regional and multilateral processes. Regionalism contributes to an acceptance of the need for international rules on the part of national governments and interest groups. The need for international rules and adjudication of rules follows recognition that national policies affect the balance of benefits in international commercial relations. The positive multilateral balance is, however, often too remote from national interest groups for them to accept the need to change established state or national practices. The benefits are generally too remote and uncertain when compared with the immediate costs. In regionalism the impact of interdependence is more immediate. Interest groups and politicians may therefore more easily recognize the need to accept international rules and disciplines.

The Organisation for Economic Co-operation and Development (hereinafter OECD) states that in Europe, high levels of interdependence have contributed to a broad acceptance of the need for international agreements by industry, trade unions, environmentalists, and national regulatory agencies, as is the case in competition policy.[45] In North America, the North American Free Trade Agreement (hereinafter NAFTA) brought home the impact of interdependence on labor and environmental interests, and the political need to address the problems felt to result from differing national labor and environmental policies if the benefits

[45] OECD, *Regional Integration and the Multilateral Trading System*, 62.

of regionalism were to be achieved. NAFTA has highlighted awareness that trade liberalization has immediate implications for national policies and national sovereignty and has heightened the awareness for such interdependence.[46]

Regionalism has also contributed as a learning process in international trade policy, not only for governments, but also for regulators and interest groups. In the past, MTNs have been remote diplomatic exercises carried out by experts within conference rooms in Geneva. Many criticize that decisions have only been taken by the most powerful developed countries in the WTO's Secretary General green-colored room, and thus consider these negotiations as "green room politics" and as a crisis of representation in the WTO.[47] The increased awareness in public opinion of the direct impact of trade liberalization on national policies has also led to a great role for lobby groups, thereby making the process of the MTS more complex. RTAs today have a fundamental role in promoting trade liberalization and development. They represent agreements on negotiations by interested countries aimed at covering or clarifying some issues beyond the MTS.

Serra describes reasons why RTAs gained momentum in the early 1990s.[48] Reasons were both economical and institutional. One of the economic reasons that the author describes is that "small and protectionist countries had to complement their internal efficiency gains, which were the product of import substitutions and infant industries, with trade and external market access. Institutional reasons were due to the complexity and deadlocks in the MTS.

[46] Ibid.

[47] Green Room meetings are "small gatherings of representatives invited by the Director-General. They are designed to provide the basis for a consensus on critical negotiation issues that can be brought to the WTO membership. They are highly criticized by the developing countries." See Kent, "Green Room Politics and the WTO's Crisis of Representation," at http://pdj.sagepub.com/content/9/4/349.abstract.

[48] Serra Puche, "Regionalism and the WTO," 124.

Some of the countries could not 'wait and see' the outcomes of the stagnated negotiations, therefore they engaged in regional trade initiatives and negotiations."[49]

When RTAs first started to proliferate, there were ongoing debates whether RTAs would lead to trade convergence or to trade divergence. Today the MTS accepts and recognizes RTAs as being supportive to the MTAs. The WTO recognizes that RTAs and economic integration can benefit countries. GATT's Article XXIV allows RTAs to be set up as a special exception to the MFN principle, provided that certain strict criteria are met. The aim of RTAs should always be to help the freer flow of trade among countries. RTAs should always complement the MTS.

Article XXIV of the GATT states that if a free trade area or customs union is created, duties and other trade barriers should be reduced or removed on substantially all sectors of trade in the group. Similarly, Article V of the General Agreement on Trade in Services (hereinafter the GATS) provides for economic integration agreements in services. "On February 6, 1996, the WTO General Council created the Regional Trade Agreements Committee. Its purpose is to examine regional groups and to assess whether they are consistent with WTO rules."[50] The WTO states the following:

> "RTAs have become increasingly prevalent since the early 1990s; as of April 7, 2015, some 612 notifications of RTAs (counting goods, services, and accession separately) had been received by the GATT/WTO. Of these, 406 are in force. WTO figures correspond to 449 physical RTAs (counting goods, services, and accessions together), of which 262 are currently in force."[51]

Many agree that RTAs, rather than diverting trade in the world, may converge and serve as stimuli for the MTS. RTAs frequently go beyond the WTO provisions. They do so

[49] Ibid.

[50] WTO homepage, 2015, at: https://www.wto.org/english/thewto_e/whatis_e/tif_e/bey1_e.htm.

[51] WTO homepage, 2015, at: https://www.wto.org/english/tratop_e/region_e/region_e.htm.

essentially by containing provisions that are more far-reaching in areas such as services, labor, investment, competition policy, trade facilitation, government procurement, intellectual property rights, contingency protection, and the environment.[52] Though RTAs are more far-reaching than MTAs, RTAs and MTAs have a nature of complementarities.

RTAs have provided an opportunity for interest groups and decision makers to come to terms with the kind of trade-offs that may have to be made when trade and industrial policies clash. The experience and expertise gained may then be employed in wider multilateral negotiations. RTAs may therefore have a positive effect on multilateral processes by helping to equip the interested parties with models and skills needed to reach wider agreements. RTAs may have contributed substantially to the increasing political interest in the trade issues that they cover.

The OECD reports that RTAs have generally proved to be compatible with multilateralism.[53] They have had a positive overall impact on international trade as well as on the MTS and its regulatory framework. They have not stood in the way of further multilateral liberalization and rather have contributed significantly to prepare public opinion and private interests to accept a more competitive environment. RTAs have contributed to the achievement of a faster and greater degree of world trade liberalization. Regionalism also tends to enhance the market power of the entity compared with that of its individual members.

Today, despite more countries acceding to the WTO, RTAs have proliferated at an unexpected pace. RTAs have been signed in various forms of bilateral and multilateral ITRs. Some forms of the reciprocal preferential trade agreements include FTAs, BITs, EPAs, and customs unions, among others. RTAs continue to grow, as well as the complexity of their

[52] The OECD provides with a comprehensive analysis on these areas in which RTAs go beyond WTO provisions. However, the analysis was done when scholars and practitioners still held debates as if RTAs are trade convergent. Today there is a general acceptance that RTAs are trade convergent. See OECD, *Regionalism and the Multilateral Trading System*, 14-20.

[53] OECD, *Regional Integration and the Multilateral Trading System*, 88.

provisions as they have the capacity to address multiple dimensions as compared to the MTS. Many countries sign more than one RTA and at times RTAs interconnect with one another. This interconnection allows for greater trade liberalization and regional integration. RTAs promote trade around the world. Prominent examples of RTAs signed in the 1990s include the European Economic Community (hereinafter EC), the Association of Southeast Nations (hereinafter ASEAN) Free Trade Area (hereinafter AFTA), the Andean Community, and the South Asian Free Trade Agreement (hereinafter SAFTA).

The success of RTAs will depend on various factors and particular context of the agreements. Common factors that have led to RTA success are the coverage and degree of liberalization. Other more successful RTAs cover and implement issues beyond tariff reductions, such as trade facilitation, investment, competition policy, labor, environment, intellectual property, and dispute settlement. RTAs also are effective when they are designed to align with economic needs and reforms of the country members. Therefore RTAs can be designed by the negotiating parties in a way that the agreement harmonizes with EPZs as industrial policies that pursue economic growth and development.

Chapter 2. Industrial Policy Revival and Policy Space Erosion of Developing Countries

With the establishment of the WTO in 1995, Smith argues that the Washington Consensus continued to erode and that something of a backlash against it took place. The author states that part of the backlash was a return to arguments for infant-industry protection as a basis for export-led growth.[54] With this argument there seems to be consensus that infant-industry protection in developing countries is not necessarily adverse to development. Nonetheless, important factors to determine are the specific industries that are being protected, the duration and magnitude of the protection, and the impact that the protection will have with counterparts in the international trade arena.

The present chapter discusses the renewed interest in industrial policy in a time in which countries' policy space has been eroded as they have engaged in MTAs and RTAs. Developing countries have shifted their interests of pure export industrialization that surged in an era when protectionism of infant industries was highly criticized due to promotion of trade liberalization. This section also identifies and conceptualizes EPZs as significant export-oriented industrial policies of developing countries since they first started to be implemented in the late 1950s until the present day. It will reference the Newly Industrialized Countries (hereinafter NICs) implementation of export subsidies in a GATT era and will refer to EPZ implementation in a WTO era of reduced policy space.

2.1. Industrial Policy and Proactive Trade

Today debates as to whether industrial policy can be beneficial or detrimental for developing countries have been revived.[55] While there still seem to be solid reasons for developing countries to liberalize at some point in their development stages, "there exists a

[54] Smith, *Industrial Policy in Developing Countries*, 14-31.
[55] Lall, "Rethinking Industrial Strategy," 33-68.

legitimate basis for limiting the impacts of imports, particularly if those imports are heavily subsidized to allow for development of sustainable and competitive national industries, or to ease a process of economic reform or transition."[56] The industrial policies that are now scorned by the developed nations in the set of MTAs are the very policies that were so essential to industrialized development for the now developed countries. Even today, many developed countries recognize the significant role of industrial policies to protect their strong domestic manufacturing sectors.

Within trade liberalization, Professor Jackson reaffirms the need for industrial policy.[57] The Tokyo Round of MTN in the context of the GATT brought to the international scene new legal obligations on certain governments concerning their own governmental purchasing procedures, concerning their methods of establishing safety and other standards of products, and concerning their use of tax or regulatory measures which may affect the competitive nature of their exports. According to Professor Jackson, a key question for the future is, "how can the necessary advantages of coordination and harmonized decision-making be obtained in the world, while at the same time reserving for the smallest possible unit of government, the decision-making authority that it needs to be responsive to constituents."[58]

In the search for an appropriate policy or mix of policies with which to try to alleviate some of these uncertainties, and to effectively manage this new world interdependence, "sovereign nations have been taking a variety of approaches, some of which are proving inconsistent with approaches of other nations and inconsistent with broader objectives for an

[56] Thomas and Trachtman, *Developing Countries in the WTO Legal System*, 6.
[57] Jackson, *Emerging Standards of International Trade and Investment*, 3.
[58] Ibid.

appropriate evolution of a technique of managing interdependences."[59] Calls for industrial policy, that is, measures designed to protect the domestic economy, "were as frequently heard in international conferences as calls for a liberal trade policy."[60] The present study considers that industrial policy can be effective if its objective is to create and strengthen domestic markets and foster innovation. Purely export-oriented strategies are becoming less effective.

Successful development experiences have generally been associated with structural transformation. The manufacturing sector plays a leading role in the structural transformation. Activities in this sector offer a great potential for innovation and increasing returns to scale.[61] Manufacturing activities are labor intensive. Therefore, given the right wage and labor market policies productivity growth has the potential to benefit a large proportion of the population. The UNCTAD states that "the central development challenge for policymakers should be focused to achieve an intersectoral shift of productive employment toward high-productivity activities combined with productivity growth within each economic sector."[62]

Success in achieving structural transformation and the policy strategies contributing to that success has varied significantly across countries. The pace of structural transformation in developing economies, such as the NICs in East Asia, especially the Republic of Korea and Taiwan between the 1960s and the 1990s, and China since the 1990s, has outperformed those in other developing countries.

Today, the renewal in this interest to implement industrial policies to achieve structural transformation has been strongly affected by the trade liberalization trends in global trade and in the evolving IEL. Mainly, the accession of various countries to the WTO and

[59] Ibid., 4.
[60] Ibid., 11.
[61] UNCTAD, Trade and Development Report, 81.
[62] Ibid.

their voluntary signing of RTAs has created such clashes with industrial policy implementation.

Provisions in the MTS significantly restrict the conduct of trade and industrial policies of all WTO members. Further restrictions followed with the proliferation of RTAs and international investment agreements (hereinafter IIAs), many of which include rules and regulations that go beyond the MTAs. Policymakers should skillfully make use of the proper policy space available to support their own manufacturing sectors and implement industrial policies that can lead them to development.

The UNCTAD recognizes two types of industrial policies: "vertical" or "selective" industrial policies and "horizontal" or "functional" industrial policies.[63] A selective industrial policy refers to measures aimed at diversifying the production structure and contributing to creating capacities in new economic sectors or in new types of activities. These measures include support in the form of sector specific subsidies, tariffs and investment-related performance requirements that have generally been associated with successful industrialization. They also include measures that target variations in different sectors' potential to help countries catch up with and then push beyond the technological frontier through direct support for innovation and learning. Functional industrial policies aim at a general improvement of economic conditions for all sectors and firms, such as improving a country's infrastructure, regulatory and competition environments, and the general business climate.[64]

In today's globalizing world, it is the way of use and implementation of industrial policies that may fall into the IEL non-compliance. However, the UNCTAD reconfirms this

[63] Ibid., 92.
[64] Chang, "Industrial policy," 83-109.

study's view that the constraint does not imply interdiction.[65] Manufacturing sectors can be fostered; developing countries may combine creative market forces with state activities to enhance domestic manufacturing sectors and improve living standards of people.

2.2. The Duality Principle of Import-Substitution Industrialization Strategy and Export-Oriented Industrialization Strategy

The trade preferential benefits and the SDT granted to developing countries during the GATT allowed these countries to maintain industrial policies to boost up their economies. Each country could make use of their own policy space while still being part of the MTS and complying with its provisions. The present section provides a theoretical review of industrialization strategies used by countries to enhance their economies during the GATT era. Development strategies from import-substitution industrialization (hereinafter ISI) strategy with a transition to export-oriented industrialization (hereinafter EOI) strategy characterized development policies worldwide. EPZs represented effective implemented industrial policies under both strategies that complied with the MTS.

During the 1950s and 1960s Raul Prebisch and Hans Singer elaborated a main argument that "developing countries needed to foster industrial capacity in non-traditional manufactures both to reduce import dependence and to diversify away from traditional commodities that were subject to declining terms of trade in the long term and adversely volatile prices in the short term."[66] Part of the recommended policy prescription was high trade barriers to protect infant industries – i.e. ISI. "At the same time it was recognized that exports were important as a source of foreign exchange and that the local market was generally too small for domestic industry to capture economies of scale that could accompany

[65] UNCTAD, Trade and Development Report, 93
[66] Todaro and Smith, *Economic Development*, 598.

industrial expansion."[67] Therefore for a long time two contrasting industrialization strategies existed the ISI and the EOI.

In history governments showed preference for either one, depending on the prevailing economic circumstances of the moment and their internal context. In fact, no model was put into practice without allowing some exceptions and nowhere was it possible to observe a model in a pure state. Pragmatism prevailed and while theorists' approach to the problems sounded dogmatic, the measures taken by the countries were essentially empirical and based on their own context.

The ISI arose during the Great Depression in 1929, when any process of economic development seemed to postulate the export of manufactured goods. The Great Depression marked a breaking point with most Latin American countries experiencing a sudden drop in their exports, substantial outflows of capital, and a sharp deterioration in their terms of trade with the outside world. Later on, the Second World War made it difficult to supply the countries concerned with manufactured goods, both because of uncertainties of transfer and because of the collapse of production among their traditional suppliers. In addition, these countries found their debt increasing and their import-financing capacity decreasing due to the fall in international demand for many of the primary products they exported. Consequently, some of the Latin American countries turned to a more realistic policy of import substitution. This policy was systematically applied from the 1950s. The trend was also accompanied by an increasing determination on the part of the countries concerned to be freed from too great dependence on the outside world. A policy of diversification through an industrialization effort supported by infant industry protection seemed the right thing to do at that time.

[67] Ibid., 599.

Todaro and Smith define ISI growth strategy, maintaining that "Import substitution entails an attempt to replace commodities that are being imported, usually manufactured consumer goods, with domestic sources of production and supply."[68] The explanation points out that import substitution takes place when tariff barriers and quotas are erected on certain imported commodities, and then local industries are set up to produce these same commodities. "Initial costs of production may be higher, but the economic rationale is that the industry "will eventually be able to reap the benefits of large-scale production and lower costs (the so-called infant industry argument for tariff protection) or that the balance of payments will be improved as fewer consumer goods are imported."[69] Other types of barriers are exchange rate controls, special preferential licensing for capital goods imports, and subsidized loans to local infant industries. At the end it is expected that the infant industry will grow and compete in the world markets. The main goal of ISI is to promote local industries to replace the foreign produced manufactured products that are consumed as imports. In the manufacturing process several stages of production are involved and these numbers of stages are a reflection and function of the complexity of the final product. One of the key successes for ISI relies on the fact that individual factories should achieve economies of scale of production which could be reflected on the market size, that is the number of consumers or population among others, and purchasing power.

As a comparison of ISI performance in Asia and in Latin America, it is recognized that the Asian countries took more advantage of the opportunities that were presented by the international markets and that they tried to maximize the benefits of modernization. Asian markets relied on a very strong state intervention to protect their home markets. Asian politicians were willing to risk dependency with a strong state. On the other hand, Latin

[68] Ibid., 623.
[69] Ibid., 624.

American countries, such as Brazil, were much more concerned about the threat of dependency. They saw international market forces as a threat. Thus they focused on developing internally. Relevant to mention is that the Asian model was more of ISI but at the same time export-oriented. Latin America, on the other hand, more focused on serving its own internal markets. The Asian model results were more successful. They focused on producing goods and services for the world markets; they could focus on continuously improving the quality of their goods and seek ways to be more efficient in producing at lower costs. Latin America focused on local markets seeking to protect themselves from global competition, not facing global pressures of quality and prices. At the end, these industries fell behind in technology and in business practices.

Cases of ISI varied between the developing countries in the world. However, common factors among them were: ISI proved costly for many; the economies that adopted ISI strategy could not easily obtain internal structural effects, because of their own context and what they were going through. Internal structural effects refer to the effects that take place when countries have their own internal industries with sufficient technology, and the necessary skilled labor force required to help keep up an infant industry or an existing industry within that economy.

Todaro and Smith describe five undesirable outcomes of the ISI strategy as follows:

> "The first one is that behind the protection of tariff walls, the domestic industries might remain inefficient and costly to operate. The second is that the main beneficiaries are the foreign firms who could invest in the country to enhance local production and who benefit from tax exemption and investment attractions in conjunction with local entrepreneurs who could jointly invest and support the industry. The third is that most of the ISI strategy has been possible by government-subsidized importation of capital goods and intermediate products by foreign and domestic companies. The fourth is the negative impact on traditional primary product exports giving place to overvalued exchange rates, makes these local farmers less competitive in world markets. The fifth reason is that even though forward and backward linkages are attempted with ISI strategy, usually they will not happen since

at times small industries will rely on input coming from external sources."[70]

The authors portray that the five outcomes became evident when the Asian and the Latin-American countries had ISI strategies.[71]

Between the 1950s and 1970s, economic planners in many developing countries such as Ireland, Taiwan, South Korea, the Philippines, Malaysia, Sri Lanka, Brazil, among others, shifted the industrialization strategy from ISI to EOI. EOI has several economic policies, including the setting up of EPZs. In the broadest sense, the strategy stresses three basic elements: emphasis on the rapid expansion of exports (rather than control of imports), free international trade (and the dismantling of protection), and a free open door environment for foreign companies in the less developed countries."[72]

Conventional wisdom in trade policy thinking had started to swing away from import substitution and towards favoring greater export orientation by the time the Tokyo Round took place in 1973. Janow, Donaldson, and Yanovich state the following:

> "The inherent limitations and trade-distorting effects of excessive reliance on import substitution were becoming better understood. The move towards a more neutral space in respect of trade policy incentives implied opening up more to import competition as well as removing the policy bias against exports. From the institutional perspective the focus was to increase developing countries' own trade policies as well as market access for their exports."[73]

Basile and Germidis explain the transition that developing countries had by turning to an export-oriented industrial policy, stating that:

> "In 1975, 51 out of 144 developing countries had turned resolutely to an export-oriented industrial policy, and very soon for most of the Third World countries foreign trade became the mainspring of any industrial strategy. The new industrial policy orientation was based on the availability of a plentiful supply of cheap labor. The

[70] Ibid., 626-27.
[71] Ibid.
[72] Asia Partnership for Human Development, *Export Processing Zones in Five Countries*, 22.
[73] Janow, Donaldson, and Yanovich, *The WTO*, 194.

> countries that had the greatest success in this new path were those that could recruit plenty of disciplined workers, drawn from an agricultural or rural sector that had prospered through rationalizing and modernizing farming techniques. The experience of Taiwan, Mexico, Korea, and Brazil might be mentioned here, although different procedures were used in each country."[74]

EOI did not necessarily imply less state interference than in the ISI process. State action simply followed other channels. Intervention was henceforward mainly at the levels of infrastructures, incentives to enterprises playing a leading role in the industrialization process, differentiated or selective openings for foreign investment, redefinitions of customs and trade policy objectives, sound management of labor force, among other specific tasks. For example, economic policies of the states at the international level played a strong role in the establishment of EPZs. Policies were destined at promoting exports as development strategies.

Basile and Germidis state the duality that takes place with EOI strategy as follows:

> "The increasing interest taken by many developing countries in policies to attract export-oriented investment is prompted by a dual concern. The aim is on the one hand to attract foreign investment, which is expected to provide foreign outlets, create jobs, transfer technology and know-how, generate inflow of foreign exchange, etc., and on the other hand, to promote a whole process of specifically national industrialization in a protected domestic market. This dual attitude has led to the preparation and adoption of foreign direct investment systems of dualistic nature. It contains an inherent basic contradiction, insofar as the host country, in dissociating the domestic market from the export market, is not certain to obtain from the foreign investment the advantages which it could legitimately expect."[75]

In the duality process, countries combined protectionism and infant industries with export subsidies and targets, credit allocation, local content rules, among other strategies to build their industrial capabilities, disciplining the process by strong export orientations.

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[74] Basile and Germidis, *Investing in Free Export Processing Zones*, 17-18.
[75] Ibid., 11.

Lall distinguishes between the two-tiered East Asian countries in undergoing duality processes on their development stages as follows:

> "A first tier of East Asian countries, i.e. Singapore, Korea, and Taiwan, invested massively in human capital (particularly technical skills), fostered local R&D, and built strong support institutions. They tapped FDI in different ways, Singapore by plugging into global production systems and Korea and Taiwan by drawing on its technologies via arm's length means such as licensing, copying and original equipment manufacturing. The second-tier countries, i.e. Malaysia, Thailand, Indonesia, and the Philippines relied more heavily on FDI in EPZs and less on indigenous capabilities. Global value chains, particularly in electronics, drove their export success."[76]

In comparison to the East Asian countries, China combined different strategies, some similar to its neighbors and others, like public enterprise restructuring, uniquely its own. The region as a whole was liberalized cautiously and retained a significant role for the state.

China and the other East Asian countries did not follow the Washington Consensus policies of liberalization, privatization, and stabilization.[77] They were slow to remove tariff barriers. The East Asian countries globalized by using industrial and trade policies to promote exports and global technology transfers, against the advice of the international economic institutions.

Todaro and Smith distinguish between the ISI and the EOI policies as follows:

> "The ISI uses protectionism to boost economic growth of countries by having inward-looking development policies. The EOI is based on outward-looking development strategy encouraging free trade, free movement of capital, workers, enterprises, and students, the multinational enterprise, and an open system of communications. Exports of export promotion of both primary and manufactured goods cite the efficiency and growth benefits of free trade and competition, the importance of substituting large world markets for narrow domestic markets, and distorting price and cost effects for protection, and the tremendous successes of such export-oriented economies as South Korea, Taiwan, Singapore, Hong Kong, China, and others in Asia. Firms in these economies have learned a great deal from the firms in the U.S., Japan, and other developed-country economies that have been their long-term customers."[78]

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[76] Lall, "Rethinking Industrial Strategy," 65.
[77] Stiglitz, "Development Policies in a World of Globalization," 15.
[78] Todaro and Smith, *Economic Development*, 619.

With the previous review on how countries either succeeded or failed by either implementing ISI or EOI strategies in history, today the policy issue to determine should be not "to globalize or not to globalize" or "to grow or not to grow."[79] The issue instead, among other questionings, should be "at what pace to liberalize trade, and what policies should accompany it?"[80] The latter indicates that appropriate policies should depend on the context of each country and by assessing the comparative advantages that each country offers.

2.3. Rethinking Industrial Policy

Today, there has been a renewal in countries' interests to implement industrial policies. Many countries consider the benefits that industrial policy can bring in structural transformation of domestic economies. The renewal in countries' interest has taken place as industrial policies may protect countries from negative effects of external financial shocks and allow countries to undergo structural transformation. Other reasons that have made countries consider and renew their interests in industrial policy have been the sharp increase in commodity prices that may raise fears for premature deindustrialization of countries. The renewal in interest for industrial policy has also been perceived in the developed countries as they have acknowledged the significance these policies can have in nurturing robust manufacturing sectors.

There is no single definition of industrial policy. Industrial policy may be defined depending on the context of each country. The introductory section of the present thesis includes a generic concept of industrial policy provided by Stiglitz, Lin and Monga. Another relevant concept in the present study is that one provided by Howard and Kamal. They define industrial policy as "any type of selective intervention or government policy that attempts to

[79] Stiglitz, "Poverty, Globalization and Growth," 80
[80] Ibid.

alter the structure of production toward sectors that are expected to offer better prospects for economic growth than would occur in the absence of such intervention, i.e., in the market equilibrium."[81]

In history, successful stories of righteous implementation of industrial policy could be seen in the NICs and in China. These countries combined protectionism while gradually opening up their markets to trade and investment. In the process, both the public and private sectors played important roles. Moreover, another reason lied on the fact that industrial policy allows for economic upgrading and product diversification of specific sectors. Rather than debating on whether industrial policy is needed or not, the issue at stake is to consider how to best pursue and implement such policies to achieve development.

EPZs have represented useful industrial policy tools for many countries in the course of history. They are considered to be industrial policies as governments hosting them grant incentives to promote industries, in the manufacturing sector and services sector. Today, the fiscal and regulatory incentives granted might clash with the provisions provided by the multilateral and regional trade agreements. However, if a righteous strategy and framework is implemented by the host governments, EPZs may be promising industrial policies even in a post-SDT era. The following subsections conceptualize EPZs as industrial policies significant for developing countries.

2.4. Export Processing Zones: Concept and Identification as Export-Oriented Industrial Policies

As previously noted, the effects of EOI strategies called into question the once popular ISI strategies. This change showed to be parallel to the development of the EPZs. EPZs are a common feature of EOI. The Asia Partnership for Human Development (hereinafter the

[81] Howard and Kamal, "The case for industrial policy: a critical survey," 2.

APHD) states that "a characteristic and, indeed, often central tactic of the broader EOI strategy are the EPZs."[82]

EPZs are seen as instruments for expanding and modernizing countries through additional investment and capital formation, technology transfer, and employment generation. In addition to these direct effects, EPZs are expected to create rippled effects upon the rest of the economy. "EPZs have been a characteristic technique in export-led industrialization"[83] which, though debatable as a general proposition, have been nevertheless associated with the significant industrial development in some countries, especially small ones such as Singapore, Republic of Korea, Taiwan, Hong Kong, Panama, Dominican Republic, and Mauritius. EPZs are industrial policies significantly important within EOI development strategies.

The developing countries in Asia, Europe, and Latin America receiving foreign direct investment (hereinafter FDI) from the most advanced economies saw an opportunity that would enable them to achieve their industrialization objectives by providing them with the production factors they lacked. As history points out, when this phenomenon occurred, the developing countries' attitude towards the foreign investor did not remain neutral. They were mainly conditioned by the concern of maximizing the positive effects of the investment while minimizing the constraints imposed on the national economy. Host governments of potential EPZs attempted to devise instruments of cooperation with the foreign enterprises, endeavoring to reconcile the requirements of their development with the enterprises' concerns. This was the context in which the institution of EPZs emerged.

Basile and Germidis state that the EPZs mark the convergence of two significant trends in the international division of labor by stating the following:

"The first relates to the will of certain countries to opt deliberately for an export

[82] Asia Partnership for Human Development, *Export Processing Zones in Five Countries*, 24.
[83] Ibid., 25

> oriented development policy following the relative failure of a number of import substitution experiments. In this connection the creation of EPZs is usually the preferred back up for such policy. This applies in particular to most of the Asian countries. In other cases however the introduction of EPZs is grafted on to a less firmly outward looking policy, e.g. India and Mexico. The second trend concerns the production cost minimization strategy followed by enterprises in the industrialized countries that either seek to meet certain structural difficulties and remove increasing competitive pressures or try to maintain or even increase their competitiveness. These enterprises are then constrained to relocate part of their production capacity with a view to re-exporting their output either to their country of origin or abroad."[84]

There is an increasing interest taken by many developing countries in policies to attract export-oriented investment prompted by the duality principle.[85] The aim of this duality is first to attract the FDI (which at the same time is expected to provide foreign outlets, create jobs, transfer technology and know-how, generate inflow of foreign exchange, among other benefits); and then, the aim is to promote a whole process of specifically national industrialization in a protected domestic environment.

EPZs are significant policy instruments for investment, trade, and development. They represent promising tools for development and export-oriented growth.[86] They have become increasingly common, as developing countries now use more export led-growth strategies than import-substitution strategies. Export promotion policies represent viable means for developing countries to pursue industrial development. The WTO World Trade Report states that "from the point of view of implementation, export promotion has some advantages compared to import substitution. First of all, chances to pick an industry where the country has a comparative advantage are better. The second is that the costs of subsidies, which show up in budgets, are more transparent than those of tariffs." [87] Developing countries have moved

[84] Basile and Germidis, *Investing in Free Export Processing Zones*, 19.
[85] Ibid.
[86] Engman, Onodera, and Pinali, "Export Processing Zones," 5.
[87] WTO World Trade Report 2006, "Exploring the links between subsidies, trade, and the WTO", xxv, at: https://www.wto.org/english/res_e/booksp_e/anrep_e/world_trade_report06_e.pdf.

from a strategy of "development based on import substitution to one based in export promotion."[88] Particular forms of support for export promotion policies are the use of EPZs.

"An EPZ refers to one or more areas of a country where barriers to trade are reduced and other incentives are created in order to attract foreign investors."[89] They are main features of globalization and may take many forms and terminology, "such as free trade zones, special economic zones, bonded warehouses, free ports and maquiladoras."[90]

EPZs, as significant that they are for developing countries worldwide, are conceptualized by various international organizations. Table 2 enlists the main concepts given by the ILO, the United Nations Industrial Development Organization (hereinafter UNIDO), the UNCTAD, the WB, and the WCO. Common denominations for EPZs include references to "geographic or fenced-in areas" and "free trade conditions" to attract "export-oriented manufacturers."[91]

Since the first modern EPZ was established in Ireland in 1959,[92] EPZs have proliferated (and continue to proliferate) worldwide especially in Southeast Asia, Eastern Europe, Latin America, and Africa. The objective pursued by countries that implement EPZs as industrial policies all over the world have remained constant: development of disadvantaged regions, income and employment generation, attracting foreign and national investment, and the promotion of transfer of technology, managerial skills, and know-how, among others.

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[88] Jenkins, Esquivel, and Larraín, "Export Processing Zones in Central America," 1.

[89] Ibid.

[90] ILO, "Export Processing Zones," at: http://www.ilo.org/inform/online-information-resources/research-guides/export-processing-zones/lang--en/index.htm.

[91] Ibid.

[92] The Shannon Free Zone in Ireland is said to be the first modern EPZ, see Engman, Onodera, and Pinali, "Export Processing Zones," 11.

Table 2. EPZ concept by International Organizations

International organization	EPZ concept
ILO	Industrial zones with special incentives set up to attract foreign investors, in which imported material undergo some degree of processing before being exported again.
UNIDO	Relatively small, geographically separated area within a country, the purpose of which is to attract export-oriented industries by offering them highly favorable investment and trade conditions as compared with the rest of the host country.
UNCTAD	Industrial estates that form enclaves within the national customs territory and are usually situated near an international port and/or airport. The entire production of such zones is normally exported. Imports of raw material, intermediate products, equipment, and machinery required for export production are not subject to customs duty.
WB	An industrial estate, usually a fenced-in area of 10 to 300 hectares that is specialized in manufacturing for export. It offers firms free trade conditions and a liberal regulatory environment.
WCO	Under the concept of "free zone" - a part of the territory of a Contracting Party where any goods introduced are generally regarded, insofar as import duties and taxes are concerned, as being outside the Customs territory.

Source: Author, adapted from ILO (2014) and the WCO Revised Kyoto Convention (1974).

As sources of employment, a recent study reporting employment generation is that of the ILO in 2014.[93] Table 3 illustrates the estimates on employment in EPZs.

With the increase of EPZs worldwide there will also exist an increase in employment creation. EPZ proliferation is possible when the junction of four main trends takes place: the increase in exports, the increase in FDI, the transfer of labor intensive industries from developed countries to developing countries, and further from developing countries to other developing countries and the growing international division of labor and incidence on global production networks. Table 4 illustrates the EPZ proliferation and the estimates of employment trends in year 2008.[94]

[93] ILO, "Trade Union Manual," 3.
[94] Ibid., 4.

Table 3. Employment and number of EPZs by 2008

Geographical region	Employment Number of workers	Number of EPZs
Asia	55,741,147	900
C.A. and Mexico	5,252,216	155
Middle East	1,043,597	50
North Africa	643,152	65
Sub-Saharan Africa	860,474	90
U.S.	340,000	713
South America	459,825	43
Transition economies	1,400,379	400
Caribbean region	546,513	250
Indian Ocean	182,712	1
Europe	364,818	50
Pacific	145,930	14
Total (estimations)	**66,980,763**	**2,731**

Note: Figures represent estimations of each geographical region by year 2008.
Source: ILO (2014), 3.

Table 4. Employment trends in EPZs by 2008

	1975	1986	1995	1997	2002	2008
Number of countries with EPZs	29	47	73	93	116	130
Number of EPZs	79	176	500	845	3000	3500
Employment (millions)	n/a	n/a	n/a	22.5	43	66
China	n/a	n/a	n/a	18	30	40
Other countries	0.8	1.9	n/a	4.5	13	26

Note: n/a: Data on figures not available.
Figures represent estimations by year 2008.
Source: ILO (2014), 4.

As compared to other countries, China shows significant figures in number of EPZs. China operates EPZs at the national, provincial and city levels. Most zone-operating countries are labor surplus economies. China is the most significant labor-using country. Other countries with labor-surplus economies are Mexico, Costa Rica, El Salvador, Guatemala,

Honduras, Malaysia, Mauritius, Philippines, Sri Lanka, among others. Women account for a large share of the workforce in EPZs.

The proliferation of EPZs throughout the years has also made them evolve substantially. Before, EPZs represented small geographic areas, today, nationwide territories may be eligible for EPZ establishments. EPZs also used to target foreign investors, but now national investors also play a significant role. The types of manufacturing activities have also evolved, from traditional textile assembly to more complex computer, automobile or other complex manufacturing. They also include services including IT business call centers, and finance services among others.

The apparel or textile assembly-manufacturing sector has been a promising activity inside EPZs. Apparel accounts for the largest share of EPZ exports, in value and in job posts created. The textile assembly manufacturing underwent a significant policy shift in the last two decades with the phase-out of the MFA and the termination of the WTO-ATC. The MFA allowed quotas on apparel products trade introduced in 1970 in the U.S., Canada and Western Europe. With the MFA, over 50 countries exported to these markets. Many EPZs were established as a result of the MFA. The phase-out of the quota system under the MFA occurred under the ATC of the Uruguay Round of MTNs. The phase-out took place over a ten-year period, with the ATC ending on December 31, 2004. China was the greatest beneficiary of the phase-out of textile and clothing quotas. Small developing countries sought ways to survive competition in textile assembly exports with China becoming the biggest competitor.

2.5. The Incentives granted in EPZs as Industrial Policies

Incentives are offered by host governments to attract investors in establishing EPZs. The EPZs would help support less developed areas in a country and encourage governments to

provide appropriate infrastructure in the specific regions. The EPZs would bring benefits to local populations as well as to the investors as compensations might be higher if compared to investment taking place outside EPZ regimes. Table 5 provides a list and description of the incentives often provided to attract investors in establishing EPZs. [95] The incentives that governments grant to investors are usually temporary with long termination periods. Some of the incentives have other aims such as providing friendly business relations and promoting conglomerates.

The incentives granted can be of various types and forms. With a general list of incentives granted by host governments to investors to promote manufacturing industries, EPZs are considered to be industrial policies as governments promote initiatives to enhance investment by granting incentives that offer benefits to special businesses establishing these schemes. The incentives granted, illustrated in Table 5, may at times be given in less transparent situations, where relaxation and flexibility in certain laws, such labor law, may lead to violations of provisions enshrined in the multilateral and regional provisions, as well as in legal dispositions of each domestic territory where the EPZs operate. The ILO recognizes such relaxed regulatory conditions given for firm investment and states that they are related to the enforcement of labor rights and standards, notably the right to unionize.[96]

In most EPZ-operating countries, the national labor and industrial relations legislation is applicable to the zones. However, as the ILO undergoes studies and monitoring of member countries enforcing labor standards, the ILO has revealed that national labor ministries are

[95] Milberg and Amengual, "Economic development and working conditions," 1.

[96] ILO, Export Processing Zones, at: http://www.ilo.org/inform/online-information-resources/research-guides/export-processing-zones/lang--en/index.htm.

Table 5. Incentives granted in Export Processing Zones

Incentives	Description
Fiscal Incentives	• Exemption from some or all export taxes • Duty drawbacks or exemptions from import duties on raw material, intermediate inputs and capital goods used in the production of goods and supply of services. This can also include various exemptions of customs fees and charges. • Exemptions from the payment of sales tax on exported products or services as well as on all goods and services domestically purchased and used in the productions. • Tax holidays, rebates or reduced tax rates on corporate income or profits, often linked to export performance of companies or to the share of exports in total production. • Exemption from direct taxes such as profit taxes, municipal and property taxes. • Exemption from indirect taxes such as value added tax on domestic purchases. • Indirect subsidies, like special grants for education and training; and direct subsidies, like the supply of water and electricity below market rates.
Regulatory incentives	• Foreign ownership, labor and environmental laws and regulations, foreign exchange regimes, and rules on the lease or purchase of land. • Free profit repatriation for foreign enterprises. • Exemption from national foreign exchange controls
Streamlined administrative services	• Single window or one-stop shop government services, fast track customs services, simplified or abolish licensing procedures, and a dedicated legal framework and court. • Services especially to facilitate import and export.
Enhanced physical infrastructure	• Enhanced access to transport and logistical networks, telecommunications networks and utility services. Some zones also provide production/office space, residential housing and services institutions such as schools
Export promotion services	• Business advisory services, sales and marketing support, finance, and export credit services.

Source: Author, adapted from Engman, Onodera, and Pinali (2007), 17 and Milberg and Amengual (2008), 1.

Note. The incentives included in the table represent general incentives granted in EPZs. Specific cases in specific countries may vary. The EPZ legal framework of each country namely enlists the specific incentives granted.

generally not equipped to monitor EPZs effectively and often consider the zones as a low priority.[97]

Intensifying international competitive pressures increasingly undermine the benefits that EPZs offer as tools for generating employment of low-cost, low-skilled labor. Host countries such as Costa Rica in Central America are recognizing that fiscal incentives, effective infrastructures, and low-cost labor are generally not the decisive factors inducing long-term investments. In contrast, while keeping the incentives, smart EPZs have adopted a number of strategies to ensure that labor productivity is continuously upgraded. Measures include incentives to investors to undertake human resource development. Zones with poor working conditions and low labor standards are likely only to attract firms that use unskilled labor and which will tend to move on to cheaper locations at their convenience. This is one of the reasons EPZs are also known as footloose companies.

2.6. The Relationship between Regional Trade Agreements and Export Processing Zones

RTAs are agreements between two or more countries with the objective of decreasing trade barriers to increase free flow of goods and services in trade activities between members of the RTA. RTAs increase trade by offering preferential market access to goods and services by reducing or eliminating tariff and non-tariff barriers in most cases beyond those offered by the MTS.[98] GATT Article XXIV allows for the deviation from MFN principles through any kind of RTA signed between two or more countries.

[97] ILO, "Employment and social policy in respect of EPZs," 7.

[98] This would apply to countries engaging in RTAs who are already WTO members. For non-WTO members any reduction of trade barriers would have beneficial results for their trade liberalization.

One of the main features of RTAs is that shipments from an RTA partner are treated in the same way as domestic shipments. With RTAs the customs territory between both members becomes a single territory with the same customs treatment. This equal treatment is regulated by preferential rules of origin. Preferential rules of origin protect from circumvention and smuggling from other countries. These rules specify the conditions required to qualify as beneficiaries of RTAs, such as percentage of required local content or change in customs classifications. Goods that are not eligible under the rules of origin criteria are subject to multilateral tariffs provided by the WTO.

In relation to RTAs, EPZs are considered to be outside of a country's custom's territory. RTA benefits apply only to goods originating from other RTA members. As EPZs are outside of the country's national territory, inputs and intermediate goods to be utilized in the EPZs are imported on a duty free basis (based on the EPZ fiscal incentives and not on the RTA tariff reduction benefits) and processed for re-export.

RTAs and EPZs are development tools that promote trade and investment of countries and regions. Successful RTAs promote trade and integration. EPZs create jobs, increase exports, and contribute to economic growth. The harmonization of both tools for trade promotion would have greatly beneficial results for developing countries.

The treatment of EPZs should be considered when signing RTAs, however this is not always the case. Also treatment may differ in different RTAs. NAFTA included EPZs in its legal text, considering that Mexican EPZs, or *maquiladoras*, would have a significant role in NAFTA performances and assessments. Article 303.1 states:

> "Except as otherwise provided in this Article, no Party may refund the amount of customs duties paid, or waive or reduce the amount of customs duties owed, on a good imported into its territory, on condition that the good is: a) subsequently exported to the territory of another Party, b) used as a material in the production of another good that is subsequently exported to the territory of another Party, or c) substituted by an identical or similar good used as a material in the production of another goods that is

> subsequently exported to the territory of another Party, in an amount that exceeds the lesser of the total amount of customs duties paid or owed on the good on importation into its territory and the total amount of customs duties paid to another Party on the good that has been subsequently exported to the territory of that other Party."

Granados from the Inter-American Development Bank (hereinafter IDB) provides a comprehensive description of how free zones and duty drawbacks are treated in America.[99] In the majority of cases, duty drawback schemes are limited to prevent circumvention. Koyama discusses the reasons of why RTAs and EPZs "sit uneasily together". The coexistence among RTAs and EPZs may be seen in several aspects. The author describes the coexistence between both tools as follows:

> **"Trade triangulation**. The primary concern for RTA members regarding EPZs is the potential for trade triangulation. If a product processed under a preferential duty scheme of an EPZ is allowed to enter into the customs territory of an RTA member as an originating product, it opens the possibility that any product not originating in an RTA may enter the RTA free of duties through the EPZ. This would infringe on the tariff collection policies of RTA members and potentially erode the RTAs bloc against extra-territory countries. From the perspective of RTA member governments, a second problem with trade triangulation is that it has the potential to undermine FDI opportunities in the territory. If an RTA prohibits the duty-free entry of EPZ-processed products, foreign suppliers of inputs to EPZ operators may consider setting up an operation in territory so that their customers and thus themselves can take advantage of the expanded market access resulting from the RTA. But when duty-free entry is possible through an EPZ, foreign suppliers may have less incentive to invest in a new operation in the territory.
> **Competitiveness of local producers**. A producer operating under an EPZ program typically benefits from preferential duty schemes, including but not limited to drawbacks and suspension of duties on imported equipment and inputs. A local producer who pays full import duties on imported equipment and inputs will therefore be at a disadvantage against an EPZ operator if products processed under the EPZ program can enter the RTAs local market as originating products. In addition, the financial incentives that may be available to EPZ-based producers often go beyond those related to import duties. In many cases, these incentives are granted partial or total exemption of direct and indirect taxes temporarily or permanently, often on the condition that their export performance meets a required threshold. Such special incentives for EPZ operators also put non-EPZ producers at disadvantage if products from the EPZs are allowed to enter local markets free of duty.
> **Promotion of regional economic integration**. Placing local suppliers at a disadvantage against EPZ-based operators also may pose a threat to the effectiveness

[99] Granados, "Export Processing Zones and other Special Regimes," 5-10.

> of the RTA in promoting one of its primary objectives, i.e., regional economic integration – by hindering inter-industrial integration across member countries. If EPZ-based operators, including those engaged in trading of foreign equipment and inputs are allowed to sell their products to local producers in RTA member countries, they risk crowding out immature local suppliers. Thus, local producers, even with greater access to suppliers in another member country of the RTA may choose to purchase foreign inputs through EPZ-based operators, who may be able to offer both a cost and quality advantage. On the one hand, this should improve the competitiveness of local producers (through their access to higher quality, lower cost inputs) at least in the short term; on the other hand, it may curtail the effectiveness of the RTA in nurturing local suppliers and promoting local vertical industrial linkages.
>
> **Competitive positioning of the EPZs**. The flip side to promoting regional integration is that firms based inside the EPZ may suffer a deterioration of the relative advantages they enjoyed before the RTA. Specifically, as many of the fiscal benefits provided in traditional EPZs are linked directly to exports, the RTA essentially turns what were regional export markets for these firms into "domestic markets." This not only puts these firms on a more level playing field in terms of market access versus non-zone based firms, but also may have implications for zone-based firms to maintain the export requirements on which their incentives are based. The implication is that this market access potentially reduces some of the advantages of being based in the EPZs, and thus has implications not only for the zone-based firms but also for existing zone developers and managers." [100]

Central American countries all implement EPZs as industrial policies, and at the same time all are members of the DR-CAFTA.[101] Therefore the analysis in the present study is based on the scenario in which member countries of an RTA, i.e., Central American countries, all host EPZs as industrial policies. Koyama identifies EPZs in the RTAs and attempts to create synergies for trade and investment, "when the two initiatives exist simultaneously they have the potential to create significant synergies."[102] For the synergy to take place, on one hand RTAs lower trade barriers and provide for the potential realizing of scale economies in regional production. On the other hand, EPZs would provide assets and

[100] Koyama, "SEZs in the Context of Regional Integration," 134-137. Koyama offers a comprehensive analysis on the issues between RTAs and EPZs while excluding the regulatory incentives. The following descriptive analysis is based on Koyama's analysis; Nonetheless, the following sections of the current chapter will focus on the regulatory incentives granted in EPZs and prohibited by RTAs.

[101] In the present study, Central America refers to Costa Rica, El Salvador, Guatemala, Honduras, and Nicaragua.

[102] Koyama, "SEZs in the Context of Regional Integration," 127.

facilities to attract investors in setting up EPZs. Intraregional growth in trade would take place with the effects of such RTA-EPZ synergies. Therefore RTAs and EPZs may coexist with each other and compliance of EPZs with the IEL regional level is possible.

Chapter 3. Central American Export Processing Zones: The Maquila Industry

The present chapter introduces the legal and structural framework of EPZs in Central America. The legal frameworks introduced in the following section are the laws that allow for EPZ existence and implementation in the domestic territory of the DR-CAFTA member countries. These laws vary in detail among the different countries. However, all of them have a commonality that the fiscal and regulatory incentives are largely generous for the investing companies establishing EPZs. As EPZs are considered to be footloose companies, the governments grant these generous incentives and benefits as a policy to attract and increase investment, manufacturing, and exports and prevent the EPZs from moving to other countries. Central America and DR-CAFTA member countries make use of their comparative advantage in the world economy.

3.1. Regional Integration in Central America. An Overview

Central America is a region that extends over an area of approximately 509,000 km^2.[103] It is a region highly characterized for regional integration and openness in its economy. Central American production represents three percent of the total Latin American production.[104] The Central American Integration System (hereinafter SICA) is the economic and political organization of Central American states founded on February 1, 1993. On December 13, 1991, the Organization of Central American States (hereinafter ODECA) signed the Protocol of Tegucigalpa. This protocol is destined to promote regional peace, democracy, and economic development.

[103] Geographically, Central America is comprised of 7 countries: Belize, Costa Rica, El Salvador, Guatemala, Honduras, Nicaragua, and Panama.

[104] Vargas-Hernández and Núñez-López, "Impact of Central American Maquiladoras," 256.

In 1991, SICA included the countries of Guatemala, El Salvador, Honduras, Nicaragua, Costa Rica, and Panama. Belize joined in 2000 as a full member and the Dominican Republic became a full member in 2013. Mexico, Chile, and Brazil are regional observers; the Republic of China, Spain, Germany, and Japan are extra-regional observers. SICA has a standing invitation to participate as observers in sessions of the United Nations General Assembly and maintains offices in the United Nations (hereinafter the UN) Headquarters.

Within Central America, four countries, Guatemala, El Salvador, Honduras, and Nicaragua experience political, cultural, and migratory integration. These four countries are now constituted under the formal name, Central American Four (hereinafter CA-4). Among the countries there are common internal borders and a same-type of passport. Belize, Costa Rica, Panama, and the Dominican Republic join the CA-4 for economic integration and regional friendship.

After the demise of the ATC in 2005, and after the global economic crisis of 2008, developing countries that had huge volumes of textile products sought strategies to stay competitive in the international trade arena. The ATC was created as a 10-year transition period agreement that would phase out the quotas that had been granted by the MFA since the 1970s. The MFA had given the developing countries a sure quota to exports entering the U.S., the EU, and other developed countries' markets. Central American countries ensured quotas on their textile exports to these markets.

The 2008 economic crisis reflected developing countries' export dependency. Developing countries' economies significantly weakened as FDI and exports decreased. Exporters sought immediate measures to alleviate their trade deficits. Central American countries also sought ways to remain competitive.

3.2. Importance of the Maquila Sector in Central America

Maquilas are the Central American EPZs *per se*. The term maquila "etymologically comes from the Arab term *makila* as a measurement for capacity used in milling to design the proportional share grain, flour, or oil."[105] Maquilas are an important tool for the development of Central American countries. They provide incentives and economic benefits that attract foreign and local investment, among them extraterritoriality treatment of goods, which excludes them from taxes, tariffs, and duties. As Bogarin explains:

> "Companies establishing EPZs obtain incentives and benefits that improve their ability to compete on a global level, such as adapted infrastructure for the companies' requirements and technology facilities. They contribute to Central America participating in globalization, international trade, and attracting FDI."[106]

During the last two decades, Central American governments have enacted domestic laws to further enhance FDI, trade, and promote maquilas. They usually operate in relation to their establishments in the geographic zones, mainly through contracts and subcontracts.

Most of the maquilas in Central America engage in apparel and garment manufacturing industry, textile and footwear assembly, although electronics, metalworking, harness and automotive parts assembly, as well as assembly of computer hardware components have increased. Maquilas engaging in the service sector are increasing. Taking advantage of the labor force language skills, call centers and business process outsourcing (hereinafter BPOs) have been established. Reasons for outsourcing are related to saving costs and productivity gain for investors. The process is purchased as a service. This is considered a recent development in Central American maquilas.

Maquila exports have increased their value to achieve almost 50% in relation to total exports of the Central American countries. Likewise, they represent a significant share over each

[105] Asociación para el Avance de las Ciencias Sociales en Guatemala, 2.
[106] Bogarin, "Central American Free Zones," 72.

country's GDP. The Economic Commission for Latin America and the Caribbean (hereinafter ECLAC) reported the share for the maquila value added contribution and its increase throughout the years as shown in Table 6.

Table 6. Share of Maquila Value Added out of Country's Total GDP[107]

	1990	**1995**	**2001**
Mexico and CACM	1.4	2.0	3.3
Mexico	1.5	2.0	3.3
Costa Rica	2.0	2.3	2.5
El Salvador	0.5	1.8	3.6
Guatemala	0.5	1.1	2.0
Honduras	1.0	4.1	9.8
Nicaragua	…	1.3	3.4

Source: ECLAC (2002), 107.

Maquilas have positive impact as sources of employment. The Union Federations of Central American Countries report that:

> "The Central American population is close to 34 million inhabitants. From this total, 21 million are in economically active age, and only 12 million have jobs. Employment generated is the main source of jobs for women, who account for up to 87% of the total labor force in maquilas. Women, of an average of 20 years of age and predominantly single mothers, make up as much as 80% of labor force of maquila industry in Central America."[108]

In spite of the low wages paid in the maquila industry, workers, and families achieve better living standards as compared to those unskilled workers generating the average minimum salary outside of maquilas. Acevedo emphasizes the importance of maquilas as sources of employment by stating, "The number of direct jobs created has grown on average 25% annually. This leads to better supply chains and diversified production capacity."[109]

Maquilas are significant industrial policies for DR-CAFTA member countries' economies therefore their legal compliance with all the IEL provisions is necessary. Firstly,

[107] ECLAC, *Latin America and the Caribbean in the World Economy*, 107.
[108] Vargas-Nuñez and Nuñez-López, "Impact of Central American Maquiladoras," 257.
[109] Acevedo, "Zonas Francas en el Paraíso," at: http://www.elobservadoreconomico.com/articulo/509.

compliance will ensure a safe legal environment that ultimately would attract national and foreign investors, enhancing in this way the maquila performance and contributing to the host country's development. And secondly, the legal compliance would provide the host government with a good reputation in legal soundness and harmony ensuring its reliability towards investors and final consumers genuine binding to the IEL.

3.3. Maquila Legal Framework in Central America: Issues and Remedies

Domestic laws regulating the maquilas grant fiscal incentives to the investors in the enterprises that establish in duty free zones to promote investment, manufacturing, and exports to the other countries. The fiscal incentives grant total or partial tax exemption to imports and exports coming in and going out of the duty free zones, sometimes for a fixed limited amount of time, sometimes for an unknown limit of time. They represent a common initiative used by many developing countries in an attempt to facilitate economic development.

EPZs are regulated within their own legal frameworks enacted in each country's domestic law. As for the DR-CAFTA members, each country ratified and enacted their own free zone laws, having the commonality that all of them promote investment by granting fiscal benefits to the imports and exports coming in and out of the zones.[110] All the Central American countries have enacted their free zone laws. These laws grant fiscal incentives to the enterprises that will engage in the textile, harness, or other good's assembly, or even in the service sector such as call centers, among other service activities.

[110] DR-CAFTA Members: Signing parties to the US-DR-CAFTA are: The Republic of Costa Rica, The Dominican Republic, The Republic of El Salvador, The Republic of Guatemala, The Republic of Honduras, The Republic of Nicaragua, and the United States of America.

Following is a list of DR-CAFTA member countries'[111] domestic laws and institutions that allow investing companies to establish EPZs in each country. The fiscal incentives in generic terms are also enlisted.[112]

1. Costa Rica

Laws: Ley de Zonas Francas de Costa Rica (Costa Rican Free Zone Law), Law No. 7210, December 14, 1990; Reglamento a la Ley de Zonas Francas (Free Zone Regime Regulation Act), Executive Decree No. 34739-COMEX-H, August 29, 2009; and Partial Reform, Executive Decree No. 35422-COMEX-H, August 7, 2009.

Institution: Asociación de Empresas de Zonas Francas de Costa Rica (hereinafter AZOFRAS), (Association of Free Zones).[113]

Fiscal Benefits: 1. a) For enterprises outside the Great Metropolitan Area (GAMA): 100 % Income Tax exemption for the first 12 years and further 50% Income Tax exemption for the following 6 years; b) For enterprises within the Great Metropolitan Area (GAMA):100% for the first 8 years, and 50% for the following 4 years.

2. 13% sales and customs tax exemption on imports on raw material, elaborate and semi-elaborate products, and certain vehicles.

3. Exoneration on taxes levied to income revenues or dividends according to specific conditions.

2. El Salvador

[111] By alphabetical order and excluding the U.S. as a DR-CAFTA member country.
[112] Grant Thornton, "Leyes de Beneficios Fiscales", as of April 2015.
[113] AZOFRAS official homepage at: http://www.azofras.com/

Laws: Ley de Inversiones (Investment Law), Decree No. 732, issued on: October 14, 1999; Ley de Zonas Francas Industriales y de Comercialización (Export Processing Zones Act and Marketing), Decree No. 405, issued on: September 3, 1998; Ley de Servicios Internacionales (International Services Law), Decree No. 431, issued on October 11, 2007.

Institution: Cámara de la Industria Textil, Confección y Zonas Francas de El Salvador (hereinafter CAMTEX), (Chamber of the Textiles, Clothing, and Free Zones of El Salvador).[114]

Fiscal Benefits: 1. Total Income Tax Exemption for users and Deposits for Active Improvements during the time period in which they carry out their operations. For developers and administrators a 15-year time limit is given for the tax exemption. Developers, administrators, direct users, and owners of service parks have the same tributary treatments within the scope of the International Services Law.

2. Total Exemption on Municipal Taxes on the company's assets. In the case of the users, during the time in which they carry out operations in the country, starting from the time in which they begin to operate, and as for the developers and administrators, a 10 year period, which may be extended for the same period.

3. Total Tax Exemption on real estate transfers, in cases where these real estates will engage in maquila activity or incentives for maquila activity. This benefit is granted to developers and free zone users.

3. Guatemala

Law: Ley de Zonas Francas (Free Zones Act); Decree No. 65-89; Issued on November 14, 1989.

[114] CAMTEX official homepage at: http://www.camtex.com.sv/

Institutions: Ministries of Economy and Public Finance, Industrial Policy Office.[115]

Fiscal Benefits: 1.Incomes Tax exemption on revenues generated from exports. Exemptions are given for a 10-year period.

2.Twelve percent exemption on VAT and on Imports Customs Duties, according to specific import tariffs on raw material, packaging material, samples, fabric samplers, bottles, among others. Twelve percent exemption on the VAT customs duties on machinery and equipment destined for the specific activities contained in the respective Law.

4. Honduras

Law: Ley de Zonas Libres (ZOLI) (Free Trade Zones Law); Decree No. 356; Issued on: July 21, 1976.

Institution: Asociación Hondureña de Maquiladores (hereinafter AHM) (Honduran Manufacturers' Association)[116]

Fiscal Benefits: 1. Total income tax exemption on revenues generated from goods exports to non-Central American countries, for a 10-year period.

2. Total tax exemption on tariff duties, charges, surcharges, consular fees, internal taxes, consumption tax, and other taxes or duties directly or indirectly related with imports and exports customs operations to the Puerto Cortes Free Zone. Revenues generated on the free zone are exempted from income tax.

3. Total exemption on tariff duties, consular fees, charges and surcharges, internal consumption taxes, production, sales and other charges, interest rates on imports and exports of goods and merchandises.

[115] Guatemalan Ministry of Economy official homepage at: http://www.mineco.gob.gt/
[116] AHM official homepage at: http://www.ahm-honduras.com/

4. Enterprises included in the Agricultural Zones Exports Law may enjoy the following benefits: total exemption in the tariff duties, consular fees, municipal taxes, charges and surcharges, internal consumption tax, productions, sales, and other races or duties, interest rates, and goods and merchandise that they import and/or export covered by the present law.

5. Nicaragua

Laws: Free Zone Law for Industrial Exportations, Decree 22, 1976; Industrial Free Zones Law, Decree No. 50-2005.

Institution: Comisión Nacional de Zonas Francas (hereinafter CNZF), (National Free Zone Commission)[117]

Fiscal Benefits: 1.100% Incomes tax exemption

2.100% tax exemption on asset acquisition

3.100% Municipal tax exemption

4.100% exemption on machinery, equipment, raw material, transportation and support services.

5.100% VAT exempted.

6. Dominican Republic

Laws: Law No. 8-90 on Export Promotion Free Zones; Law No. 56-07, declares textile chain sectors of national priority; Law No. 84-99, on Exports Promotion and Renewal Law No. 392-07 on Competition and Industrial Innovation.

Institution: Consejo Nacional de Zonas Francas de Exportación (hereinafter CNZFE) (National Free Zones Council)[118]

[117] CNZF official homepage at: http://cnzf.gob.ni/

Fiscal Benefits: 1. Law No.8-90: Benefits with a special regime on customs control, fiscal incentives of up to 100% on Income Tax sectors such as: construction, immovable assets, municipal, patents, assets, among others; all of which are intended to work or operate within the free zones.

2. Law No. 56-07: Provides the exemption on the Transfer of industrialized goods and services, as well as other taxes, to all enterprises engaged in textile assembly process, garments, and accessories; fur, footwear manufacturing and leather manufacturing.

3. Law No. 84-99: Allows the reimbursement on ITBIS paid on export products.

Table 7 summarizes specific fiscal incentives granted by Central American governments.[119] EPZs are essential tools of economic growth for developing countries.[120] EPZs employ sixty eight million people worldwide, or about 3 percent of the global workforce,[121] and exist in over 119 countries across Asia, Latin America, Eastern Europe, the Middle East, and sub-Saharan Africa.[122] In the DR-CAFTA members they still represent significant core pillars to sustain the domestic economies. Thus incentives appear to be very generous in granting total or *quasi-total* exemptions.

[118] CNZFE official homepage at: http://www.cnzfe.gov.do/
[119] Author, adapted from Grant Thornton, "Leyes de Beneficios Fiscales," as of April 2015.
[120] McCallum, "Export Processing Zones," 1.
[121] Ibid., 2.
[122] Waters, "Achieving World Trade Organization Compliance," 482.

Table 7. EPZ Fiscal Incentive schemes in Central America

C.A. Country	Laws granting Fiscal Incentives	Export Subsidy Component and other Granted Exemptions
Costa Rica	Free Zone Law	Exemption from all taxes on imports of raw materials, components and parts, packaging materials, machinery, equipment, spare parts, automobile vehicles required, etc. (indefinite); Exemption from all taxes on imports of fuel, oil, and lubricants (indefinite); Exemption from payment of tax on capital and assets and payment of land tax (10 years); Exemption from all taxes on profits (4-6 years); Exemption from any municipal tax or business tax (10 years); Enterprises based in relatively less-developed areas are entitled to a credit of 10 percent of the amount paid as wages, which will be gradually phased out over five years.
El Salvador	Industrial and Marketing Free Zones Law; International Services Law	Exemption from import duties on raw material, parts, components, packaging, machinery, equipment, tools, spare parts, etc.; Exemption from import duties on fuels, lubricants, catalysts, etc.; Total exemption from income tax, municipal taxes, real estate transfer tax.
Guatemala	Maquila and Exports Promotion Law; Free Zones Law (Private Free Zones); ZOLIC Law (Public Free Zone); Incentives Law for Development Projects on Renewable Energy	Exemption from corporate income tax; Exemption from customs duties and other import taxes, including Valued Added Tax (VAT) on machinery, equipment, parts, components, and accessories required for the production process.
Honduras	Temporal Imports Regime (RIT); The Puerto Cortés Free Zone Law (ZOLI); Industrial Export Processing Zones Law (ZIP)	Total Income Tax exemption on revenues generated from goods exports to non-Central American countries, for a 10 year period; Total tax exemption on tariff duties, charges, surcharges, consular fees, internal taxes, consumption tax, and other taxes or duties directly or indirectly related with imports and exports customs operations to the Puerto Cortes Free Zone.
Nicaragua	Free Zone Law for Industrial Exportations; Industrial Free Zones Law	Total exemption from the following: revenue tax, asset acquisition tax, municipal tax, machinery, equipment, raw material, transportation and support services, and VAT.

Source: Author, adapted from Grant Thornton, (2011).

3.4. The Honduran Maquila Industry: A Case Study

The Honduran Free Trade Zones Act of 1976 covers all the Honduran territory making it possible for investors to establish an EPZ in any part of the Honduran territory. The fiscal incentives that have been granted since the beginnings of the maquila industry have not been modified to the day. This has guaranteed constant foreign and national investment in Honduran maquilas.[123]

Besides the fiscal incentives granted within a maquila legal framework, regulatory incentives such as streamlined customs procedures have also attracted the investors. Import and export procedures may take up to one hour for clearance. Prominent companies of worldwide recognition have established maquilas in Honduras. Examples are textile and garment MNCs, such as Fruit of the Loom, Gildan, Hanes Brands, Nike, Adidas, Gap, Van Heusen, Reebok, Ralph Lauren, Vanity Fair, Aéropostale, among others.

Besides the Ley de Zonas Libres that allows for EPZ or maquila establishments, Honduran laws supporting the maquila framework are various, among them are the: Temporal Imports Regime (RIT), The Puerto Cortés Free Zone Law (ZOLI), Industrial Export Processing Zones Law (ZIP), Agricultural Exports Zones Law (ZADE), Investment Promotion and Protection Law, Agreement 215 for Sales Tax Withholding, Decree 181-2007 Reform to the General Environment Law, Decree No. 51-2007 Interpretation of Article 11 of the Law for the Thirteenth Month Bonus, Decree PCM 43-2006 Incentives to Investment Promotion in ZIE, Decree 50-2003 on Holidays, Decree 150-2008 Partial Reform to Article 120 of the Labor Code, DEI 215 1% Withholding, The DR-CAFTA Implementation Law, Industrial Property Law, Copyright and Related Rights Law, INFOP 1972 Law, Seventh Day and Thirteenth Month Payment Law, General Environment Law, Education Bonus Law and

[123] Asociación Hondureña de Maquiladores, http://www.ahm-honduras.com/.

Regulations, National Program for Hourly Payment, Regulations of the Law of Entry of Currency originated from Exports, Administrative Regulations for the Application for the Chapter 8 on Safeguards, Temporary Import Regime Regulations, Environmental Audit Regulations, Regulations of the General Environment Law, General Regulations of the IHSS 2005 Law, Regulations of the Hourly Employment Law, Regulations of the Public-Private Promotion Law, Minimum Wages 2011 and Education Bonus 2011.[124]

The Law for the Promotion and Protection of Investments guarantees the foreign investors that their goods and resources have return rates and are duly protected, for example in the cases of political risk insurance. The law widens its protection to International Law. For those companies that require hourly work due to the type of trading activities, there is a legal framework within the Law for the National Program of Hourly Employment, which facilitates these types of hiring processes.

FDI in Honduran maquilas include countries such as: the U.S., Canada, Taiwan, Hong Kong, Germany, Denmark, France, Korea, Mexico, El Salvador, Guatemala, Costa Rica, among others. The AHM reports investments of USD $3,000 million in industrial parks, as well as other investments in machinery, equipment, and capital.[125] Manufacturing activities that take place inside maquilas include textile assembly (apparel and garments), tobacco plantations, furniture manufacturing, agro industry, auto and electronic parts assembly (harness). In relation to the service sector, business process outsourcing (hereinafter BPOs) through call centers has increased and given place for innovation in maquila industry. The Honduran government has facilitated infrastructure and processing plants for any kind of EPZ that would like to establish operations in the country. Besides the infrastructure for the

[124] Complete text of each legal instrument at: http://www.ahm-honduras.com/?p=1925/ .
[125] Lavaire, "Industria Maquiladora a la Alza en Honduras," at: http://www.honduras.com/espanol/industria-maquiladora-a-la-alza-en-honduras/.

operation processes, the facilities include banks, health clinics, and cafeterias, among others. The facilities may host operations in goods manufacturing and in the service sector.

Maquilas in Honduras are significant to the national economy. Lavaire states that in 2012 textile exports from maquilas to the U.S. market ranked fourth after China, Taiwan, and Bangladesh.[126] By 2014 maquilas provided 124,941 job posts,[127] taking into account that Honduran population is currently of approximately 8.7 million inhabitants with an annual increase of 1.8%.[128] Fifty-one percent of maquila workers were female workers. The BCH reports that 95,887 workers were engaged in the textile sector, representing a 76.7% of the total maquila employment.[129] Workers in textile manufacturing increased by 2,789 posts as compared to the previous year 2013. The harness and automobile manufacturing reveal figures of 14,230 job posts, with a 1,255 decrease as compared to 2013. The total number of maquilas reported by the end of 2014 were 320 companies, out of which 38.1% were in the textile manufacturing, 32.5% in commerce (storage of raw materials and machine components), 4.4% in food industry, 3.1% in harness manufacturing, 3.1% in chemical product manufacturing, plastic products 2.2%, furniture and wooden goods manufacturing 1.6%, services provided to other companies 1.9%, paper and cardboard 0.9%, tobacco products 0.9%, other manufactures, 11.3%.[130]

All maquilas are located throughout 18 industrial parks nationwide. Among them are Altia Business Park, Continental Free Zones, Green Valley Industrial Park, Inmobiliaria Hondureña del Valle S.A. de C.V., Villanueva Industrial Park, Industrial Processing Zone

[126] Ibid.

[127] BCH, Industria de Bienes para la Transformación (Maquila) y Actividades Conexas en Honduras (2014): 12, at: http://www.bch.hn/download/maquila/informe_bienest2014.pdf.

[128] Instituto Nacional de Estadística de Honduras, at: http://www.ine.gob.hn/.

[129] BCH, Industria de Bienes para la Transformación (Maquila) y Actividades Conexas en Honduras (2014): 12, at: http://www.bch.hn/download/maquila/informe_bienest2014.pdf.

[130] Ibid.

(hereinafter ZIP) Calpules, ZIP Buena Vista, ZIP Búfalo, ZIP Choloma S.A., ZIP El Porvenir, ZIP San José S.A. and Zona Libre América, S.A. de C.V.[131]

Lavaire states that maquilas generate annually approximately USD $448 million in fully loaded salaries.[132] Fully loaded salaries are those that include social-compensation packages, local sales and service payments, among other work benefits. The movement of capital generated by the maquila-manufacturing sector spurred new businesses and micro-companies that operate within the local market, which in turn created approximately 479,135 new jobs in the last five years.[133]

In February 2012, the Honduran government, private sector representatives, and labor representatives signed the "Great National Agreement".[134] This agreement was to consolidate growth in the manufacturing sector (including the maquila sector). The agreement includes seven main goals: a) promote economic growth; b) increase investment in the public and private sectors; c) spur the creation of jobs; d) establish higher wages; e) spark increased productivity and competitiveness; f) provide quick resolution of conflicts; g) protect the most vulnerable segment and population.[135] The purpose of the Agreement is to spur dynamic public and private investment in construction, maquila-type and "light" manufacturing, generating renewable energy, bolstering micro, small, and medium enterprises (hereinafter MSMEs), diversification and expansion of exports.

One of the main aims to establish EPZs in developing countries is to attract investment. The foreign investors usually seek geographic areas where they consider they

[131] AHM (2013) at: http://www.ahm-honduras.com/.

[132] Lavaire, "Industria Maquiladora a la Alza en Honduras," at: http://www.honduras.com/espanol/industria-maquiladora-a-la-alza-en-honduras/.

[133] Ibid.

[134] The Great National Agreement (in Spanish "El Gran Acuerdo Nacional") is a social basis of short, medium, and long-term partnership between the government, employers, and workers in order to address the national crisis in developed economies, in a stage of growth with equity. See: http://www.elheraldo.hn/opinion/615474-210/el-gran-acuerdo-nacional

[135] Ibid.

would gain profits and have security. Factors that indicate competitive advantage for the investors are price, duty-free access, proximity and speed to access markets, quality and variety of fabric, infrastructure, and labor regulations and labor relations climate. In Honduras, the regulatory incentives granted to attract and promote investment might be materialized in flexible labor regulations that eventually lead to specific violations. Interviews conducted in maquilas in Honduras reveal that MNCs prohibit freedom of association by encouraging employees to have friendly and mutual understanding with employers. Additionally, a 2009 rise in the minimum wage in Honduras excluded EPZs as a regulatory incentive to investors. The latter was amended and EPZ workers could also later enjoy an increase in minimum wage.[136]

[136] Interview survey was carried out in Tegucigalpa, Honduras in 2010 with authorities from the Honduran Maquila Association and managers from two maquilas (EPZs) – the Maquila "Zona Libre de Tegucigalpa" (In English Tegucigalpa Free Zone) financed by national investment, and the Maquila "Fruit of the Loom", financed by FDI and representing a worldwide renowned MNC.

Chapter 4. The Multilateral Level: Multilateral Trade Agreements and Fiscal Incentives in Export Processing Zones

The present chapter identifies EPZs within the MTAs. Other than the international organizations that define EPZs,[137] the only multilateral agreement that defines EPZs *per se* is the WCO Revised Kyoto Convention, in its Chapter 2, specific Annex D, under the concept of free zones. A free zone "means a part of the territory of a Contracting Party where any goods introduced are generally regarded, insofar as import duties and taxes are concerned, as being outside the Customs territory."[138] The legal instrument emphasizes that "the domestic legislation shall specify the specific conditionalities for establishing free zones, as well as specifying the kinds of goods admissible the rules on operation for the zones."[139]

The WTO does not define free zones or EPZs *per se* in any of its agreements. The present chapter identifies the specific WTO Law provisions that prohibit the fiscal incentives granted in EPZs. The WTO Law does not affect the regulatory incentives granted in EPZs, especially the labor law flexibilities to be discussed in Chapter 6. This is because the trade-labor linkage inclusion has not been possible in the MTS but rather the inclusion takes place in the RTAs. The WTO-ASCM has no provision against the regulatory incentives of EPZs. The present section then identifies the SDT benefits within the ASCM granted to a specific list of developing countries that allows the use of prohibited fiscal incentives. These benefits are facing a final phase-out period to conclude with no final extensions in December 2015.

[137] See Chapter 3, Table 2.

[138] Revised Kyoto Convention, numeral (2) standard, at: http://www.wcoomd.org/en/topics/facilitation/instrument-and-tools/conventions/pf_revised_kyoto_conv/kyoto_new/spand.aspx.

[139] Ibid.

4.1. The World Trade Organization Agreement on Subsidies and Countervailing Measures

EPZs *per se* are not mentioned in any of the WTO agreements. Nonetheless, the specific incentives that are typically granted in EPZs are subject to disciplines under the WTO, specifically under the provisions included in the ASCM.[140] Article 1.1 of the ASCM defines a subsidy as a financial contribution by a government that confers a benefit to a recipient:

> "1.1 For the purpose of this Agreement, a subsidy shall be deemed to exist if: (a) (1) there is a financial contribution by a government or any public body within the territory of a Member (referred to in this Agreement as "government"), i.e. where: (i) a government practice involves a direct transfer of funds (e.g. grants, loans, and equity infusion), potential direct transfers of funds or liabilities (e.g. loan guarantees); (ii) government revenue that is otherwise due is foregone or not collected (e.g. fiscal incentives such as tax credits, import duty exemption); (iii) a government provides goods or services other than general infrastructure, or purchases goods; (iv) a government makes payments to a funding mechanism, or entrusts or directs a private body to carry out one or more of the type of functions illustrated in (i) to (iii) above which would normally be vested in the government and the practice, in no real sense, differs from practices normally followed by governments."

Article 1.2 introduces the concept of specificity and provides that only those subsidies that are specific are covered by the Agreement:

> "(2) (a) there is any form of income or price support in the sense of Article XVI of GATT 1994; and (b) a benefit is thereby conferred."

Footnote 1 of Article 1.1 (a)(1)(ii) relates to EPZ incentive schemes as it represents a permissible duty exemption and thus, incentives within Footnote 1 shall *not* be deemed to be a (prohibited) subsidy:

> "In accordance with the provisions of Article XVI of GATT 1994 (Note to Article XVI) and the provisions of Annexes I through III of this Agreement, the exemption of an exported product from duties or taxes borne by the like product

[140] ASCM full legal text at: https://www.wto.org/english/docs_e/legal_e/24-scm.pdf.

> when destined for domestic consumption, or the remission of such duties or taxes in amounts not in excess of those which have accrued, shall not be deemed to be a subsidy".

The ASCM also distinguishes between prohibited subsidies and actionable subsidies:

> "3.1 Except as provided in the Agreement on Agriculture, the following subsidies, within the meaning of Article 1, shall be prohibited:
> (a) Subsidies contingent, in law [de jure] or in fact [de facto], whether solely or as one of several other conditions, upon export performance, including those illustrated in Annex XV;
> (b) Subsidies contingent, whether solely or as one of several other conditions, upon the use of domestic over imported goods.
> 3.2 A Member shall neither grant nor maintain subsidies referred to in paragraph 1".

According to Article 3, prohibited subsidies are those which are either contingent upon export performance or upon the use of domestic over imported goods. It is very important to point out that prohibition applies only to trade in goods, as the ASCM only touches upon goods and not on trade in services. Specific subsidies are those granted to particular industries, enterprises, or regions. These subsidies commonly referred to as export subsidies and import substitution subsidies or red subsidies are prohibited by the ASCM. Actionable subsidies or yellow subsidies are subsidies that are not prohibited *per se* but which may cause adverse effects to the interest of other Members, and thus their prohibition depends on the case-by-case scenario.

4.2. The WTO-ASCM Special and Differential Treatment of Developing Countries

Based on the 1979 Enabling Clause, the WTO granted SDT in 1995 to a specific list of developing countries granting them exceptions to the export subsidy prohibition provided in Article 3 of the ASCM. The developing countries eligible for the exception to the prohibitions are included in Article 27.2 and Annex VII of the ASCM. However, the SDT on the exemptions of export subsidy prohibitions expired in 2013, being the final phase-out

period in December 2015. Article 27 enlists the eligible members eligible for the ASCM SDT:

> "27.1 Members recognize that subsidies may play an important role in economic development programs of developing country Members.
> 27.2 The prohibition of paragraph 1(a) of Article 3 shall not apply to:
> (a) developing country Members referred to in Annex VII (Least-developed countries (hereinafter LDCs) and developing countries' GNP per capita less than USD $1,000 per year).[141]
> (b) other developing country Members for a period of eight years from the date of entry into force of the WTO Agreement, subject to compliance with the provisions in paragraph 4."

Table 8 illustrates WTO-ASCM classification of countries that may use prohibited export subsidies, and those, that by December 2015 according to Article 27.2 (b) need to phase out such export subsidies. As noted before, it is the specific fiscal incentives, tax break benefits, and requirements of EPZs that can be inconsistent with the ASCM provisions. Therefore, to determine compliance or non-compliance of EPZs with the WTO provisions, it is necessary to follow a case-by-case analysis. General factors to identify, however, are first, if the EPZs confer subsidies, and if so, whether those subsidies are prohibited or actionable.

[141] Annex VII of the ASCM provides the specific list of countries eligible for the exemptions to the export subsidy prohibition. "The developing country Members not subject to the provisions of paragraph 1(a) of Article 3 under the terms of paragraph 2(a) of Article 27 are: (a) LDCs designated as such by the United Nations which are Members of the WTO; and (b) Each of the following developing countries which are Members of the WTO shall be subject to the provisions which are applicable to other developing country Members according to paragraph 2(b) of Article 27 when GNP per capita has reached USD $1,000 per annum: Bolivia, Cameroon, Congo, Côte d'Ivoire, Dominican Republic, Egypt, Ghana, Guatemala, Guyana, Honduras, India, Indonesia, Kenya, Morocco, Nicaragua, Nigeria, Pakistan, Philippines, Senegal, Sri Lanka and Zimbabwe." https://www.wto.org/english/docs_e/legal_e/24-scm_03_e.htm.

Table 8. SDT of Export Subsidy Prohibition and the End of the Exemptions

Exemptions to Prohibitions according to the WTO classification of Developing Countries	End of the Exemptions
1. LDCs - Article 27.2 (a) referring to Annex VII (a) of the ASCM	Graduation
2. Developing countries with a GNP per capita less than USD $1000 per year - Article 27.2 (a) referring to Annex VII (b) of the ASCM	Graduation
3. Other developing countries - Article 27.2 (b) for a period of 8 years	2002-2007: Extensions granted + 2 year phase-out period by the ASCM committee 2006: G/SCM/W/535, G/SCM/W/537 proposal to extend until 2018, no outcome 2007: ASCM Committee granted final extension until 2013 + 2-year phase out period 2015.

Source: Author, adapted from the ASCM.

Table 9 illustrates the kinds of subsidies; prohibition with ASCM rules and in the case there is prohibition, the kinds of applicable remedies.

Table 9. Achieving EPZ compliance with the WTO-ASCM in a post SDT era

Kind of Subsidy	Prohibited by the WTO?	WTO Rule	Remedy
A. Subsidies contingent on export performance e.g. tariff exemptions, tax exemptions, income tax exemptions	Yes	ASCM Article 3.1 (a) and Annex I (Illustrative List of Export Subsidies)	Eliminate the export contingency factor/ relax export requirement, leave for the domestic market
B. Duty free imports of raw material and intermediate inputs used in the production for exports	No	Footnote 1 to Article 1.1.(a)(1)(ii)	WTO consistent, may remain
C. Exemption or Remission of indirect taxes on inputs consumed in the production	Yes	Item (g) and (h) of Annex I and Annex II (Guidelines on Consumption of Inputs in the Production Process)	Eliminate the export contingency factor
D. Subsidies contingent on the use of domestic goods over imported goods	Yes	ASCM Article 3.1 (b)	Out of the EPZ study scope because EPZs seek tax exemption on imported goods.
E. Subsidies on Services	No	The ASCM does not touch upon prohibition on subsidies on trade in services	Promotion of the service sector, e.g. business process outsourcing (BPO) such as call centers

Source: Author, adapted from the ASCM.

Directly related to Table 9, Table 10 exemplifies EPZ incentives in a textile and garment EPZ and concretely analyzes on which import and export activities prohibition applies, by referring to the specific ASCM provision, either allowing or prohibiting such provisions.

Table 10. EPZ compliance with the WTO: A textile industry model

Tax exemption, or duty free on:	Prohibition	WTO provision	Kind of Subsidy (Ref. to prev. slide)
Processed raw material	No	Footnote 1	B
Consumed Fuel	No	Footnote 1	B
Domestic utilized dyes	Yes	Annex I and II	C
Income tax	Yes	Article 3.1	A
Sewing machines	Yes	Article 3.1	A
Construction material	Yes	Article 3.1	A

Source: Author, adapted from the ASCM.

Besides the efforts from host governments in introducing EPZ reforms to comply with the MTAs in a post 2015 SDT era, the MTS also needs to offer flexibility in the transition of such reforms until they are compliant with the IEL. Kodama portrays that:

> "WTO law should grant developing countries the room and flexibility to use policies. In the case that SDTs are revisited under the WTO in the years to come in a post-SDT era, they should be made more meaningful in order for developing countries to benefit from such flexibilities. This will allow countries to reach development stages that they are aiming for."[142]

Currently, SDTs are yet not revisited. Therefore, the flexibility to implement industrial policies such as EPZs should be allowed according to the development stage of each member. Targeted industries by WTO rules, such as prohibitions in EPZs, and the necessary policy response from each member, will be different depending on where the economy stands. In reaching EPZ compliance with the MTAs, developing countries that shall abide by WTO Law

[142] Kodama, "S&D under the WTO Agreements," 129.

by reforming EPZ legal frameworks, should also receive certain flexibility by the MTS in the implementation of the new schemes depending on the specific circumstance and needs that that the domestic economies reveal.

With such export subsidies prohibition and an end of the SDT it is necessary to refer to the role of WTO bodies, specifically relevant ones, such as the WTO-ASCM Committee and the Trade Policy Review (hereinafter TPR) Body. The ASCM Committee clearly expressed that the final extension was the one granted in 2007 that was to expire in 2013 with the additional two-year phase-out period. Countries enlisted in such termination of exemptions have been drafting EPZ reforms to align with the remedies pointed out in Table 9. The TPR Body of DR-CAFTA member countries has acknowledged the significant importance of EPZs for the export-oriented economies within a trade and development context, but has not directly referred to the legal aspects of fiscal incentives contravening WTO Law.

The post-Uruguay Round implementation and SDT agendas reflect the view that WTO commitments and rules are denying many developing countries access to policies that foster economic development. In essence these agendas press for greater flexibility in trade rules on the grounds that the latter are too constraining upon governments that seek to react flexibly in the face of developmental exigencies, or to intervene in the economy in more far-reaching ways than currently contemplated under WTO rules.

Citing the fact that developing countries gained very little from the Uruguay Round, developing countries agreed to enter the new round, the Doha Development Agenda (hereinafter the DDA). This was to be only on the condition that the Round considered development to be the centerpiece.[143] There are growing concerns that this promise will go

[143] Gallagher, "Globalization and the Nation-State," 1.

unfulfilled, as there are deadlocks in the multilateral negotiations. Key among those concerns is the notion that additional commitments will not give the developing world the "policy space" to use the very instruments and tools that many industrialized nations took advantage of to reach their current levels of development before the WTO was established. The outcome in full of the DDA is at present pending.

4.3. A Single case brought to the WTO Dispute Settlement: DS451 China – Measures Relating to the Production and Exportation of Apparel and Textile Products

To the date, there has been only one single case of a WTO member country complaining against the use of export subsidies in the textile sector.

> "On 15 October 2012 Mexico requested consultations against China under the WTO Dispute Settlement DS 451. Mexico claimed that China maintained a wide variety of measures that supported producers and exporters of apparel and textile products, as well as suppliers in the cotton and chemical fiber industries. Measures cited by the complainant-Mexico, included tax exemptions for certain enterprises, reduction of import duties and VAT for purchase of equipment by certain groups of enterprises and those located in certain regions, measures contingent on use of Chinese goods and contingent on export performance, low cost loans by state-owned banks to certain industries, preferential land use rights, discounted electricity rates, support for production, sale and transportation provided to cotton farmers and the Chinese petrochemical industry, and cash payments from government agencies. According to Mexico, these measures appear to involve both prohibited and actionable subsidies that are causing or threatening to cause serious prejudice through displacement and impedance of Mexican exports to the United States as well as through significant price undercutting, price suppression, price depression, and lost sales in the United States. In the complaint, Mexico claimed that these measures utilized by China were inconsistent with: Articles 3.1(a) and (b), 5(c), 6.3(b) and (c), 6.4, and 6.5 of the ASCM, Article III: 4 of the GATT 1994; Articles 3,9, and 10 of the Agreement of Agriculture, and Paragraph 1.2 of the Part I of China's Accession Protocol. On 25 October 2012, the European Union requested to join the consultations. On 26 October 2012, Australia and Guatemala requested to join the consultations. On 29 October 2012, Brazil, Peru and the United States requested to join the consultations. On 30 October 2012, Honduras requested to join the consultations. On 15 November 2012, Colombia requested to join the consultations."[144]
>
> Until November 2015, the case DS451 revealed neither progress nor a reached agreement among the parties.

[144] WTO DS451, at: https://www.wto.org/english/tratop_e/dispu_e/cases_e/ds451_e.htm.

4.4. A Post-Special and Differential Treatment Era from 2016

The EPZ-MTA analysis has identified the clashes that exist between the fiscal incentives granted in EPZs and the provisions enshrined in the WTO-ASCM. To achieve compliance with the IEL, governments need to align with multilateral trade rules to continue implementing EPZs. Though in December 2015 exemptions to export subsidy prohibitions end, EPZs will continue to prevail as important industrial policy tools of developing countries. The non-compliance that countries might fall into from January 2016 will require flexibilities from the MTAs so that developing countries can gradually align to the ASCM.

EPZ reforms to comply with WTO in a post-SDT era will lead to product diversification and social upgrading. The current case for the Central American EPZs is that Costa Rica and Panama have reformed their domestic laws; Guatemala, El Salvador, and Dominican Republic are working on action plans for the elimination of subsidies, and Nicaragua and Honduras will need to reform in the case that they graduate, according to the SDT exemption of Article 27, Annex VII of the ASCM. Concretely, Costa Rica and the Dominican Republic are seeking to expand their service sector within the DR-CAFTA, beyond GATS provisions.

In the case of Costa Rica, the country has undergone a Free Zone Law domestic reform that eliminates the exports requirement; this means that the local market can import from a zone with MFN tariffs. It has also promoted a public-private commission under the National Development Plan of Costa Rica to determine eligible enterprises to the zones considering the contribution that they can provide to the country. The criteria of the interested parties (i.e. potential EPZs to receive benefits) must cover certain characteristics: a) Projects with significant social development contribution and generating high skilled employment; b) Projects that include high technology equipment and manufacturing, and thus can contribute

to the modernized production sector of the country; c) Projects that involve research and development activities; d) Projects that promote innovation or technology transfer, or the incorporation of clean technology, waste and residual treatment, energy saving, and rational water use; e) Companies shall be established in areas of lower economic development; and f) Fiscal credit grants of up to 10% if companies reinvest in fixed capital or training to personnel. In the case of Panama, the country's new EPZ legal framework does not exempt companies in free zones from income tax, dividend tax, annual tax on the capital of the company, and excise tax on certain goods. Companies that contribute with technology, research and development, scientific contributions or health or environment are tax exempted.

If developing countries strive to receive an SDT treatment forever within the WTO, it would imply that they forever want to remain in a developing state where special treatment should be granted. Governments need to implement and go through structural reforms that can bring these countries out of the developing state. The flexibility from the MTS for countries to align to the WTO Law is necessary, although the compliance with such provisions in relation to EPZs *per se* would successfully lead to EPZ economic and social upgrading, product diversification, and development.

Stiglitz states that globalization raises awareness on countries on how they should remain competitive in the global economy.[145] He emphasizes that:

> "The gap between developed and developing countries today is not only disparities in capital, but also big gaps in knowledge levels. Developing countries are seeking ways to upgrade their technologies, to enhance trade and at the same time to compete with foreign imports in their domestic markets."[146]

EPZs can represent viable means to promote technology and enhance competitiveness in order to achieve such economic and social upgrading. Diversifying production and engaging

[145] Stiglitz, "Poverty, Globalization and Growth," 80.
[146] Ibid.

in more complex manufacturing sectors rather than in traditional textile assembly would lead to a sustainable development. Reforms in EPZ legal frameworks to comply with WTO Law would allow for countries to upgrade EPZ manufacturing activities as could be seen in the Costa Rican EPZ legal reform case.

Chapter 5. The Regional Level: Regional Trade Agreements and the Regulatory Incentives in Export Processing Zones

RTA provisions have rules that have direct effects on EPZs, specifically on the regulatory incentives that governments grant to EPZs. The fiscal incentives that the MTS covers in the WTO-ASCM and which have been discussed in Chapter 4 are also prohibited by the RTAs. RTAs in principle aim to comply with the MTS, specifically under Article XXIV of the GATT, which concerns customs unions and free trade areas. In this sense RTAs echo the WTO Law. Matters affecting the fiscal and customs issues in EPZs are the rules of origin and duty drawback mechanisms. These rules always seek to comply with the GATT-MFN and national treatment principles.[147] The present chapter focuses on the regulatory incentives that EPZs grant and which may contravene dispositions in labor provisions enshrined in RTAs.

The trade-labor linkage inclusion in RTAs, which has not been possible in history to be included in MTAs, has a direct impact on EPZ operation and implementation. The chapter discusses the internationally enforceable labor provisions that trade policy now encounters in RTAs and analyzes labor cases taken to the NAFTA side labor agreement, the North American Agreement on Labor Cooperation (hereinafter NAALC) and the DR-CAFTA. The study proposes RTAs as stepping-stones to achieve EPZ compliance with the multilevel IEL and advocates for a trade-labor linkage inclusion in RTAs to protect CLS of workers engaged in EPZ manufacturing processes. "RTAs can be instrumental to aid the MTS. They can have synergistic effects with the WTO in trade and non-trade related areas to ensure compliance with the IEL and development of countries."[148]

[147] Koyama, "SEZs in the Context of Regional Integration," 127-156.
[148] Estevadeordal, Suominen, and Martinicus, "Regional Trade Agreements," http://e15initiative.org/wp-content/uploads/2015/01/E15_RTAs-_Estevadeordal-et-al_FINAL.pdf.

5.1. The Trade-Labor Linkage Inclusion in RTAs: A Historical Review

RTAs and EPZs have a close relationship regarding trade policy. One of the relationships is based on the regulatory incentives that governments grant to investors so that they can establish EPZs. The regulatory incentives referred to in this subsection refer to labor law flexibilities that may violate labor standards provided in the ILO and which are adopted by the domestic labor law of countries. International enforceability of labor standard violations has not been possible in the MTS, but is a challenging issue RTAs are assuming in today's globalized economy.

Labor issues have been part of trade relations longer than most other social policy issues; mainly due to the significant impact trade policy can have on workers. Lester and Mercurio describe a number of ways in which labor issues arise:

> "The fundamental impact of trade on employment in specific industries, an effect which is enhanced when trade is between countries of different development levels; the existence of varying degrees of labor rights in different countries, relating to such policies as the minimum wage, unionization, and safe working conditions; and the use of trade measures to coerce better labor practices in other countries."[149]

The inclusion of internationally enforceable labor provisions in RTAs represents a new trend in world trade policy and an alternate way to improve labor conditions in the process of globalization. Labor provisions are defined as "provisions comprising any labor standard which establishes minimum working conditions, terms of employment, or worker rights; any norm on the protection provided to workers under national labor law and its enforcement mechanisms; and any regulatory framework for cooperation in and/or monitoring of these issues." [150] Internationally enforceable labor provisions are labor provisions that can be taken to a dispute settlement mechanism (hereinafter DSM) contained

[149] Lester and Mercurio with Davies and Leitner, *World Trade Law Text*, 836.
[150] Ebert and Posthuma, *Labour provisions in trade agreements*, 1.

within the trade agreement in the cases where non-compliance with labor standards takes place. The enforceability character allows for monetary or trade sanctions to be imposed by an international DSM. The inclusion of internationally enforceable labor provisions either in the MTS or in RTAs to protect labor standards is what the present study refers to as the trade-labor linkage.

Internationally enforceable labor provisions have the aim to protect labor standards. Labor standards are the norms and rules that govern working conditions and industrial relations. The Asian Development Bank (hereinafter the ADB) and the ILO define them as the rules that govern how people are treated in a working environment."[151] The ILO states, "they are an essential component in the international framework for ensuring that the growth of the global economy provides benefits to all."[152] Labor standards embrace practically all aspects of labor markets: "minimum wages, working time, health and safety, labor inspection, statistics, industrial relations, non-discrimination, child labor, among others."[153] They are found at the national and international level. Those included in the national laws are legally binding and governments have their own bodies to enforce them. Those included in international treaties, conventions, or agreements are legally binding to members or signing parties and their enforcement bodies may be defined by the agreements *per se* or from recommendations from international organizations.

In the multilateral system, the ILO, founded in 1919, represents the multilateral organization with faculties to set forth, monitor, and enforce labor standards. These standards are included in the Conventions and Recommendations that the ILO adopts in its International

[151] ADB, ILO. *Core Labor Standards Handbook*, 10.

[152] ILO, Introduction to Labor Standards, at: http://ilo.org/global/standards/introduction-to-international-labour-standards/lang--en/index.htm.

[153] OECD. *Trade Employment and Labor Standards*, 25.

Labour Conferences of member countries.[154] The ILO has adopted 190 Conventions,[155] eight of which define four CLS.[156] CLS embody basic human rights derived from the United Nations Universal Declaration of Human Rights of 1948.[157] As the OECD states, "they involve the fundamental liberty, dignity and respect of the individual."[158] The ILO Declaration on Fundamental Principles and Rights at Work and its Follow-up of 1998, states, "all Members, even if they have not ratified the conventions, should promote, and realize in good faith and in accordance with the Constitution, the principles concerning the fundamental rights, which are the subject of those Conventions, namely: (a) freedom of association and the effective recognition of the right to collective bargaining, (b) the elimination of all forms of forced or compulsory labor, (c) the effective abolition of child labor, and (d) the elimination of discrimination in respect of employment and occupation."[159] Table 11 illustrates the CLS and the Conventions that enshrine them.[160]

[154] As of August 2015 the ILO counts with 185 members, at: http://www.ilo.org/dyn/normlex/en/f?p=1000:10011:907315495132922:::P10011_DISPLAY_BY:1

[155] ILO Conventions and Recommendations, available at: http://ilo.org/global/standards/introduction-to-international-labour-standards/conventions-and-recommendations/lang--en/index.htm

[156] Eight Conventions are Fundamental Conventions as they embrace the 4 CLS: Freedom of Association and Protection of the Right to Organize Convention, 1948 (No. 87); Right to Organize and Collective Bargaining Convention, 1949 (No. 98); Forced Labor Convention, 1930 (No.29); Abolition of Forced Labor Convention, 1957 (No.105); Minimum Age Convention, 1973 (No.138); Worst Forms of Child Labor Convention, 1999 (No.182); Equal Remuneration Convention, 1951 (No.100); Discrimination (Employment and Occupation) Convention, 1958 (No.111)These fundamental Conventions are binding to all of the 185 members, regardless of ratification.

[157] The Universal Declaration of Human Rights, available at: http://www.un.org/en/universal-declaration-human-rights/

[158] OECD. *Trade Employment and Labor Standards*, 27.

[159] ILO Declaration on Fundamental Principles and Rights at Work and its Follow-Up, adopted by the International Labour Conference at its Eighty-sixth session, Geneva, 1998, available at: http://www.ilo.org/declaration/thedeclaration/textdeclaration/lang--en/index.htm.

[160] ILO, *International Trade and Core Labour Standards*, 20.

Table 11. The Fundamental Principles and Rights as Work and the Fundamental Conventions, as laid out in ILO Documents and Decisions

CLS	Convention	Year	No.
Freedom of association and effective recognition of the right to collective bargaining	Freedom of Association and Protection to Organise Convention	1948	87
	Right to Organise and Collective Bargaining Convention	1949	98
Elimination of all forms of forced or compulsory labor	Forced Labour Convention	1930	29
	Abolition of Forced Labour Convention	1957	105
Effective abolition of child labor	Minimum Age Convention	1973	138
	Worst Forms of Child Labour Convention	1999	182
Elimination of discrimination in respect of employment and occupation	Equal Remuneration Convention	1951	100
	Discrimination (Employment and Occupation) Convention	1958	111

Source: ILO, (2000), 20.

To enforce labor standards, the ILO counts with a supervisory enforcement mechanism. However, the mechanism's enforcement actions limit to technical assistance, recommendations, peer pressure, and persuasion to encourage greater labor standard compliance. As Brown, Deardoff, and Stern argue "It is considered to be weak and with 'lack of teeth' as it imposes no trade or monetary sanctions."[161] In this way, attempts to include internationally enforceable labor provisions in the MTS have been done in history; the most recent attempts those done with the establishment of the WTO. In the first WTO Ministerial

[161] Brown, Deardoff, and Stern, "Pros and Cons of Linking Trade and Labor Standards," 5.

Conference, the Singapore Ministerial Conference of 1996,[162] in numeral 4 of the Ministerial Declaration, corresponding to CLS, member countries recognized the ILO as the competent body to set standards and they reaffirmed their support in promoting them. However, in the Third Ministerial Conference, held in Seattle 1999,[163] developed nations, specifically the U.S., Canada, and the EU, formally proposed to include internationally enforceable labor provisions and the establishment of a labor-working group. Such active proposals were strongly opposed by the developing country members.[164] The attempts to include the trade-labor linkage in the MTS-WTO have failed, and even though the WTO has reaffirmed its close cooperation with the ILO, the current Doha Development Agenda (hereinafter DDA) has remained moot over a trade-labor linkage inclusion in the WTO.

The trade-labor linkage inclusion has not been possible in the MTS. However, the trade-labor linkage has been possible in RTAs. The International Institute of Labor Studies (hereinafter the IILS) reports there has been substantial growth in the number of trade agreements featuring labor-related measures since the mid-1990s, including South-South Agreements between developing countries.[165] In many cases, the improvement of labor standards is a significant condition for the entry into force of the RTA. Torres recognizes "the increasing number of trade agreements which include provisions with respect to labor standards is a reflection of the growing awareness that trade liberalization, important as it is, should go hand-in-in hand with progress on the employment and social front."[166] Provisions

[162] Singapore Ministerial Declaration adopted on December 13, 1996, available at: http://www.wto.org/english/thewto_e/minist_e/min96_e/wtodec_e.htm.

[163] Seattle Ministerial Conference from November 30th to December 3rd, available at: http://www.wto.org/english/thewto_e/minist_e/min99_e/english/about_e/resum02_e.htm.

[164] The proposal is considered as "one of the most controversial issues in the WTO". For more details on the position of the developed and developing nations on such proposal see http://www.wto.org/english/thewto_e/minist_e/min99_e/english/about_e/18lab_e.htm.

[165] IILS, *The Social Dimensions of Free Trade Agreements*, 1.

[166] Torres, available at: http://www.ilo.org/global/about-the-ilo/newsroom/news/WCMS_228969/lang--en/index.htm.

have proliferated over the last two decades, "from only four in 1995, to 21 in 2005, and to 58 in June 2013 – including 16 South-South trade agreements. Of about 190 countries with trade agreements, roughly 120 are partners to trade agreements that include labor provisions."[167]

The first RTA to ever include internationally enforceable labor provisions was the NAFTA of 1994 in its labor side agreement, the NAALC. However, it was not until 2012 when trade policy history saw for the first time a labor case brought to an RTA-DSM requesting the establishment of an arbitral panel. The labor case takes place in the Latin American-Caribbean context specifically within the DR-CAFTA. The case, named the Guatemala – Issues Relating to the Obligations Under Article 16.2.1(a) of the DR-CAFTA (hereinafter the U.S.-Guatemala case) represents an experimental case in which for the first time in history the U.S. (or any other country in the world) has filed a complaint against a government and requested the establishment of an arbitral panel within an RTA for failure of Guatemala to enforce its own labor laws as stipulated in Article 16.2.1 of the DR-CAFTA. The case has already set precedents that are quite new in trade policy studies. The precedents refer to an 18-Point Enforcement Plan agreed between both parties when the established arbitral panel was deactivated. Guatemala compromised to implement the Enforcement Plan within a determined period. However, she failed to fully implement it. In September 2014 the panel was reactivated. The following two subsections analyze the substantive, institutional, and procedural aspects of the internationally enforceable provisions included in the NAFTA-NAALC and in the DR-CAFTA.

[167] IILS, *The Social Dimensions of Free Trade Agreements*, 5.

5.1.1. The NAFTA-NAALC Internationally Enforceable Labor Provisions: Substantive, Institutional, and Procedural Aspects

Addo identifies the NAFTA as the largest and most comprehensive trade agreement signed to date.[168] It is the first agreement to include labor provisions in a trade agreement. The NAFTA was negotiated under then-U.S. president George H. W. Bush under the 1988 Omnibus Trade and Competitive Act fast-track authority. The fast track authority guarantees "Congress will not be entitled to make any amendment to the legislation during the review process and will vote to approve the agreement and the implementing legislation within a fixed period of time."[169] The NAFTA negotiations were critically shaped by three factors: "(1) asymmetries of power between the three states; (2) sharply contrasting domestic political institutions; and (3) differences in the non-agreement alternatives, patience, and risk orientations of the heads of government and their chief negotiators."[170] Heated negotiations on the main NAFTA took over three years between the three member countries, the U.S., Canada, and Mexico until it was finalized in 1992.[171]

To understand the effectiveness of the NAFTA side agreement - the NAALC - it is noteworthy to mention that final negotiations of the NAFTA took place during a U.S. presidential campaign between Bush and then-Democratic Governor Bill Clinton. It is well known that the NAALC represents an "afterthought of the NAFTA."[172] As a Democratic candidate, Clinton endorsed free trade and the passing of the NAFTA. Moreover, receiving strong support and "pressure from his political allies in the U.S. labor and environmental

[168] Addo, *The Global Debate*, 216.
[169] Mazuyer, "Labor Regulation and Trade," 242.
[170] Cameron and Tomlin, *The Making of NAFTA*, 15.
[171] Pomeroy, "The Labor Side Agreement Under the NAFTA," 769.
[172] Weiss, "Symposium Two Steps Forward, One Step Back," 701.

movements"[173] he committed to helping U.S. workers and to prevent aggravation of the wage differential, especially between the U.S. and Mexico that the NAFTA could bring. He assured that he would level the playing field to ensure that no member country would gain unfair trade advantages by relaxing labor law enforcement to benefit from investment and trade.[174] He promised to initiate negotiations on NAFTA side agreements if elected, one of them being labor issues.[175] Clinton's main goal in negotiating a labor side agreement was to "ensure the strongest possible improvements in worker standards throughout North America."[176]

Hufbauer and Schott discuss the "facts about fears" concerning the inclusion of labor issues in the NAFTA as follows:

> "Labor issues were important in all three North American countries while NAFTA was being negotiated, but for different reasons. In the U.S. employment and wages became a primary measuring rod for evaluating NAFTA. There was fear of U.S. job migration to Mexico. The Clinton administration justified the latter by claiming that thousands of jobs would be created as a balance if NAFTA were to be ratified. In Canada, labor issues were important but less important than questions of sovereignty. NAFTA itself did not generate a great deal of labor concerns in Canada because Canada had very little exposure to Mexico. Rather, debates within Canada over labor have evolved as Canada has become more integrated with the U.S. At first, Canadians showed concern that their publicly funded social programs would be at risk if Canadian firms were exposed to US competitors that had lower corporate taxes. This fear turned out to be unfounded as Canadian attention shifted to emigration, cross-border labor mobility of highly skilled workers. In Mexico, labor-related issues were less contentious than in the other countries and at the same time more diffused. Some employees in the state sector feared layoffs, but most recognized that the potential trade and investment NAFTA generated would boost Mexican employment. Ironically most of the attention to labor issues in Mexico came not from Mexicans but from opponents of NAFTA in the U.S. who claimed that NAFTA would exacerbate already bad

[173] Ibid., 703.

[174] Prior to the NAALC, a Memorandum of Understanding (MOU) was signed between the U.S. and Mexico in 1991 to ensure both countries' cooperation in enforcement of child labor and health and safety standards. In 1992, Canada and Mexico also signed an MOU. These represent the first experiences of bilateral intergovernmental cooperation to address labor issues among the countries, which are now NAFTA-NAALC signatory parties. *See* Mazuyer, "Labor Regulation and Trade," 241.

[175] The other promised agreement was in environmental issues, which later came to be the Environmental Side Agreement of NAFTA.

[176] Pomeroy, "The Labor Side Agreement Under the NAFTA," 772.

> labor practices in Mexico. This strain of opposition led to negotiations and the later creation of the labor side agreement to the NAFTA."[177]

The NAFTA labor side agreement, the NAALC, began to be negotiated after Clinton was elected. Negotiations began in March 1993 and it was signed roughly six months later, in September 1993.[178] The bargaining position of the countries reflects weaknesses in the final agreement. The U.S. was serious about giving teeth to the labor side deal and wanted to cover all industrial relations; negotiators placed a strong emphasis on obligations and enforcement. Canada originally wanted no trade sanctions, weak accords, and no violations of sovereignty. Mexico wanted respect for sovereignty, no renegotiation of NAFTA, and no trade sanctions. The U.S. advocated for a DSM on a consistent basis, but neither Canada nor Mexico accepted an institution that would supersede their domestic tribunals.

The U.S. insistence on trade sanctions as a means of enforcing labor standards constituted the main hurdle in the talks between the three countries. "Both Mexico and Canada balked at the idea of including any kind of trade sanction in the enforcement provisions, and the Canadian business community claimed that freer trade should not be held ransom for environmental or labor provisions."[179] The parties were also concerned about setting a common international standard that would violate national sovereignty rights. In the U.S., Republicans threatened to withdraw support for NAFTA if the side deals were too strict. Also, unions opposing the NAFTA weakened the labor side deal. As a result, Canada and Mexico accepted that a weak form of trade sanctions and enforcement would only be applied if a country had persistently violated its own laws and refused to pay fines after dispute resolution had assessed damages. The U.S. had no other option but to "drop the insistence on

[177] Hufbauer and Schott, *NAFTA Revisited*, 80-81.
[178] Cameron and Tomlin, *The Making of NAFTA*, 186.
[179] Pomeroy, "The Labor Side Agreement Under the NAFTA," 776.

covering all industrial relations and accepted that panels would address issues only relating to health and safety, child labor, and minimum wages."[180]

The final NAALC[181] signed in 1993 entered into force with the main NAFTA[182] on January 1, 1994. According to Addo, "the agreement created a multinational enforcement and review system that allows each country to monitor how the others enforce their national laws."[183] It may be considered as if the NAALC broke new ground in the history of trade agreements by creating labor-related obligations and establishing sanctions for failure to fulfill them in certain cases.

The NAALC represents a side agreement alone. It is comprised of 55 articles divided into 7 parts – Part 1: Objectives; Part 2: Obligations; Part 3: Commission for Labor Cooperation; Part 4: Cooperative Consultations and Evaluations; Part 5: Resolution of Disputes; Part 6: General Provisions; and Part 7: Final Provisions. Additionally it has numerous annexes – Annex 1: Labor Principles, Annex 23: Interpretive Ruling, Annex 39: Monetary Enforcement Assessments, Annex 41A: Canadian Domestic Enforcement and Collection, Annex 41B: Suspension of Benefits, Annex 46: Extent of Obligations, and Annex 49: Country-specific definitions.

Provisions of the NAALC represent internationally enforceable labor provisions as an instrument for the implementation of labor standards and encourage cooperation in the exchange of information and technical assistance. They represent legally binding normative standards that the member countries agreed to comply with when signing the RTA. The objectives of the NAALC are stated in Article 1: "[I]mprove working conditions and living standards…promote labor principles set out in the Annex…" In relation to the normative

[180] Cameron and Tomlin, *The Making of NAFTA*, 206.
[181] Full text of the NAALC available at: http://www.naalc.org/naalc/naalc-full-text.htm.
[182] The other side agreement is the NAFTA Environmental Side Agreement.
[183] Addo, *The Global Debate*, 217.

content and obligations undertaken, the NAALC does not directly refer to the ILO,[184] but rather parties agreed to enforce their own labor laws and standards (Article 2, Levels of Protection). Mazuyer clarifies that "the purpose was not to create supranational labor standards or pursue a harmonization among national legislations, but to obtain an effective enforcement of each country's domestic existing labor law."[185] In this way, sovereignty issues cannot be claimed by any of the parties when enforcing the NAALC.

The obligations undertaken are those specifically stated in Annex 1 of the Agreement "Labor Principles". These principles are recognized as included in each of the parties' domestic laws; however, the agreement once again explicitly lists and describes them. The principles to be protected are: (1) Freedom of association; (2) The right to bargain collectively; (3) The right to strike; (4) Prohibition of forced labor; (5) Labor protection for children and young persons; (6) Minimum employment standards; (7) Elimination of employment discrimination; (8) Equal pay for women and men; (9) prevention of occupational injuries and illnesses; (10) Compensation in cases of occupational injures and illnesses; and (11) Protection of migrant workers. The scope of the application in the NAALC is related to the trade activities among the parties within the RTA (Interpretive Ruling Annex 23).

The NAALC creates institutions. Article 8 establishes the Commission for Labor Cooperation (hereinafter CLC), comprised of a Ministerial Council and Secretariat at the supranational level. It further establishes the National Administrative Office (hereinafter NAO) at the domestic level, in each party's national territory, to receive labor complaints, assist, and work in close cooperation with the CLC. NAO are unique in that they have no

[184] The U.S. has not ratified most of the major ILO conventions; *See* Pomeroy, "The Labor Side Agreement Under the NAFTA," 776.

[185] Mazuyer, "Labor Regulation and Trade," 245.

counterpart under the NAFTA Environmental Side Agreement or under any other labor rights regime in Europe or elsewhere. The Agreement provides oversight mechanisms to ensure that labor laws are being enforced in all three countries and provides the ability to invoke trade sanctions as a last resort for non-enforcement law by any of the parties.

Part 5 of the NAALC establishes the dispute settlement procedures. Public communication of cases that want to be brought to the NAALC should follow the following steps: 1. Submission filed with the NAO; 2. Consultations with other NAO; 3. Minister-to-Minister consultations; 4. Evaluation by a Committee of Experts (ECE); 5. Ministerial Council Minister-to-Minister Consultations; 6. Ministerial Council Special Session; 7. Dispute Resolution; and 8. Sanctions. Any private person, legal representative, corporation, non-governmental organization, or labor organization having an administrative, judicial, or *quasi*-judicial reason which proves its relationship to the dispute may submit a claim at any of the two NAO located in the territories outside of the territory that the presumed labor violation took place.

Article 21.3 of the NAALC allows third-party participation at the NAO consultations stage: "Any other NAO shall be entitled to participate in the consultations on notice to the other NAO and the Secretariat." The establishment of an arbitral panel in accordance with Article 29, may only be convened "to consider the matter where the alleged persistent failure by the Party complained against to effectively enforce its occupational safety and health, child labor, or minimum wage standards, being trade-related and/or covered by mutually recognized labor laws." These are the only internationally enforceable labor provisions within the NAALC: occupational safety and health, child labor, or minimum health standards (not freedom of association or collective bargaining). This means that the establishment of an independent ECE and arbitral panel request is possible only in the cases concerning

occupational safety and health, child labor, or minimum health standards. If the complaint alleges violations in freedom of association or collective bargaining, the review process ends at the ministerial level with government-to-government consultations. In this case, no monetary or trade sanctions are to be imposed. Remedies would be limited to recommendations and improvement. If issues concern the principles enshrined in Article 29, sanctions to be imposed are of monetary assessments, up to USD $20 million based on Annex 39: Monetary Enforcement Assessments, and/or suspension of trade benefits based on Annex 41B: Suspension of Benefits.

In accordance with the procedural aspects provided in Article 29 and described in the preceding paragraph, Hafbauer and Schott characterize the procedural aspects of the NAALC by a three-tiered structure:

> "The first tier is limited to NAO review and ministerial oversight. A committee of experts cannot evaluate the enforcement of labor principles in this tier, and no penalties are provided for non-compliance. The labor principles in this tier are freedom of association, collective bargaining, and the right to strike. In the second tier are principles subject to NAO review, ministerial consultations, and evaluation by a committee of experts. This does not call for the arbitration of disputes and does not require the imposition of penalties. Included in this tier are forced labor, gender pay equity, employment discrimination, compensation in case of injury or illness, and protection of migrant labor. The labor principles in the third tier are child labor, minimum wages, and occupational safety. They receive full treatment: NAO review, ministerial consultations, evaluation and arbitration, and eventually monetary penalties." [186]

Soon after the NAALC came into force in 1994, NAO received complaints. Cases have mainly been solved through ministerial agreements (joint programs, workshop, or other measures), and no case has ever gone beyond Ministerial Consultations, thus there has never been an arbitral panel request or sanctions within the NAALC. The present study has Soon after the NAALC came into force in 1994, NAO received complaints. Cases have mainly

[186] Hufbauer and Schott, *NAFTA Revisited*, 123.

been solved through ministerial agreements (joint programs, workshop, or other measures), and no case has ever gone beyond Ministerial Consultations, thus there has never been an arbitral panel request or sanctions within the NAALC. The present study has analyzed the 39 submissions brought to the NAO as of August 2015.[187] Table 12 summarizes the cases filed in each of the NAO, whereas Figure 1 illustrates the total number of cases submitted per year, highlighting the three most violated labor principles included in Annex 1 of the NAALC.

Both, Table 12 and Figure 1, show that freedom of association is the most frequently violated principle, having 24 submitted cases, followed by occupational health and safety with 17 cases and the right to bargain collectively with 16 cases. Other violated labor principles have been minimum employment standards, discrimination, migrant workers, right to strike, and child labor. Mexico is the member country that shows the most labor violations, and it is relevant to mention that most of these complaints took place inside the maquiladoras that make use of cheap and intensive labor work.

Table 12. Cases submitted to each NAO[188]

NAO Submissions as of August 2015

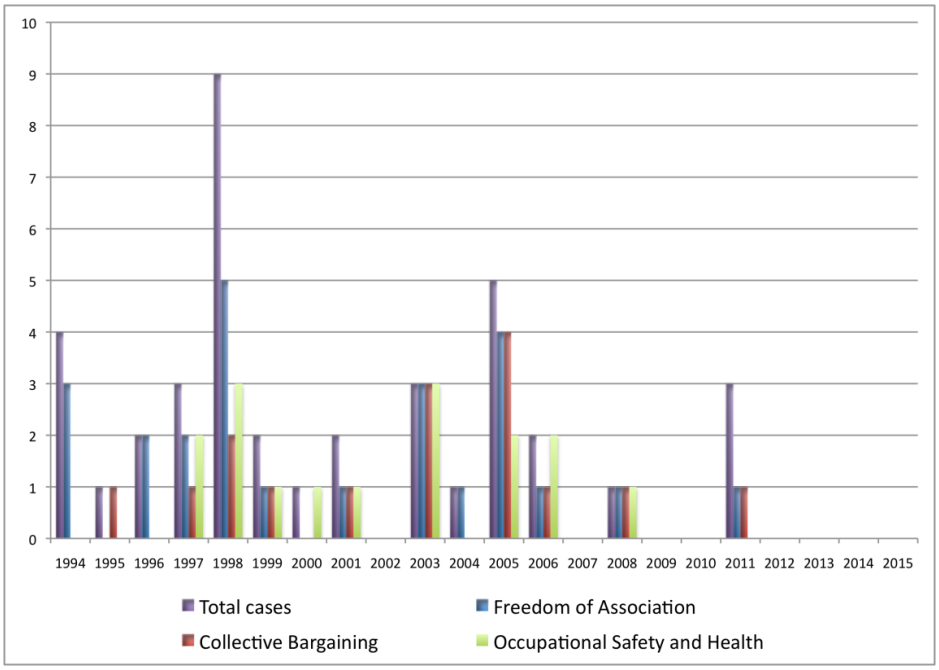
NAO	Against Canada	Against Mexico	Against U.S.	Total
In Canada	0	3	3	6
In Mexico	0	0	10	10
In U.S.	2	21	0	23
Total	2	24	13	39

Source: Author, adapted from Submissions under the NAALC, 2015

[187] Submissions analyzed in this work are based on Department of Labor, Status of Submissions under the NAALC as of August 2015, available at:
http://www.dol.gov/ilab/programs/nao/status.htm and
http://www.dol.gov/ilab/trade/agreements/naalc.htm

[188] Ibid.

Figure 1. Most violated labor standards within the NAFTA[189]



Labour Principle/ Year	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	Total 1994-2015
Freedom of Association	3	0	2	2	5	1		1	0	3	1	4	1	0	1	0	0	1	0	0	0	0	25
Collective Bargaining	0	1	0	1	2	1		1	0	3	0	4	1	0	1	0	0	1	0	0	0	0	16
Occupational Safety and Health	0	0	0	2	3	1	1	1	0	3	0	2	2	0	1	0	0		0	0	0	0	16
Total cases	4	1	2	3	9	2	1	2	0	3	1	5	2	0	1	0	0	3	0	0	0	0	39

Source: Author, adapted from Submissions under the NAALC, 2015

There are four withdrawn cases to date: U.S. NAO 2004-01, U.S. NAO 9803, U.S. NAO 9602, and U.S. NAO 940004. Likewise cases submitted to the U.S. NAO: 9601, 2003-01 2005-02, 2005-03, and Canada NAO 2005-01 reveal failures in the existing Mexican tribunal courts and legal institutional bodies to receive claims and enforce labor standard compliance, or even to provide transparent labor hearings during the procedures.

None of the submission up to August 2015 has established an ECE nor requested an arbitral panel. Submissions at most have had reports issued and reached the ministerial

[189] As of August 2015, available at: http://www.dol.gov/ilab/trade/agreements/naalc.htm.

consultations stage. Labor champions consider the NAALC mechanism for enforcement very ineffective, as governments are unlikely to take a punitive action for fear of retaliation.[190] Governments have avoided dispute resolution and sanctions.

From 2011 to present, the NAALC has received no submissions. First, it may be considered that labor violations have noticeably decreased and employers are striving to comply with NAALC provisions. Second, perhaps a more probable interpretation is that interest groups filing complaints have lost confidence on the NAALC, considering it ineffective or weak. One reason may be the need to travel across borders to the NAO office of another country to file a complaint. This results in monetary and time costs for the submitting party, in many cases private parties. Furthermore, submissions might be accepted or rejected by the NAO office, or the complaining parties might even withdraw the cases as they do not rely on the institution or even consider the processes too bureaucratic. The original intensity that the petitioner might have might be diluted. Critics see the procedure as cumbersome with quasi-diplomatic enforcement procedures claiming that it would take more than 30 months to reach the final stage. Similar to the ILO, members use diplomatic pressure and moral suasion.

Besides the lengthy and costly procedure, a principal argument about the ineffectiveness of the NAALC is its weakness and lack of enforceability. NAALC only sanctions the failure to enforce occupational safety and health, child labor, or minimum wage standards (Article 29). A glaring omission is the failure to impose sanctions regarding freedom of association and collective bargaining, though they are the most violated CLS. These are the most important standards because they represent means to achieving all other CLS. Freedom of association and collective bargaining appear to be associated positively with

[190] Kirschner, "Fast Track Authority," 398.

the success of trade reforms.[191] EPZs can become a testing ground for demonstrating that trade and labor standards can reinforce one another in raising standards of living in poor countries.[192] These are the most important CLS as they represent tools and means to achieving the other CLS.

This study emphasizes the importance of including internationally enforceable labor provisions in RTAs that can guarantee all of the CLS. To genuinely level the playing field in a trade agreement, all of the principles in the agreement should have equal enforcement intensity. The internationally enforceable provisions of the NAALC should equally enforce all the principles stated in NAALC Annex 1, and which also include the CLS, with due process until the end, including the establishment of arbitral panels and imposing of sanctions, as stated in Annex 39 of the NAALC, whenever it would result necessary.

NAALC amendment to equally enforce all the internationally recognized labor standards would ensure protection of workers benefitting from the NAFTA in the three member countries. In fact, the Democrats sought to amend the NAFTA in the 2008 Democratic Party platform to improve the pact for all three countries.[193] Canada and Mexico did not sustain the motion; however, amendments to the NAALC itself would restructure weaknesses identified in this section. It would guarantee equal protection of all the labor principles the NAALC recognized in Annex 1.

[191] Aidt and Tzannatos, *Unions and Collective Bargaining*, 20.
[192] Elliot and Freeman, "The Role Global Labor Standards," 320-322.
[193] *Inside U.S. Trade*, "Democrats in Platform."

5.1.2. The DR-CAFTA Internationally Enforceable Labor Provisions: Substantive, Institutional, and Procedural Aspects

As a region, Central America and the Dominican Republic represents the third largest U.S. export market in Latin America.[194] After the NAFTA came into force in 1994, the region found itself in a disadvantageous position, as it had to compete with Mexico, which had taken an advantageous position to enter U.S. markets. In 2001, Central America and the U.S. met on the sidelines of the IX meeting of the Free Trade Area of the Americas (hereinafter FTAA) Trade Negotiations Committee to discuss possibilities of deepening their bilateral trade and investment relations. In 2002 the U.S. announced its intent to explore the possibility of negotiations of an RTA with Central America, and in 2003 negotiations officially began. In relation to the internationally enforceable labor provisions of the DR-CAFTA, Weiss portrays that during the time of the negotiations, "none of the Central American countries expressed willingness to incorporate labor rights within the main agreement; however Costa Rica indicated receptiveness to following the NAFTA-NAALC model."[195]

In 2003, negotiations included one negotiating group that covered labor and environment. Negotiations concluded in December 2003 and the agreement was signed in August 2004 with the five Central American countries, the Dominican Republic, and the U.S. under the Trade Promotion Authority (TPA) statute of the U.S.[196] It entered into force in 2006 for the U.S., El Salvador, Guatemala, Honduras, and Nicaragua, in 2007 for Dominican Republic, and in 2009 for Costa Rica.

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[194] This is after Mexico and Brazil, see USTR: http://www.ustr.gov/trade-agreements/free-trade-agreements/cafta-dr-dominican-republic-central-america-fta.

[195] Weiss, "Symposium Two Steps Forward, One Step Back," 723.
Costa Rica had already signed a similar side agreement with Canada, the Canada-Costa Rica Agreement on Labour Cooperation of 2001. Full text of the agreement available at: http://www.labour.gc.ca/eng/relations/international/agreements/lca_costa-rica.shtml.

[196] Details on DR-CAFTA negotiation history see Organization of American States, available at: http://www.sice.oas.org/TPD/USA_CAFTA/USA_CAFTA_e.ASP.

The DR-CAFTA came to be the first RTA between the U.S. and a group of smaller developing countries. The DR-CAFTA promotes stronger trade and investment ties. Trade in goods within the region has increased over 71% since entry into force, from USD $35 billion in 2005 to USD $60 billion in 2013. For the U.S., exports summed USD $30 billion and imports summed USD $30 billion.[197]

The DR-CAFTA is a trade agreement alone (with no side agreements) comprised of 22 chapters, three annexes, tariff schedules, amendments and side letters for each party. Considered as "one of the post NAFTA FTAs", [198] and also pursuing labor standard compliance, the DR-CAFTA includes internationally enforceable labor provisions within the text of the agreement, specifically in Chapter 16-the Labor Chapter. The Labor Chapter includes 8 subsections. Supporting the Labor Chapter is the Dispute Settlement Chapter, Chapter 20, including 22 subsections and which applies to matters concerning all the agreement, being them trade issues and expanding jurisdiction to labor and environment issues.

The DR-CAFTA encourages cooperation of exchange of information and technical assistance. The legal implications of DR-CAFTA labor provisions also represent legally binding normative standards that the member countries agreed to comply with. The normative content and obligations of the DR-CAFTA refer to "internationally recognized labor rights" and limit to one single obligation which is stated in Article 16.2.1(a): "A Party shall not fail to effectively enforce its labor laws" and the norm directly reflects that internationally enforceable provisions are only those related to trade. Set forth, in Article 16.8, labor law is defined "as a Party's statutes or regulations, or provisions thereof, that are directly related to

[197] Full text of the DR-CAFTA available at: https://ustr.gov/trade-agreements/free-trade-agreements/cafta-dr-dominican-republic-central-america-fta.

[198] Gantz, "Settlement of Disputes under the DR-CAFTA," 333.

the following internationally recognized labor rights: (a) the right of association; (b) the right to organize and bargain collectively; (c) a prohibition on the use of any form of forced or compulsory labor; (d) a minimum age for the employment of children and the prohibition and elimination of the worst forms of child labor; and (e) acceptable conditions of work with respect to minimum wages, hours of work, and occupational safety and health."

Under the DR-CAFTA, new institutions are created to enforce the labor provisions. The Labor Affairs Council- LAC (Article 16.4) is comprised of cabinet-level representatives to "oversee the implementation and review progress" of the Labor Chapter. There are also designated offices within their labor ministries as contact points (Article16.4.3). Additionally, Article 16.5, "recognizing that cooperation on labor issues can play an important role in advancing development", created the Labor Cooperation and Capacity Building Mechanism (hereinafter the LCCBM) which explicitly, in Annex 16.5, describes its functions as: "to follow procedures, to enhance cooperation, consultations, and assistance among member countries and international organizations." The United States Trade Representative (hereinafter the USTR) categorized the creation of the LCCBM as "a groundbreaking mechanism to promote labor rights through specialized consultations and targeted training programs, a tool to improve labor laws and their enforcement, and build the capacity of Central American nations to monitor and enforce labor rights".[199]

All of the labor provisions in the DR-CAFTA are enforceable. When labor disputes arise, procedural measures to follow are stated in the agreement, Article 16.6, which refers to procedures to take prior to taking the case to a DSM, which is regulated on Article 20.5 and

[199] USTR, Free Trade with Central America: Summary of the U.S.-Central America Free Trade Agreement, available at: http://www.ustr.gov.

Article 20.6, the DS Chapter.[200] Under Article 16, a complaining party shall first send a written request to the party who has allegedly not complied with the provisions. In this sense, the parties should promptly meet and make every attempt to arrive at a mutually satisfactory resolution. In the case in which no resolution is agreed upon, one of the consulting parties may request the LAC to be convened. In this case, the LAC should attempt to resolve the matter through conciliation or similar means. In the ultimate case in which the parties fail to resolve the matter within 60 days under the guidance of the LAC, a request on consultations under Article 20.4 of the DS shall take place. It is very important to emphasize that the DR-CAFTA clearly states "no Party may have recourse to dispute settlement under this Agreement for any matter arising under any provision of this Chapter other than Article 16.2.1(a)," which states, "a Party shall not fail to effectively enforce its labor laws". All the claims may be done at private level, however only members can take part in the consultation stage and the request of panels.

When a case is brought to the DS phase under Article 20, another round of negotiations take place. At this point, Article 20.4 allows other members showing "substantial trade interest" to have participation in the matter in the case they justify so. The consultation process may make every attempt to arrive at a "mutually satisfactory resolution" by exchanging information to make full examinations of the matter at stake. If a resolution is not possible within 60 days (or other agreed upon period) as Article 20.5 refers to, then a request of a Commission shall take place. The Commission refers to a cabinet-level of representatives as established in the Annex 19.1. The Commission is to "resolve the dispute as promptly as possible". In cases in which the parties cannot resolve matters within 30 to 75 days (Article 20.6.3), an arbitral panel, upon request delivered by any of the parties may be established.

[200] Article 20 applies to any dispute arising within the DR-CAFTA and not only to labor provisions.

The arbitral panel is to be comprised of three members with expertise or experience relevant to the subject matter. Each party selects one member each and the panel chair shall be chosen upon agreement of both parties. In failure to agree, panelists may be chosen from a roster. Article 20.10 sets forth the "Rules of Procedure", which shall include hearings before the panel, rebuttals, consultations with non-governmental organizations (NGOs) or other concerned groups, an initial report and an implementation or final report.

After a complained-against party fails to implement recommendations set forth on the implementation or final report, Article 20.17 clarifies the "Non-Implementation in Certain Disputes" by specifically stating that an annual monetary assessment of USD $15 million annually be paid to a fund created by the DR-CAFTA Free Trade Commission. The monetary sources are to be utilized for labor law enforcement of the same country. In cases where failure to pay occurs, suspension of tariff benefits, i.e. trade sanctions, may be incurred.

5.2. The First-ever Labor Case in an RTA: The U.S.-Guatemala Labor Case: Guatemala Issues Relating to the Obligations under Article 16.2.1(a) of the DR-CAFTA

The U.S.-Guatemala case does not only represent the single labor case brought to the DR-CAFTA DSM requesting an arbitral panel, but it also represents the first-ever labor case in trade policy history that the U.S, a trade-labor linkage advocate throughout history, and any other government takes to an RTA DSM requesting the establishment of an arbitral panel. The requested arbitral panel is expected to resolve labor standard violations in matters affecting trade within the agreement, a procedure that is taking place for the first time. The case deserves a thorough analysis of the steps taken by the parties and of the precedents that have already been set forth.

5.2.1. A Seven-year Sequence of Events Leading to an Arbitral Panel Establishment

In 2008 the American Federation of Labor and Congress of Industrial Organizations (hereinafter the AFL–CIO)[201] together with six Guatemalan labor unions filed a joint complaint within the Labor Chapter against Guatemala claiming that Guatemala was "failing to enforce its labor laws" specifically those related to freedom of association and rights to collective bargaining. The claim argued that despite the DR-CAFTA ratification, labor conditions remained the same, or even worsened. One of the six claiming unions, the Coalition of Avandia Workers from an apparel export-processing zone or maquila, claimed that workers were dismissed as they joined the labor union.

The claims were filed under the U.S. Bush Administration of the Republican Party and mainly sought solution through bilateral consultations.[202] In an effort to settle the dispute, the U.S. and Guatemala attempted to negotiate a labor action plan that would establish a framework for addressing the U.S. complaint without proceeding to arbitration.[203] However, three years later, in 2011 and with no effective solutions encountered, the USTR, under the U.S. Obama Administration of the Democratic Party stated that though there were recognized attempts, "efforts had not succeeded".[204] The administration thus proceeded to move ahead with the request of an arbitral panel, as it argued that Guatemala showed no signs of enforcing points included in the labor action plan. Therefore, on August 9, 2011, the U.S. officially announced its request of an arbitral panel to rule its charges that Guatemala had violated labor provisions by "failing to enforce its own labor laws". Labor rights sources assured that the arbitral panel would have positive results since it could ultimately lead to Guatemala being

[201] The AFL–CIO is the largest federation of unions in the U.S., with more than 12 million workers being represented.
[202] The Republicans are not known for supporting labor protection as the Democrats are.
[203] *Inside U.S. Trade*, "U.S. Guatemala Discuss."
[204] *Inside U.S. Trade*, "U.S. Seeks CAFTA Panel."

assessed a monetary penalty that would go toward improving labor rights. This means that in the case in which the panel ruled against Guatemala, and both governments failed to settle the disputes, the panel could put in place an annual monetary assessment of up to USD $15 million on Guatemala according to the monetary sanctions of the DS Chapter. That money would be paid into a fund established by the two countries and spent to improve labor law enforcement in Guatemala.

Guatemalan action following the U.S. request of an arbitral panel was immediate. In response to the announcement, the following day, Guatemala refused to recognize such a request, as it alleged it was "procedurally inappropriate" and "substantively unjustified" as it claimed that Guatemala was indeed complying with all of its current laws and fulfilling DR-CAFTA labor commitments. Guatemalan Minister of Economy argued that the U.S. had to exhaust all other previous procedures stated in Articles 16 and 20 of the DR-CAFTA, which it had not done.[205] Specifically three main reasons were alleged by Guatemala. First, the U.S. did not follow the dispute settlement process outlined in the agreement as it had failed to make an argument during bilateral consultations that the labor law violations it alleged had an "impact on trade" (Article 16.2.1) between the two countries. Second, the U.S. did not hold a meeting of the Free Trade Commission with Guatemala and all other DR-CAFTA members. In response, the U.S. argued that the meeting had in fact taken place between the two countries without the other DR-CAFTA members, as Guatemala had requested it be strictly bilateral.[206] And third, that the U.S. did not convoke a meeting of the LAC as outlined by

[205] Minister of Economy, Luis Velasquez held a press conference on Aug. 17 2011 arguing that Guatemala does not oppose the request of the panel, but U.S. should first exhaust all previous procedural instances set forth in the DR-CAFTA.

[206] *Inside U.S. Trade*, "Guatemala Details Objections."
Minister Velasquez held a videoconference with trade ministers of DR-CAFTA members urging them to support Guatemala's request for a meeting of the Free Trade Commission with all DR-CAFTA parties represented; however DR-CAFTA members did not participate. This study assumes that their

Article 16.6.4. Regarding the last argument, the statement in the article suggests that such a meeting is optional rather than required – "if the consulting parties fail to resolve the matter in consultations, a consulting Party *may* request that the Council be convened to consider the matter".

Besides the failures in procedure that Guatemala argued, the labor action plan that the U.S. had proposed during the consultations period included 17 points, 14 of which Guatemala agreed upon, and three, which Guatemala refused to implement as it argued were against its Constitution and legislation. One of the points that Guatemala refused "was to return to the Labor Ministry the power to sanction employers for noncompliance with labor laws". The Labor Ministry was stripped of this authority in an August 2004 constitutional court ruling that was supported by the private business sector. The second action that the U.S. had demanded was the hiring of 100 additional labor inspectors by the Labor Ministry, however, Guatemala expressed that it was unable to meet that demand as it lacked sufficient funds in its budget. The third point was to require businesses operating under the special law promoting the growth of maquilas to post a deposit that would compensate workers in the event they are laid off. Guatemala argued that it would not be legally viable to impose this requirement retroactively on businesses operating under the law, and that it would be discriminatory to apply it only to new businesses that just signed up. Later on, Guatemala agreed on hiring 100 inspectors. The other two points to comply with still remained debated by Guatemala.

In response to the Guatemalan position, the U.S. recognized that it would not ask Guatemala to go against its legislation nor constitutional provisions, however, in relation to other points alleged by Guatemala, the U.S. proved that labor violations taking place were affecting the trade among the agreement, that meeting with the Free Trade Commission had

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participation might reveal labor standard violations taking place in these DR-CAFTA member countries.

effectively taken place between the two Parties (without the participation of the other DR-CAFTA members), and that its request for the arbitral panel would go ahead. The U.S. was clear in its position and message to the world with the proceeded action: the USTR emphasized that by seeking a panel "we're sending a strong message that the Obama Administration will act firmly to ensure effective enforcement of labor laws by our trading partners."[207]

Despite the fact that the panel had been requested, towards the end of 2011 Guatemala stated that due to its efforts and willingness to work cooperatively to resolve the dispute, the U.S. was giving more time to work out a bilateral dispute through "informal bilateral consultations to find an alternative route to resolving the labor dispute without resorting to a panel".[208] Guatemala's efforts to resolve the labor dispute outside of an arbitral panel were evident. The bilateral consultations took place and in April 2013, (one year and eight months after the request of the panel which remained deactivated), both parties in order to resolve the dispute signed the "Mutually Agreed Enforcement Action Plan between the Government of the United States and the Government of Guatemala" (hereinafter the Enforcement Plan).[209] The Enforcement Plan (based on the same legal framework as the previously failed 17-point labor action plan) includes three main Parts: A. "Ministry of Labor Investigation of Alleged Labor Law Violations in Guatemala, B. Enforcement of Labor Court Orders, and C. General Provisions", covering overall 18 main points which were to be implemented within six months. The specific commitments of the plan are: 1) strengthen labor inspections; 2) expedite and streamline the process of sanctioning employers and ordering remediation of labor violations; 3) increase labor law compliance by exporting companies; 4) improve the

[207] Trade policy in the U.S. has for long had the ongoing debate as if to pursue labor standards in trade activities. The message came as a response to the previous administration.

[208] *Inside U.S. Trade*, "U.S. Guatemala Takes Another Stab."

[209] The Enforcement Plan, full text available at: https://www.dol.gov/ilab/reports/pdf/0413GuatEnforcementPlan.pdf.

monitoring and enforcement of labor court orders; 5) publish labor law enforcement information; 6) establish mechanisms to ensure that workers are paid what they are owed when factories close. These dispositions were to be enforced nationwide with the cooperation of several institutions, including Ministries of Labor and Economy, and courts, and would have direct effects on Guatemalan maquilas. When signing the Enforcement Plan, the U.S. and Guatemala agreed on jointly requesting the established panel "to suspend its work for a period of six months from the date of the signing of the Enforcement Plan" (Enforcement Plan 2013, Final Provisions 18.1).

Six months later, Guatemala failed to implement successfully the Enforcement Plan. In April 2014, the USTR recognized the efforts done by Guatemala but pointed out that more things had to be done, and therefore the case could still not be closed and a further four-month extension was granted.[210] After the four-month extension and with no notable progress from Guatemala, in August 2014, the USTR traveled to Guatemala and emphasized the importance to ensure workers' rights and the rule of law. By complying with the agreements provisions and ensuring the protection of workers the U.S. expressed to Guatemala that the country would attract more investment and provide with more economic opportunity to nationals who currently flee the country to seek better opportunities in the U.S.[211]

On August 25, 2014, the U.S. decided to extend for the third time the Enforcement Plan by one month instead of reactivating the panel, "specifically, Guatemala has not yet passed legislation aimed at expediting the process by which fines are imposed on employers for violating labor laws".[212] The inside economic environment of Guatemala is relevant to consider. The Guatemalan private business sector as well as the public sector, has specific

[210] *Inside U.S. Trade*, "USTR Extends Guatemala."
[211] Ibid.
[212] Ibid.

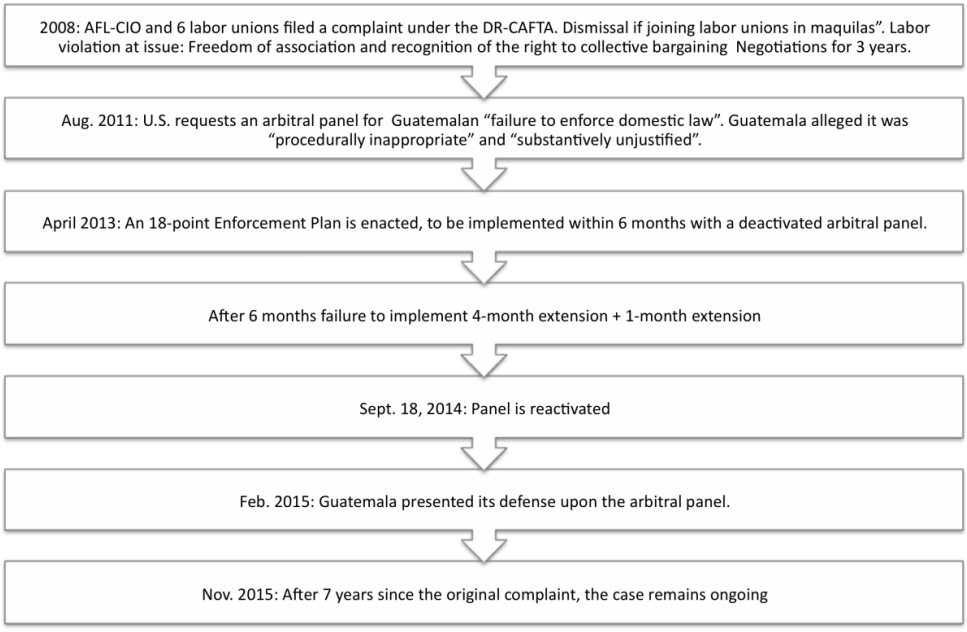
commitments with investing companies, in many cases multinational companies (MNCs) in granting them legal security and keeping sound investment opportunities. The labor violations that originally brought the labor case to the RTA happened inside maquilas. Maquilas represent footloose companies, meaning that they can easily close operations in any location and relocate across borders, as they keep no ties with the territories in which they are established. Sanctioning employers would make these companies move elsewhere and such actions would cause significant detriments to the Guatemalan economy. Maquilas have long been sources of employment, generating foreign exchange earnings, transferring technologies and know-how, among other benefits. In particular, DR-CAFTA members are competitive in the maquila sector as they offer low-cost labor markets, sound investing environments, expedite and streamlined procedures for investments and initiating operations, and expedite customs procedures facilitating imports and exports.[213] Commitments and pressures of the private sector to protect investors and keeping sound and secure business environment for exporters may create non-compliance with the specific U.S. request of sanctioning employers violating labor standards.

With such non-compliance, a press release stated that the U.S. Government "retains the right to reactivate the arbitral panel at any point during the next four weeks."[214] The AFL-CIO expressed concern and hoped for it to be a final delay. AFL-CIO representatives argued that only an arbitral panel would provide leverage for Guatemala to do its duty and protect fundamental rights. USTR however expressed that though the DS is a means of achieving labor rights protection, they would like to "support changes on the ground and not punish

[213] Servicios al Exportador, Asociación Guatemalteca de Exportadores, see http://export.com.gt/agexport/acerca-de/.

[214] *Inside U.S. Trade*, "U.S. Restarts Guatemala."

Figure 2. The sequence of events in the U.S.-Guatemala case, 2008 to 2015



Source: Original by author

Guatemala."[215] A joint statement from the involved unions in the case charged that the Enforcement Plan had only achieved minimal formal changes with no real improvements for workers. Figure 2 illustrates a summary of the sequence of events in the U.S.-Guatemala case from 2008 to the date. After the third extension and allegedly with little progress observed by the U.S. of Guatemalan implementation of the Enforcement Plan, the USTR on September 18, 2014, announced the reactivation of the arbitration panel originally launched in 2011.[216] On February 2, 2015 Guatemala provided an initial written submission[217] and on February 13, 2015 Guatemala initiated its defense upon the arbitral panel. The case remains ongoing.[218]

[215] Ibid.
[216] Ibid.
[217] Initial written submission by Guatemala, see: https://ustr.gov/sites/default/files/enforcement/labor/NON-CONFIDENTIAL%20-%20Guatemala%20-%20Initial%20written%20communication%20%202-02-2015.pdf
[218] *Inside U.S. Trade*, "Mounts Defense in CAFTA."

Currently, the initial confidential ruling by the arbitral panel has been delayed by more than three months to December 15, 2015 "due to the complexity of the dispute," according to letters between the parties and the panel chair.[219] Previously, the panel had been due to release its initial report to the U.S. and Guatemala on September 8th, but the panel on August 11th asked the U.S. and Guatemala to push the deadline back to December 15th. Neither government objected in separate responses sent to the panel. Both the USTR and the panel cite that factors that have led to such delays are that the issues are complex and the submission and evidence presented to the panel are voluminous. The U.S. submitted over 230 exhibits comprising of 230 pages.[220]

The U.S.-Guatemala case may be considered as an experimental tool on trade policy studies and labor procedures taking place within an RTA. The Enforcement Plan represents a new kind of legal instrument and the deliberations of both parties before an established arbitral panel are certainly creating lessons for countries in future labor issues that might take place in other RTAs worldwide, including in the TPP.

5.2.2 Discussion: Strengths and Weaknesses in the U.S.-Guatemala Case

The U.S.-Guatemala case is quite important for scholars and practitioners as it represents an ongoing experimental case of the first labor case brought to an RTA-DSM. It concretely represents a lack of enforcement of the domestic law from the Guatemalan side, and the intervention and pressure of the U.S. through DR-CAFTA-DSM to enforce labor laws by requesting the establishment of an arbitral panel.

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[219] *Inside U.S. Trade*, "Initial Ruling Delayed."

[220] Ibid. The U.S.-Guatemala case remains ongoing; follow-ups on the case available at: https://ustr.gov/issue-areas/labor/bilateral-and-regional-trade-agreements/guatemala-submission-under-cafta-dr

The request of an arbitral panel by the U.S. released pressure on Guatemala to accelerate and improve its diligent enforcement on domestic labor laws. This study considers the pressure as strength as it may have positive effects on third parties, particularly on the other DR-CAFTA members to be more diligent in enforcing their own domestic labor laws. The U.S. request proves that the DR-CAFTA-DSM will indeed be utilized by either one of the parties when labor law violations are detected. In history the U.S. has always been a strong promoter to include labor provisions in the MTS, though such attempts failed. The U.S.-Guatemala case reflects U.S. success in including the trade-labor linkage in RTAs, and its determined attitude to utilize the DSM. The case also raises awareness and may inform labor unions in any of the other countries that complaints may be filed under the DR-CAFTA as the agreement allows labor groups, associations, unions, or other NGOs to file complaints, though later they have to be represented at the state level during consultations, meetings, and bilateral negotiations.

The study also identifies weaknesses in the procedures and substantive norms. First, as the DR-CAFTA was born from negotiations and the *bona fide* of the parties to engage in trade activities it may create a weak, delayed procedure, almost entirely based on negotiations without ever reaching an end point. The case was originally filed in 2008. Three years later, in 2011, an arbitral panel was established and at the same time deactivated. During the following three additional years, negotiations were attempted to reach a solution to the controversy outside of the arbitral panel, though such negotiations, lengthy in time, failed. In 2014 the arbitral panel was reactivated. This means that workers that were originally deprived of their CLS, and their successors cannot yet see a concrete resolution of the dispute. Bilateral talks at the governmental level may cause delays that produce direct negative effects for workers, who represent the main focus of labor standard protection.

A second weakness derives from the substantive essence of the norm. To bring a case to the DSM, the party must prove that labor violations indeed affect trade within the agreement. The justification for this argument might be subjective. While the filing party might argue that the labor violation substantially affects trade within the RTA, the defending party might deny so. The legal text of the DR-CAFTA needs to provide a parameter of how to consider if labor violations have direct effects on trade.

A third weakness might be created by the change in the administration of parties involved. This means that while negotiations might be taking place outside of an arbitral panel to solve labor disputes within the RTA model, a new administration, with new cabinet members and different trade policies may cause direct negative effects to the ongoing negotiations causing delays in the procedure. Such delays would only affect workers, as labor cases would not be solved in considerable procedural periods. The previous argument may be justified with the U.S. Democrats stating their political will that the Obama Administration wanted to "send a message to the world that labor standard enforcement was going to be pursued". Though this represents a politically based argument, it may directly affect the legal enforcement mechanisms of RTAs in delaying the procedural aspects contained in the labor provisions of the RTA model.

A fourth weakness is that there is no monitoring institution that follows the implementation of the accorded points in the Enforcement Plan. The DR-CAFTA established the LCCBM and at the time of the creation the USTR recognized it as a "groundbreaking mechanism". Based on the norm, this mechanism has attributes to convene and carry on cooperative actions between the parties. In the U.S.-Guatemala case, the interventions of the LCCBM could not be found. Organizations such as the Human Right Watch (HRW) argue

that the mechanism has fallen short of budget and therefore it has not been actively present.[221] The LCCBM may serve as an impartial support for both parties in negotiating and monitoring the implementation of the Enforcement Plan, given that the signing parties already agreed to its existence and functions at the time of signing the DR-CAFTA.

As noted by the USTR, the DR-CAFTA is strengthening workers' rights and conditions in the region, through enforcement of labor protections to which its workers are entitled under countries' national laws. The DR-CAFTA has the first labor dispute under any RTA. The case is motivated by the U.S. to ensure Guatemalan workers inside maquilas they can exercise their rights under Guatemalan labor law. The commitment and aim of the U.S. in this case is to make Guatemalan government enforce its law to uphold internationally recognized labor rights.[222]

The U.S.-Guatemala case reveals the well and the ill functioning of a DSM created within one of the chapters included in an RTA model. The findings, though still not yet fully justified, as the case remains ongoing, may serve as a new departing point for future drafting of labor provisions within an RTA model and/or for amendments of existing ones.

5.3. The Trade-Labor Linkage. Concluding Notes

Trade and labor have a natural linkage and this linkage has been recognized by both levels of the IEL, the multilateral and regional levels, and included in the regional level. At the same time EPZ issues are inseparable with labor issues.[223] As could be seen from the preceding subsections of the present chapter, many labor violations within the NAALC and

[221] Human Rights Watch available at: http://www.hrw.org/legacy/backgrounder/arms/hearing0405/hearing0405.pdf.

[222] USTR, available at: https://ustr.gov/trade-agreements/free-trade-agreements/cafta-dr-dominican-republic-central-america-fta.

[223] ILO, "La Industria de la Maquila en Centro América," 1.

the DR-CAFTA have taken place inside EPZs. There is the imminent need for the protection of CLS of workers inside EPZs.

The positive effects that CLS protection brings to economic growth are undisputed. Stiglitz in challenging the neo-classical assumption that labor is just another factor of production, argues that the "high road to economic development, surely including the freedom of association and right to collective bargaining, can increase efficiency by, *inter alia*, promoting the increased buy-in by workers to the goals of the immediate work group. This in turn, can lead to higher productivity via a voice mechanism."[224] He also argues "collective bargaining can enhance the overall efficiency of the economy by facilitating income redistribution that would not occur or would be more costly to implement, through the tax/welfare system."[225]

There can be many economic benefits that can result from the enforcement of CLS. Freedom of association, collective bargaining and tripartite dialogue are necessary elements for creating an environment that encourages innovation and higher productivity, attract FDI, and enables the society and economy to adjust to external shocks such as financial crises and natural disasters.[226]

As reviewed in the present chapter, the trade-labor linkage has been possible to be included in RTAs rather than in MTAs. The cases submitted to both the NAALC and the DR-CAFTA show the extent to which the EPZ host governments have been violating CLS within the trade agreements. Level of impunity as well as indifference and lack of transparency from domestic labor courts was reflected. Therefore, a question on how trade agreements can help

[224] Stiglitz, "Democratic Development as the Fruits of Labor," 16.
[225] Ibid.
[226] OECD, *International Trade and Core Labour Standards*, 32.

ensure compliance in developing countries that offer low-cost labor force and other regulatory incentives to MNCs to enhance economic growth is raised.

Despite some failures in the procedures for labor standard enforcement in RTAs, the analysis based on the NAALC provides with lessons on the effectiveness of a trade-labor linkage inclusion in RTAs. The submission of the 39 cases, though none has requested the establishment of an arbitral panel, they have implicitly shown that there is some basis to the submissions brought against the employers and governments involved. Even though the mandate of NAO are criticized because it is not adequate by many or because of "lack of teeth" which means that not all the obligations are internationally enforceable, pressure is put on governments and on employers to bring about changes for improvement. The procedure in this way reveals positive effects. For instance, in the case of Mexico some MNCs have taken steps to bring their actions in compliance with national labor laws.

Table 13 provides with a comparative analysis of NAFTA-NAALC and DR-CAFTA. It synthesizes the substantive, institutional, and procedural aspects of the NAFTA-NAALC and DR-CAFTA labor provision that have been analyzed in the present chapter.

Table 13. Internationally enforceable Labor Provisions in the NAFTA-NAALC and DR-CAFTA

	NAALC (1994) (Signed under the Omnibus Trade and Competitive Act of 1988)	**DR-CAFTA (2006) (Signed under the Bipartisan Trade Promotion Authority Act of 2002)**
Signatory countries	Canada, Mexico, and the United States	United States, Dominican Republic, Costa Rica, El Salvador, Guatemala, Honduras, and Nicaragua
Obligations undertaken	Does not refer to ILO Conventions. Labor Principles in Annex 1	Refers to "internationally recognized labor rights". (Art.16.8)
Legal Implications	Legally binding normative standards	Legally binding normative standards
Enforceable Provisions	A Party's persistent pattern of failure to effectively enforce its occupational safety and health, child labor or minimum wage standards (Art.29), not including matters related to freedom association and collective bargaining.	A country shall not fail to effectively enforce its labor laws in a manner affecting trade between the parties. (Art.16.2.1), including matters related to freedom association and collective bargaining.
Scope of DSM	Labor issues concerning trade relations within the FTA (Annex 23)	Labor issues concerning trade relations within the FTA (Art. 16.2.1.(a))
Institutions created	Commission for Labor Cooperation (CLC) (Art.8) National Administrative Office (NAO) (Art.15)	Labor Affairs Council (LAC) (Art.16.4) Labor Cooperation and Capacity Building Mechanism (LCCBM) (Art. 16.4.3)
Standing (Government or private sector)	Private parties can submit complaint and participate in the consultations (Art.16.3) Only governments have authority in the DSM, ECE, and Arbitral Panel Stage (Art.20-29)	Private parties can submit complaints. Only governments can participate in Consultations and DSM, Arbitral Panel Stage (Art. 16.6, Art. 20)
Enforcement mechanisms	Limits on monetary enforcement assessments of US$ 20 million (Annex 39) Suspension of trade benefits (Art. 41)	Limits on monetary penalties of US$ 15 million Suspension of trade benefits (Art.20.16, Annex 20.17)

Source: Original by author.

In relation to the NAFTA-NAALC, Compa states that the NAO review process, though no sanctions are imposed, has forced private businesses and governments to review their corporate actions and to have subordinate officials explain their decisions to superiors as follows:

> "On stage they had to explain corporate conduct and governmental administration, and to defend themselves in the court of public opinion and political judgment …[E]asy access for trade union and worker complainants to public review and public hearing on the types of issues raised in the first NAO cases might [make] companies more careful in their employment policies where union organizing is underway, and make Mexican labor law authorities more evenhanded in their treatment of independent unions and more assertive on behalf of workers discharged for organizing." [227]

The NAO acts in many respects like the ILO when they take up labor rights issues. Though some of the obligations lack sanctions, there exists a forum for labor rights advocacy that has an effect of its own. Workers may claim labor standard protections and claim violations under the provisions enshrined in the respective RTA. This may be greatly beneficial for the industrial relations between RTA members. Addo states that "the conduct of the NAO in reviewing cases has been compared to the ILO in the taking up of labor issues. Even where the sanctions are not sanctionable, the provision of a forum for promotion of workers' rights has helped tilt the balance of power, which used to be solely within the confines of management."[228]

Addo confirms that "the public forums are an important step in ensuring that the public is informed of the workings of MNCs in their countries and other NAFTA countries, making the companies accountable, which without the NAO process would not have been

[227] Compa, "The First NAFTA Cases," 178.
[228] Addo, *The Global Debate*, 287.

possible."[229] NAO forum allows review of cases; it puts on the spotlight issues that otherwise would may not have been perceived.

Table 14. Trade-Labor Linkage Inclusion in RTAs – the Pros and the Cons

Pros	Cons
Based on the *bona fide* and mutual interests: Procedural aspects always give priority to negotiations and bilateral talks prior to establishing an arbitral panel.	Based on the *bona fide* and mutual interests: Never ending negotiations to reach agreements.
It has created a new forum for the protection of labor violations	Too flexible periods of compliance
Has risen awareness of the victims of labor standard violations to file cases and private parties can submit complaints	Though private parties can submit complaints, at later stages the negotiating parts should be raised to the state level.
It exerts pressure on governments to comply with ILO standards. Intl. reputation of states to comply with CLS.	The state (government) can seek its own interests which might differ from those of the workers. Interests with powerful private enterprises.
MNCs have new commitments *vis à vis* governments, workers, and final consumers. Care for their corporate image.	Both alleging parties are parts of a trade agreement in which both have interest in; retaliation seems unlikely
Alternate means of protecting domestic labor law of RTA signing members. Retaliation is possible	

Source: Original by author

In the U.S.-Guatemala case, besides the forum that the agreement created for labor issues as it did in the NAALC, the Enforcement Plan represents a promising sign of how to bring about the necessary changes by ensuring that the government meets its obligations in adhering to the CLS, both as an ILO member and as DR-CAFTA member. This commitment is positive as it also can extend to the other members of the agreement. It exerts somewhat of a positive pressure to governments and other members. Table 14 enlists the positive and negative findings in including the trade-labor linkage in RTAs from the NAALC and DR-CAFTA lessons.

As it is a relative new trend in which cases remain ongoing in both RTAs, the general effects can be considered positive as lessons can be learned to improve the righteous implementation so that workers in EPZs engaged in international trade can enjoy good

[229] Ibid., 286.

working conditions. Addo states that "the issue of adherence to CLS is a combination of increased trade, cooperation, and capacity building, leading to strong government institutions, trade incentives, and – equally important – political will. This shows how a multifaceted approach is vital in promoting compliance."[230]

This chapter has provided an analytical policy and practice of trade-labor linkage inclusion in RTAs, and important lessons for trade policy have been drawn from the NAALC and DR-CAFTA perspective. However, it is still quite early to conclude that the trade-labor linkage inclusion in RTAs is either positive or negative. Nonetheless a foreseen path is that the trade policy trend of trade-labor linkage inclusion in RTAs rather than in MTAs will prevail. The Trans-Pacific Partnership (hereinafter the TPP), the most ambitious RTA in history, covering the longest list of issues and the largest region for an RTA ever, has included a comprehensive labor chapter in its final text. Chapter 19, the Labour Chapter of the TPP, is dedicated exclusively to labor standard protection and enforceability.[231] It is has been stated by the U.S. government that the TPP "includes the strongest labor provisions ever."[232] This shows that the trade policy trend is to continue at least, for a long run.

[230] Addo, *The Global Debate*, 304.

[231] A full text of the TPP Labour Chapter can be seen at https://ustr.gov/sites/default/files/TPP-Final-Text-Labour.pdf.

[232] https://ustr.gov/trade-agreements/free-trade-agreements/trans-pacific-partnership/tpp-chapter-chapter-negotiating-4.

Chapter 6. International Soft Law and Export Processing Zones

There is a great variety in the degrees and forms of legalization in today's globalizing world. In the previous sections, the study has given an insight on the formal IEL provisions. These forms of legalization are all encountered in the traditional hard law realm, which have prevailed in the societies since the first forms of law. Hard law represents legal binding instruments created at the state level or by negotiations of sovereign countries in the form of international agreements, recognized by the domestic law and therefore implemented through the public enforcers.

Nonetheless, today various types of legal forms rule over the various types of industrial policies. Soft law, *vis-à-vis* hard law, is considered a quasi-legal non-binding instrument, voluntarily created, accepted and followed by non-state actors such as by MNCs, which play an important role in today's globalized world. International soft law is stated in various forms. Corporate Social Responsibility (hereinafter CSR) and CoC are very well known soft law provisions. These provisions are created by international organizations or by private MNCs with aims to ensure to the final consumers of trade in goods and services that private businesses adhere to clean production processes.

Keller recognizes the existence and legitimacy of these private actor arrangements as follows:

> "The issue concerning the regulation of international business conduct is superheaded by voluntary codes of conduct developed by non-state actors and thus outside the conventional realm of international state relations. Private and non-binding as they are, these codes nevertheless perform a public function in putting forth ethical claims of good corporate practices." [233]

[233] Keller, "Corporate Codes of Conduct," 36-37.

The present study as well, rather than considering the international soft law as a level *per se* within the IEL, considers it within the international soft law realm. The present chapter identifies the globalization and significance of international soft law; it offers an analysis of the role of international soft law CSR CoC, as contemporary supportive legal tools for achieving EPZ compliance with the IEL. Also, the relationship between CSR and sustainable development is stated.

6.1. The Significance and Globalization of International Soft Law

In today's globalizing world where rules on hard law and soft law rule the trade among countries, it is also necessary for the different stakeholders in trade activities to ensure compliance of EPZs with the IEL. The stakeholders are among the public and private actors, such as states and MNCs, who play predominant roles in international trade. These actors should promote the protection of CLS that also represent basic human rights of workers in EPZs.

The international soft law plays a leading role in achieving such compliance. Today, globalization does not only connote economic activities, but has social implications as well. Worldwide, there have been important areas of consensus concerning the social dimensions of globalization in the context of the ILO. Since the World Summit for Social Development in Copenhagen of 1995, international consensus has been achieved on the four CLS. This led to the adoption by the International Labour Conference (hereinafter ILC) in 1998 of the ILO Declaration on Fundamental Principles and Rights at Work and its follow-up.[234] As noted in the previous chapter, labor standards are also prominent in the agenda of most RTAs.

[234] ILO Declaration on Fundamental Principles and Rights at Work and its follow-up, available at: http://www.ilo.org/declaration/thedeclaration/textdeclaration/lang--en/index.htm

Globalization may bring many benefits to countries and people worldwide; however, negative effects will always take place when labor standards of workers are violated. These kinds of violations often take place in EPZs and maquilas. In this way, private parties, such as MNCs, in their corporate interest of ensuring to final consumers their compliance with CLS and protection of human rights in their operations, have on their own elaborated CoC. These CoC express their willingness to implement CLS in their operating policies. Therefore, it can be said that CLS have become globalized, as they are standards to be implanted worldwide. Today not only the states, but also the MNCs are showing responsibility in complying with ILO CLS through CoC that they voluntarily create.

These voluntary instruments carry great weight. Unlike other legal instruments that states traditionally and formally create, these instruments are created by enterprises, raising in this way the credibility that partner private enterprises might have and raising the awareness of the public opinion in clean production processes. Consumers become aware of labor standard protection by companies from which they purchase goods and services. When enterprises do not respect the fundamental social principles provided in the ILO and endorsed by CoC they are severely sanctioned by consumers where it hurts the most, i.e. by not buying their goods or services. In this sense, soft law tools may be equally or even more important than so-called legally binding instruments, which are unilaterally imposed and whose effective implementation can often be guaranteed through due processes and the imposing of sanctions. The sanctions, monetary or trade sanctions, apply only to states and not to private parties such as MNCs. As noted in the U.S.-Guatemala case, prior to the sanctions, never-ending negotiations might take place among the interested parties, i.e. the involved states, in RTAs.

The guidelines that promote soft law, such as the OECD Guidelines for Multinational Enterprises support companies doing their business in a positive way. They provide images of good conduct to enterprises engaged in world trade; if followed, companies are lifted above criticism, giving them the corporate image that they behave in a way the world society at large expects from them.

Besides the corporate image that guidelines can give to the enterprises, the employees and their representatives can also achieve positive impact. Employees like to work for "good employers, who enjoy public respect". In this way, complying with international soft law, guidelines, and CoC has a strong appeal: they are a call from society, respond to the need of enterprises and serve the interests of the employees and communities as well.

There is a need to compromise company law and operations with the IEL. The growing concern of some governments with the phenomenon of MNCs constituted the starting point, after 1970, for renewed international efforts to regulate direct investment activities. The OECD was established in 1960. After lengthy negotiations, the governments of the OECD member countries adopted on June 21, 1976 the Declaration on International Investment and Multinational Enterprises. After 1977 a question arose as to the relationship between the OECD Guidelines and the ILO Tripartite Declaration of Principles. Pointing to differences in both geographical scope and material coverage, the 1979 OECD Review Report stated:

> "Wherever the ILO principles refer to the behavior expected from enterprises, they parallel the OECD Guidelines and do not conflict with them. They can, therefore, be of use in relation to the OECD Guidelines to the extent they are of a greater degree of elaboration. It must, however, be borne in mind that the responsibilities for the follow-up procedures of the OECD Guidelines." [235]

[235] Williams, *Global Institutions Corporate Social Responsibility*, 52.

Labor standards in the first place have to be implemented by corporations. They are as employers, the actors in labor and employment *par excellence*. Indeed they have to apply labor standards on a daily basis. Legally binding international agreements addressed to MNCs also regarding labor issues were not realistic, since the political will to do so was lacking. Governments have to rely on non-legally binding instruments, namely voluntary CoC, in order to see to it that labor standards are respected worldwide. Today, Governments united in international bodies like the UN, the ILO, the OECD, the NAFTA, or the DR-CAFTA, have developed codes of conduct for MNCs.

6.2. Rules on Corporate Social Responsibility and Codes of Conduct

The World Business Council for Sustainable Development (hereinafter the WBCSD) defines CSR as "the continuing commitment by business to contribute to economic development while improving the quality of life of the workforce and their families as well as of the community."[236] CSR and CoCs encompass the economic, legal, ethical, discretionary, and philanthropic expectations that societies have of organizations at a given point in time. This is to ensure business accountability and clean (environmentally and socially) production processes.

Today, companies are considered as socially responsible political actors in the global economy. As institutions they can generate not only material wealth but also wealth that nourishes the full range of human needs. The strict division of labor between the private and public sectors is no longer a reality nowadays. Under the rubric of CSR, corporate citizenship, or sustainability, companies are increasingly taking responsibility for problems in the wider

[236] World Business Council for Sustainable Development - WBCSD, available at: http://www.wbcsd.org/work-program/business-role/previous-work/corporate-social-responsibility.aspx.

society. "The role of business is seen as a community of persons and that this community can foster development of society as well as people."[237]

CSR, as a new field of management studies began to emerge in the early 1950s and took on added importance in the 1990s. CSR is thought to be "that behavior of business that seeks to solve social problems in the wider society that would not ordinarily be addressed in the pursuit of profits."[238] Williams recognizes that "in the new millennium, many argue the business case for CSR under the rubric "sustainability." Sustainability is a widely used term by companies around the world to discuss their CSR activities."[239] Sustainability was first defined in the 1987 Report of the World Commission on the Environment and Development, the Brundtland Commission: "Sustainable development is development that meets the needs of the present without compromising the ability of the future generations to meet their own needs."[240] The main focus at this time was on the environment. Nevertheless, today the term has been broadened to any kind of environment that leads to business success. Williams states that "the environment necessary for business long-term survival is thought to be the physical environment, the economic and governance issues, and the social/ethical climate. Sustainability focuses on the long-term contribution of business to society and the impact of such activity on future generations."[241]

Within globalization and trade liberalization, scholars and practitioners consider that the role of business is far beyond generating private profits. Rather, today businesses have corporate responsibility to help improve social problems that may be encountered in the society. Williams states that "business is not only responsible for its private goods, but also to

[237] Williams, *Global Institutions Corporate Social Responsibility*, 1-2.
[238] Ibid., 5.
[239] Ibid.
[240] World Commission on Environment and Development, *Our Common Future*, 43.
[241] Williams, *Global Institutions Corporate Social Responsibility*, 26.

some extent for the common goods. In the final analysis, for business to flourish, society must flourish."[242]

6.3. Corporate Social Responsibility and Sustainable Development

It is of interest to note that since 2013 corporate leaders have put sustainability on their agendas. Williams states that businesses are "recognizing the growing relevance and urgency of global environmental, social and economic challenges. Over 7,000 companies in 140 countries have joined the UN Global Compact and adopted a principles-based management and operations approach."[243] The UN Global Compact is the world's largest CSR initiative. It represents a call to companies to align strategies and operations with universal principles on "human rights, labor, environment and anti-corruption, and take actions that advance societal goals."[244]

The investment community is increasingly considering the materiality of sustainability, more often considering factors such as sound environmental stewardship, social responsibility and good ethics in calculating a company's long-term value. The reason for this fundamental transformation is because companies have gone global. They have built global value chains and invested in new markets. This has brought with it rapid diffusion of know-how and helped hundreds of millions of people to escape absolute poverty while ensuring growth.

Sustainability has direct effects on the investing companies establishing EPZs. The reason is because in many cases EPZs use low-cost labor intensive manufacturing processes and these companies want to ensure to the final consumers that the products holding the MNCs label are adhered to specific CSR or CoC and that processes were ethical and

[242] Ibid., 27.
[243] Ibid.
[244] United Nations Global Compact available at: https://www.unglobalcompact.org/what-is-gc.

compliant with law. Though CSR and CoC represent private business practices, the Organization for Economic Cooperation and Development refers to the "voluntarily and not legally enforceable rules encouraging MNCs to pursue CSR."[245] Likewise, the International Organization for Standardization (hereinafter ISO) has introduced ISO 26000 guidelines which recommend CSR policies in 7 areas to MNCs.[246]

6.4. Private Business Codes of Conduct and Export Processing Zones - The World Responsible Accredited Production

In the late 1990s there was a growing call for global ethics. From various parts of the world, proposals were emerging for a new global code of conduct.[247] There is an ever-increasing concern that human rights in developing countries should be promoted and protected.[248] The basic premise is that good ethics means good business. Business needs predictability in order to thrive, and ethic codes ensure that predictability has a chance. A global ethic is a requirement of the situation of the shrinking borders in globalization. The nature of globalization is such that the role of firms has been being defined like the roles of national and global institutions.

Voluntary efforts to define and implement appropriate standards for business conduct constitute one of the most noteworthy trends in international business in the last few decades. The issuance of voluntary CoC has been an important face of this development. CoC are written expressions of commitment to a given standard of business conduct. Individual businesses, business associations, non-governmental organizations, governments, and inter-

[245] OECD, Guidelines for Multinational Enterprises, 17, available at: http://www.oecd.org/daf/inv/mne/48004323.pdf

[246] ISO, 26000 Social Responsibility, available at: http://www.iso.org/iso/home/standards/iso26000.htm.

[247] Examples are the Caux Round Table Principles, work of the Japanese, European and U.S. business leaders and the CERES Principles destined to protect the worldwide environment.

[248] In the case of the apparel industry, the U.S. White House Apparel Industry Code of Conduct.

governmental organizations issue them. Labor issues are often discussed in these codes. Surveys carried out by the OECD reveal that, from 246 codes in total, environmental management and labor standards dominate among other issues.[249]

The reasons for issuance and implementation of related management systems may be several. The OECD states the following:

> "Companies wish to integrate broader CSR initiatives with their efforts to comply with laws, to preserve and enhance their corporate reputations as important business assets, to reinforce their ability, to compete in tight labor markets, to boost employee morale and loyalty to the firm, and to become eligible for financing from ethical investing funds."[250]

A worldwide renowned CoC is the World Responsible Accredited Production (hereinafter WRAP). The WRAP is founded on 12 basic principles and has worldwide membership of MNCs establishing textile EPZs.[251] It is the world's largest facility-based social and environmental certification program, mainly focused on the apparel, footwear, and sewn product sectors. Facilities adhered to the WRAP receive a certification of six months to two years, based on compliance with the 12 principles. The 12 principles of the WRAP are: "1. Compliance with laws and workplace regulations; 2. Prohibition of forced labor; 3. Prohibition of child labor; 4. Prohibition of harassment or abuse; 5. Compensations and benefits; 6. Hours of work; 7. Prohibition of discrimination; 8. Health and safety; 9. Freedom of association and collective bargaining; 10. Environment; 11. Customs compliance; and 12. Security."[252] Adhering to this CoC gives companies prestige and clean corporate image to

[249] Other issues are consumer protection, bribery, and corruption. See OECD, "Codes of Corporate Conduct Expanded Review of their Contents", Working Paper on International Investment 2001/OECD publishing, available at: http://dx.doi.org/10.1787/206157234626.

[250] OECD, *International Trade and Core Labour Standards*, 73.

[251] Worldwide Responsible Accredited Production, available at: http://www.wrapcompliance.org.

[252] Ibid.

intermediate and final consumers, especially when considering that business accountability is quite influential for EPZ success (or failure) in worldwide corporate life.

6.5. International Standards for the Conduct of Firms

International organizations that have created soft law provisions destined for corporate operation of large MNCs and companies engaged in trade are the ILO with the Tripartite Declaration of Principles concerning MNCs and Social Policy and the OECD Guidelines for MNCs. Following is an overview of the provisions.

> "1. The ILO with the Tripartite Declaration of Principles concerning MNCs and Social Policy. The sixth review of the ILO Tripartite Declaration was concluded in 1997. The analysis concluded that over the years there has been a fairly wide degree of observance of the Tripartite Declaration and that, on the whole, the social and economic effects of MNCs have been positive.
> 2. The OECD Guidelines for MNCs. The OECD Guidelines are non-binding recommendations addressed to MNCs by adhering OECD member countries and four non-members countries: Brazil, Argentina, Chile, and Slovak Republic. The recommendations that cover such areas as employment and industrial relations, environment, among other issues, seek to ensure that MNCs operate in harmony with government policies, to strengthen the basis of mutual confidence between enterprises and the societies in which they operate and to help improve the FDI climate.
> One chapter of the Guidelines addresses employment and industrial relations. It urges firms to: respect workers' rights to freedom of association; to provide information and facilities to employee representatives: to communicate effectively with employees so as to enable them to obtain a fair view of the enterprises' performance; to train employees not to engage in discrimination in their employment practices." [253] (underline original)

The international standards that the ILO and the OECD have provided in the form of non-binding recommendations reflect the importance that international organizations give to the role of international soft law in trade practice. These international organizations encourage firms to voluntarily harmonize with public policies given by governments and to strengthen the confidence that should prevail with the societies in which they operate. The international standards set forth in the Principles concerning MNCs and in the Guidelines for MNCs

[253] OECD, *International Trade and Core Labour Standards*, 72.

promote a public-private partnership of social responsibility in international trade. With such public-private partnership prevailing, the regulatory incentives granted to the investors that establish EPZs would never be intended to violating internationally recognized CLS. Each stakeholder in the implementation of EPZs as industrial policies, i.e. government, MNCs, and workers, would assume their own role and responsibility in complying with rules provided in the different levels of the IEL.

Chapter 7. A Multilateral and Regional Synergistic Approach: RTAs as catalysts for EPZ compliance with MTAs

The present study has determined the extent to which the new and proposed global trade rules under the MTAs and RTAs restrict the ability of developing countries to establish effective industrial policies. Insights on the existence of multilateral and regional provisions that provide the rules for international trade among countries and the clashes that take place with EPZs in a globalized world has been closely reviewed. Considering that developing countries' policy space has been limited, there is a need to determine the policies that countries can still implement and how to implement them, to either preserve, or expand the existing policy space. There are huge concerns that the policy space has been limited to countries that need development the most.

The present chapter offers the legal framework in which EPZs, as industrial policies, can harmonize with trade liberalization rules, and thus comply with the multilevel IEL. Rather than proposing amendments to the WTO Law, the designed framework utilizes the existing instruments in the multilateral and regional levels of the IEL and includes the proper provisions in them, which make EPZs comply with the IEL. The framework has the synergistic effects that the RTAs can create with the MTAs.

7.1. Harmonization of EPZs and the Multilevel IEL – Designing an Appropriate Legal Framework.

The framework proposed is designed with the already existing tools found in the multilevel IEL. Reasons that prevent the study from proposing amendments to the MTS lie in the fact that currently the MTS is deadlocked at the current Doha Round. Smooth negotiations between the WTO members have not been possible. Stagnation has taken place since the unanticipated disappointments of the Uruguay Round, for many developing countries it

created resentments regarding the WTO system. These resentments have surfaced in the Doha Round, making it extremely difficult to reach consensus on a new trade agreement. The developed countries in fact acknowledged their resentment at the outset by calling it "the development round, which, ironically, fostered unrealistic expectations among developing countries and only made matters worse."[254] Proposals to amend the existing WTO Law might take time to be digested by the MTS and thus immediate effects would seem less than possible.

Provisions of the IEL at the regional level have taken on great importance in recent decades. Regionalism has come to cover issues that the MTS has not been able to cover and which are still on the table in the Doha Round. At the same time and as stated in the previous chapter, the role of private businesses to foster development through international trade has also gained interest and momentum. CSR rules and the awareness of MNCs to comply with international trade rules have increased. With stagnation in the MTS, the proliferation of RTAs, and the gain of momentum of the roles of private MNCs and their responsibility to comply with certain standards that are also contained in the IEL, the study designs the appropriate legal frameworks so that EPZs, as industrial policies, can harmonize with MTAs and thus comply with the IEL.

Gallagher reaffirms the study's approach by stating, "today we should find avenues for reform."[255] Utilizing the available policy space can lead to practical and immediate IEL compliance. Amsden states "countries can creatively adhere to the letter but not necessarily the spirit of the WTO Law in order to achieve development. For instances, Thailand and

[254] Jones, *The Doha Blues*, 47.
[255] Gallagher, "Globalization and the Nation-State," 2.

Taiwan craftily set up effective control mechanisms to steer the private sector toward growth and innovation while avoiding the bite from the WTO."[256]

Today developing countries seeking to industrialize may expect to utilize beneficial tools offered by both the GATT and the WTO. However, such use is not possible. Amsden points out that the major difference between the two trade regimes (the GATT and the WTO) from the perspective of developing countries seeking industrialization is that in the WTO, export subsidies are prohibited based on Article 3 of the ASCM. These prohibited subsidies are very characteristic of EPZs. After the Second World War, many countries achieved upgrading from low technology to mid-technology through the use of these exports, which was the condition for operating in protected domestic markets.

With the aforementioned, the framework proposed in the present study utilizes the already existing tools in the different levels of the IEL. First, in relation with the fiscal incentives that contravene the WTO Law, the study proposes alignment with the ASCM as this would make EPZs upgrade and diversify and lead countries to development. Likewise, EPZ exemption provisions may be included in RTAs. These provisions would, however, only be obligatory for the signing members and not for third parties outside RTAs. Second, in relation to the regulatory incentives, trade-labor linkage inclusion in RTAs as well as inclusion of CSR rules would allow for labor standard protection and enforcement. Governments and MNCs would take equal responsibility on clean productions processes and protection of workers' rights for the trade in goods and services taking place within the RTA. The inclusion of these provisions should also create institutions that can serve to channel the participation and voice from the different stakeholders. A social dialogue and a tripartite system similar to that of the ILO are proposed within the RTA. These institutions would

[256] Amsden, "Promoting Industry under WTO Law," 217.

enable stakeholders, such as government, MNCs, and most importantly labor representatives to take active participation and make their voices heard. The following subsections will detail the proposed measures to achieve and EPZ - IEL compliance.

7.1.1. Aligning EPZ schemes with WTO-ASCM provisions.

In a post-SDT era that is to initiate in January 2016, EPZs will continue to prevail among the developing countries. The need to align with WTO Law to achieve compliance as well as the flexibility that is required from the MTS so that those member countries can align with the WTO Law should be prioritized.

Aligning with WTO Law may prove most beneficial in the long run for development rather than requesting never-ending SDTs. Today, WTO provisions promote science and technology. Provisions enable countries to promote Research and Development and high-technology industries. A lesson learnt from industrializers since the beginning of the GATT is that whenever industrial policies were implemented, these were always destined for general industrial expansion. This means that results would go well beyond the simple manufacturing activity. Amsden emphasizes such goals by stating that "getting right control mechanisms, in conjunction with promoting science and technology, are twin pillars of a new industrial development strategy."[257] Costa Rica and Panama have made use of this available space offered by the WTO while they still grant incentives to EPZs. EPZs can at this point comply with the MTAs, upgrade and diversify their manufacturing activities and lead to development.

On the contrary, requesting never-ending SDT extension implies that countries would never escape the "developing" status that makes them eligible for such "special treatment". The SDT may help countries at some specific stages in countries' path for development, but

[257] Amsden, "Promoting Industry under WTO Law," 230.

should never be considered as final goals. The final goal for countries should always be to graduate from the "developing stage" and reach sustainable development.

7.1.2. Legalizing EPZs through EPZ exemption clauses in RTAs and Canalizing through Multilateral RTA Exchange Committees.

The provisions provided by RTAs represent the *bona fide* negotiations and agreement by the members of that RTA, therefore RTAs can also further contribute in "legalizing" EPZs. This legalization can be possible in the specific components that would make them non-compliant by violating certain prohibitions of performance requirements under BITs or under an investment chapter of any RTA. Host governments could seek compliance by incorporating possible EPZ exception clauses to the general prohibitions.

Examples can be found in Japan's BITs and EPAs, such as in the Japan-Mexico EPA of 2005.[258] Article 65(2) and (3) of the Japan-Mexico EPA allows a host country to set several types of performance requirements to foreign investors, when they are contingent on provision of favorable treatment to them by the host country. These kinds of provisions can "legalize" EPZs and make them compliant with IEL. However, such provisions would only be applicable within RTA members and would need to exclude export requirement as they violate the ASCM. The inclusion of these specific EPZ provisions in RTAs represents a good practice in balancing trade and investment liberalization, and securing policy space for development.

[258] Japan-Mexico Economic Partnership Agreement, full text available at: http://www.mofa.go.jp.

To effectively canalize RTA provisions to the MTS, an RTA Exchange Committee within the WTO is necessary. The E15 Initiative[259] related to strengthening the global trading system through RTAs states the following:

> "The WTO is uniquely placed to act as a dedicated clearing house and forum where all matters related to RTAs, their rules, and their practices can be discussed among all WTO Members. This type of an "RTA Exchange" could feature an annual forum where the Members regularly share practices and challenges from building RTAs, as well as an informative and interactive website on RTAs, their rules, the various research findings on them, the practical experiences in negotiating and implementing them, and the various ways in which regional governments have sought to complement them through further regional cooperation."[260]

With this kind of exchange at the multilateral level, member countries would be able to take lessons from RTAs worldwide and systemize some of the provisions contained in the discussed RTAs. Provisions as for the EPZ schemes, fiscal and regulatory incentives granted to the investors might reach multilateral levels through this RTA Exchange Committee. And while the RTAs nature would prevail in making the provisions obligatory only for the signing members, RTA transparency would be promoted; advice and opinions may also be raised among the different levels of the IEL.

7.1.3. Trade-Labor Linkage and a Forum for a Tripartite Social Dialogue System

Inclusion in RTAs

RTAs can be stepping stones to achieve EPZ compliance with the IEL. RTAs should be used to aid the multilateral trade liberalization and be synergistic with MTS rules in trade and non-trade related areas, such as in labor standard enforcement, to ensure development of

[259] The E15 Initiative "convenes world-class experts and institutions to generate strategic analysis and recommendations from government, business, and civil society geared towards strengthening the global trade and investment system for sustainable development," official homepage available at: http://e15initiative.org/about-e15/

[260] Estevadeordal, Suominen, and Volpe, "Regional Trade Agreements," 14.

countries.[261] At the same time, labor issues should always be a priority in the context of globalization. Economic as social issues should both be part of countries' international trade policies to achieve sustainable development.

As reviewed in Chapter six, the trade-labor linkage inclusion has been possible in RTAs rather than in MTAs. This inclusion allows member countries to file complaints in the cases in which they consider labor violations might be taking place within the RTA. The trade-labor linkage inclusion in RTAs reveals that countries are trying to level the playing field in trade matters. This means promoting and enhancing trade while resisting any attempts to downgrade labor standards.

The present study promotes the trade-labor linkage inclusion in RTAs. The internationally enforceable labor provisions can exert pressure to member countries granting regulatory incentives in EPZs to comply with the CLS and basic human rights provided by the ILO. Besides the inclusion of these internationally enforceable labor provisions, the creation and promotion of institutions that will strengthen joint efforts between governments, MNCs, and labor representatives is proposed. These institutions should be based on a form similar to the social dialogue and the tripartite system used by the ILO.

According to the ILO, social dialogue can be defined as "any kind of negotiations, consultations, or exchange of information between representatives of governments, employers and workers on issues of economic and social policy."[262] Non-governmental organizations (hereinafter NGOs) may also take participation in these dialogues. Social dialogue may take place in a tripartite process or in bipartite relations. The main objective is to promote transparent discussion between stakeholders, such as the state, employers, and labor union representatives to promote industrial development, peace, economic and social justice.

[261] Ibid., 5.

[262] ILO, *Trade Union Manual*, 57.

An effective tripartite social dialogue system in RTAs will only be possible if workers in EPZs are well represented. For this to take place, governments should comply with the RTA labor provisions that refer to the ILO conventions, specifically Conventions 87 and 98 respectively, which promote freedom of association and collective bargaining. The awareness of workers of their rights to engage in labor unions will allow for transparent social dialogue in a regional level forum and therefore improve their working and living conditions.

Social dialogue is quite necessary for EPZs to comply with the IEL. Currently, and as could be perceived from the U.S.-Guatemala case, the CLS of freedom of association and collective bargaining is often violated. As such violations still take place, the study proposes for a strong promotion of social dialogue through the labor chapters in RTAs. The regional level might prove more effective than the multilateral level as particular cases and concerns taking place inside EPZs could easily be discussed and solved in more immediate terms. This is because trade interests of the signing parties could lead them to efficient and expedient labor solutions in regional forums as compared to the costly and lengthy in time multilateral forums.

Framework agreements also inspire the inclusion of a tripartite social dialogue forum in RTAs. International Framework Agreements (hereinafter IFAs) are instruments negotiated between MNCs and Global Union Federations (hereinafter GUF). IFAs are based on the commitment of companies to certain principles, however unlike CSR provisions, they are product of negotiations of companies with international labor representatives. IFAs represent sophisticated instruments as their existence assumes the existence of international labor unions. Countries hosting EPZs still face challenges to promote and protect national labor unions as violations to freedom of association and collective bargaining take place inside the plants. RTA forums, as international instruments *per se*, could stimulate the creation of

international labor unions among RTA member countries. The international labor unions could then create an IFA with MNCs establishing EPZs. IFAs all include the four fundamental principles and rights at work and specifically reference ILO Core Conventions. In this way EPZs could easily comply with CLS.

The legal framework or blueprint adapted to RTAs without sacrificing any economic objectives the RTA might have and also without any major amendments to the MTS will enable effective protection of labor standards in a scenario in which the three stakeholders can actively and equally participate. The EU-Korea FTA deserves recognition. In this RTA, there was an introduction of civil society groups, including labor groups and environment representatives. This represents an advance in RTAs as it points out that objectives inside an RTA should go beyond economic goals, but that they must cover issues destined at protecting CLS of workers as well as to protecting the environment. It can be interpreted as succeeding in a cooperative mechanism structure at the IEL regional level.

The NAFTA NAALC, another example of international law enforcement at the regional level also encourages non-governmental parties to take part in dispute settlement procedures before the formal establishment of any arbitral panel. NAALC procedures allow ministries and labor representatives to meet and have discussions to achieve agreements on the disputed claim. It also incites the use of seminars and training programs for workers. These non-governmental parties may also have participation in procedures' hearings and in filing complaints at any time. Therefore the NAALC has also promoted a collaborative practice among parties of interest in any case concerning labor standard protection or labor standard violations.

This proposed participative mechanism at the international regional level resembles the tripartite system of the ILO and would prove more effective as within an RTA the

interests of the parties and the results are more immediate and direct compared to the multilateral level.

7.1.4. Soft Law Provisions in Hard Law RTAs

While governments enter into trade agreements, either because of political and/or economic reasons, it is the private sector, such as MNCs, that are expected to translate the agreements into trade benefits, therefore the role of private parties engaged in trade and complying to the IEL is extremely important. CSR can be supporting tools to ensure EPZ compliance with the IEL. A very recent approach and one that is also proposed in the present study, is the inclusion of CSR provisions in RTA models.[263] Today social clauses and the promotion of CSR are being mentioned in recent RTA models. A first example of such a legal framework is found in Article 810 of Chapter 8, Investment Chapter, of the Canada-Peru FTA of 2009.

Article 810 contemplates CSR by encouraging the member countries to incorporate CSR in their internal policies. From such example it can be seen that hard law is recognizing some forms of the international soft law as supportive legal tools. Article 810 states the following:

> "Article 810: Corporate Social Responsibility. Each Party should encourage enterprises operating within its territory or subject to its jurisdiction to voluntarily incorporate internationally recognized standards of corporate social responsibility in their internal policies, such as statements of principle that have been endorsed or are supported by the Parties. These principles address issues such as labor, the environment, human rights, community relations and anti-corruption. The Parties therefore remind those enterprises of the importance of incorporating such corporate social responsibility standards in their internal policies." [264]

[263] Corporate Social Responsibility and Regional Trade and Investment Agreements, United Nations Environment Programme (2011), available at: http://www.unep.ch/etb/publications/CSR%20publication/UNEP_Corporate%20Social%20Responsibility.pdf.

[264] Canada-Peru FTA, full text available at: http://www.international.gc.ca/trade-agreements-accords-commerciaux/agr-acc/peru-perou/chapter-chapitre-8.aspx?lang=eng.

A second example can be found in Article 816 of Chapter 8, Investment Chapter, of the Canada- Colombia FTA of 2011. Article 816 states the following:

> "Article 816: Each Party should encourage enterprises operating within its territory or subject to its jurisdiction to voluntarily incorporate internationally recognized standards of corporate social responsibility in their internal policies, such as statements of principle that have been endorsed or are supported by the Parties. These principles address issues such as labor, the environment, human rights, community relations and anti-corruption. The Parties therefore remind those enterprises of the importance of incorporating such corporate social responsibility standards in their internal policies." [265]

Hufbauer and Schott also acknowledge the possible connectivity that is possible between CSR and RTAs. While revisiting the NAFTA-NAALC and stating recommendations for improving labor standards, the authors imply that businesses with operations in two or three NAFTA countries "should adopt common labor codes of conduct. These codes should reflect the OECD guidelines and the ILO declaration. Companies would certify their compliance. Such self-certification program should be gradually extended to smaller companies that do business in two or more NAFTA countries. Oversight from both private-sector interest groups and the CLS would back up these self-regulatory efforts."[266]

Motives for including specific CSR provisions in RTAs will only be borne from the trade interests and concerns that countries have in each other at the moment of negotiating the RTA. The Canada-Peru and Canada-Colombia FTA examples reveal that parties decided to include such CSR provisions to enhance enterprise awareness on labor, environment, human rights, among other issues' protection. The inclusion of soft law in hard law does not necessarily mean that the pure nature of soft law would then transform to hard law, making the provision legally binding. It is too soon to conclude on such happening, or even to

[265] Canada-Colombia FTA, full text available at: http://www.international.gc.ca/trade-agreements-accords-commerciaux/agr-acc/colombia-colombie/chapter8-chapitre8.aspx?lang=eng.

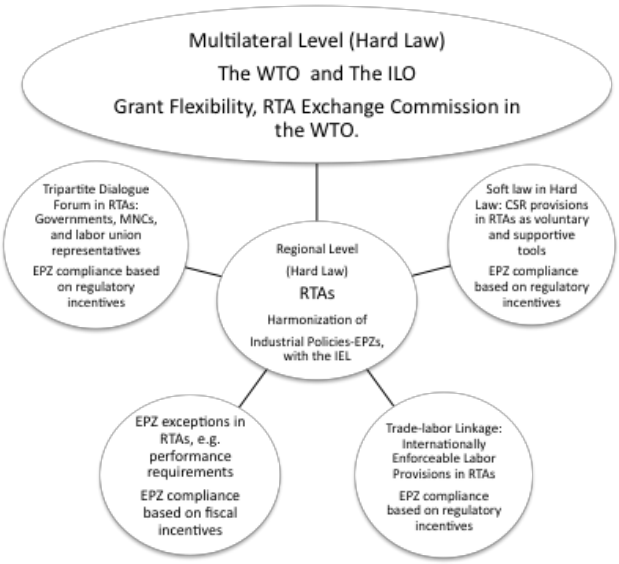
[266] Hufbauer and Schott, *NAFTA Revisited,* 135.

consider it would ever occur. What is true and can be easily understood as for now, is that soft law, e.g. private CSR provisions, are serving as supportive legal tools inside hard law instruments, i.e. RTAs, to help them achieve compliance of provisions that are provided by the multilateral organizations. Effectively, hard law instruments, i.e. RTAs, are referring to soft law provisions as supportive tools without necessarily changing the nature of soft law *per se*. These provisions encourage states to voluntarily incorporate private practice, ethical rules of corporate social responsibility in their internal policies. The provisions stimulate a voluntary commitment of public parties, i.e. states, in acknowledging CSR provisions that correspond to private parties, e.g. MNCs, to adopt and implement them. A public-private partnership for a voluntary clean practice is sought through CSR provisions.

7.2. The Synergistic Effects of RTAs with MTAs.

The harmonization of EPZs as industrial policies with trade liberalization rules provided in the MTAs and in the RTAs that limit the policy space of developing countries is possible with an appropriate framework and a righteous implementation of the available tools countries count on at present. The preceding subsections of the present chapter have analyzed the parts of the designed framework in detail. The ultimate goal is to allow EPZs to exist while they can still comply with the MTS in a post-SDT era. The synergistic effect is achieved when both the MTS and RTAs connect smoothly and pursue same goals. Figure 3 synthesizes the preceding subsections of the present chapter and illustrates the framework's synergistic approach.

Figure 3. The Synergistic Effects of RTAs with MTAs in Harmonizing Industrial Policies with the IEL



Source: Original by author.

The MTS have now become more complex with many issues being covered and also with 161 member countries participating in negotiations.[267] To make it more effective this international framework offered in the present study entails reliance on a combination of hard and soft laws. Hard law represents the MTAs and the RTAs. Soft law represents the ILO's moral suasion to enforce CLS, which are considered human rights, and the CSR rules and CoC of MNCs. A framework that combines both approaches is recommended. The MTS alone cannot do it, and the RTAs alone cannot do it either. Hard law can receive support from soft law, and soft law does not necessarily need to change its own soft law, voluntary nature. The measures proposed in Figure 3 illustrate that while making use of the available IEL tools

[267] As of November 17, 2015.

and current available policy space of developing countries, EPZ compliance with the IEL in its different levels is possible.

7.3. A New Global Trend and Future Implications

Today, countries negotiating and signing RTAs, are still opting for the trade-labor linkage inclusion in RTAs. The most recent inclusion of a labor chapter, and the one that will have the farthest reach and impact on the largest number of countries ever, is the inclusion of internationally enforceable labor provisions in the TPP. The TPP is the largest RTA ratified in history covering several issues that go well beyond the MTS and the RTA covering the largest area ever. Though still not fully enforced, the 12 negotiating countries[268] have reached agreement on October 5, 2015.

In relation to the labor issues the TPP Labour Chapter is considered to be the most ambitious in relation to internationally enforceable labor provisions. Country members want to ensure that international trade policies and trade liberalization should consider social and economic issues in a cooperative manner. Canada states that competitive economies in world trade should include safe, healthy, and cooperative workplaces as it seeks its pursuance of labor protection in the TPP.

The TPP provides opportunities to raise and improve labor standards in member countries through and ambitious level of obligations to ensure that domestic labor laws and policies in partner countries respect international labor standards. The Labour Chapter in the TPP first of all provides internationally enforceable commitments to protect and promote internationally recognized labor principles and rights, including the ILO 1998 Declaration on Fundamental Principles and Rights at Work. It includes commitments to ensure that national

[268] The twelve negotiating countries of the TPP are: Australia, Canada, Japan, Malaysia, Mexico, Peru, United States, Vietnam, Chile, Brunei, Singapore, and New Zealand.

laws and policies provide protection of the fundamental principles and rights at work, including: the right to freedom of association and collective bargaining; and the elimination of child labor, forced labor or compulsory labor, and of discrimination in respect of employment and occupation. It ensures that laws provide acceptable conditions of work with respect to minimum wages, hours of work, and occupational health and safety.

The chapter also encourages cooperation on labor matters and encourages companies to adopt voluntary CSR initiatives related to labor issues. Article 19.7 states the following: "Each Party shall endeavor to encourage enterprises to voluntarily adopt corporate social responsibility initiatives on labor issues that have been endorsed or are supported by that Party."[269]

The TPP prevents parties from derogating from their domestic labor laws in order to encourage trade or investment. It also includes structures to implement and monitor compliance with the commitments in the chapter: a Party may request consultations with another Party on any matter arising under the Chapter in order to jointly decide any course of action to address the matter; establishes a mechanism through which member of the public can raise concerns about labor issues related to the Chapter. Finally, the TPP includes enforceable dispute settlement procedures in case of non-compliance to help ensure that all labor obligations are respected.

Assessments done on the Labour Chapter of the TPP, lead scholars and practitioners to assume that countries are still utilizing RTAs as catalysts to comply and to cover some issues that have been left out on the multilateral negotiations. In this particular case, the TPP shows evolution of internationally enforceable labor provisions. Lessons were drawn from the NAFTA-NAALC, the DR-CAFTA, and from other RTAs. The current text of the labor

[269] Article 19. 7 available at: http://www.international.gc.ca/trade-agreements-accords-commerciaux/agr-acc/tpp-ptp/text-texte/19.aspx?lang=eng

provisions of the TPP shows such evolution and the trend in trade policy that is expected to continue at least for the near to medium-term future.

Conclusions

Today we live in a globalized world. Globalization brings many advantages to countries worldwide. With globalization countries can trade with one another and investment may cross borders. Local producers of countries around the world can have access to the most advanced technology from other countries. EPZs bring all these advantages to countries implementing them as industrial policies. It has been said that no country has prospered historically – not even the largest countries – in the absence of engagement in international trade.[270] The present study has provided with a comprehensive analysis on how provisions in the multilateral and regional levels of the IEL have eroded the policy space of sovereign developing countries to implement certain industrial policies. Industrial policies are protectionist in nature and grant specific benefits to specific sectors or industries, contravening in this way, the MFN and reciprocity principles prevalent in the IEL. The analysis on policy space erosion by the multilevel IEL has been possible in light of the fiscal and regulatory incentives granted in Central American EPZ schemes.

EPZs are significant industrial policies for many countries in the world. The study has provided insights on how the EPZ fiscal and regulatory incentives may fall into prohibitions provided by the IEL provisions, either in its hard law instruments or in the soft law instruments, specifically from the Central American perspective, as the countries in the region use EPZs as significant industrial policies for economic growth and development. It is natural that when these countries became signing members of MTAs and RTAs, their policy space eroded and the implementation of industrial policies became constrained. However, if governments in the region utilize their remaining, or their own *proper* policy space, EPZs can

[270] Janow, Donaldson, and Yanovich, *The WTO*, 205.

righteously comply with the IEL. The study identified specific reconciling points in which MTAs, RTAs, and international soft law, can harmonize with EPZ policy contained in Central American EPZ legal frameworks.

An evident conclusion is that even in a WTO-ASCM post-SDT era, which starts from January 1, 2016, EPZs will continue to exist in Central America. In a post-SDT era, a new EPZ framework should concretely eliminate prohibited export subsidies and exemptions from direct taxes. The elements that now make prohibited export subsidies according to the WTO-ASCM can be amended through EPZ legal reforms by making those elements compliant with the WTO, while they could still fulfill the objectives of the zone. For the Central American countries, shifting the export requirement in EPZs, and allowing merchandise to remain in the domestic market represents a viable means of compliance. In this case, subsidies given to the firms would cease to be contingent upon export performance and it would enhance the forward linkages of EPZs to the domestic economies in the region.

In the cases in which elements of export contingency are to remain, the elements should be compliant with WTO Law. Concrete measures would include the elimination of exemptions on direct taxes and import duties on goods that are not consumed in the production process. WTO-compatible duty-drawback schemes could also be adopted for the importation of other inputs that would remain *de facto* duty-free. Additionally, EPZs should also promote the service sector as the ASCM covers only trade in goods.

In Central America, alignment with the WTO Law will allow for EPZ manufacturing activities to upgrade and diversify in production as could clearly be exemplified with the EPZ legal reforms in Costa Rica and in Panama. These reforms are moving on from traditional textile assembly manufacturing and rather pursuing higher technology manufacturing, research and development, contributing in this way to sustainable development. At the same

time, while developing countries worldwide, including Central American countries, do their utmost effort to align with the WTO Law, it is also expected from the MTS that the necessary and specific flexibilities are granted in transition periods and in the context of each member country while they align their EPZ schemes with the WTO Law. EPZs should be promoted as development tools so that countries can achieve, in the future, larger trade and investment reform efforts in their paths towards development.

In relation to the regulatory incentives, the trade-labor linkage and CSR inclusion in RTAs can lead to a compliance of EPZs with labor laws and international labor standards. RTAs should represent stepping-stones in the multilevel harmonization of industrial policies and trade liberalization. In Central America, achieving this compliance would also lead to EPZ upgrading in social aspects such as improving working conditions and workers' lifestyles. EPZ host governments and policymakers are key actors to achieve EPZ compliance with the multilevel IEL. At the same time, a public- private partnership from the legal and social perspective, where all the stakeholders participate and engage in social dialogue is necessary for sound compliance to be achieved, i.e. governments, private enterprises, and labor representatives engaging in a tripartite system at the regional level.

Considering all the existing legal instruments a multilevel coordination of legal instruments is possible. The regional level instruments can comply with the multilateral legal instruments, and vice versa. The law of global space often involves the coordination of multiple levels of governance from global to national and from national to global. In parallel, the proliferation of RTAs continues at a feverish pace. The regional level is a promising tool in reaching a consensus on trade-labor linkage issues as compared to the multilateral level. RTAs consider the level of development and the current context of a country. A key is to

create synergies based on the lessons learned at the regional level with the policy space erosion that the multilateral level creates.

RTAs can be complementary and useful tools, especially in today's revival of industrial policy. RTAs operate in full openness and comply with the multilateral rules. Notwithstanding the important contributions that have been made by RTAs, they can never be a substitute for the MTS. Addo acknowledges the necessity to intertwine rules as follows:

> "The interconnectivity of the global economy demands building a much stronger international economic and social order based on a better international legal framework which reflects the changing landscape of political and economic relations. This new international order must be based on the already established system."[271]

Additional to the different levels of the IEL structure, the international legal framework should entail reliance on a combination of hard and soft laws. This precise legal framework is what has been offered throughout the study. The framework that this study has designed in which industrial policy harmonizes with a multilevel IEL composed of hard and soft law provisions, achieves successfully sound compliance of EPZs as industrial policies with the multilevel IEL provisions. Moreover, this international legal framework of compliance can also serve as a model for other industrial policies that other developing countries would like to implement or which they nowadays implement and which are currently in a non-compliant state with the IEL provisions. The synergistic RTA-MTA model is a promising tool for industrial policy implementation in an era in which countries can make use of their own proper policy space.

[271] Addo, *The Global Debate*, 317.

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Annex I.

Final extensions to the exemptions of the use of prohibited subsidies as provided by the WTO – ASCM

WORLD TRADE ORGANIZATION

WT/L/691
31 July 2007
(07-3259)

ARTICLE 27.4 OF THE AGREEMENT ON SUBSIDIES AND COUNTERVAILING MEASURES

Decision of 27 July 2007

The General Council,

Having regard to Articles IV:1 and 2 and IX:1 of the Marrakesh Agreement Establishing the World Trade Organization ("WTO Agreement") and Article 27.4 of the *Agreement on Subsidies and Countervailing Measures* ("*SCM Agreement*");

Recalling that the Members of the Committee on Subsidies and Countervailing Measures ("SCM Committee" or "Committee"), as directed by the Ministerial Conference[1] have granted, pursuant to the procedures set forth in document G/SCM/39, extensions pursuant to Article 27.4 of the *SCM Agreement* of the transition period under Article 27.2(b) of the *SCM Agreement* for the elimination of export subsidies, in respect of certain programmes of certain developing country Members;

Noting the proposals submitted by those developing country Members to extend the procedures contained in G/SCM/39;[2]

Noting the terms of paragraph 5 of this Decision;

Recognizing the economic, financial and development needs, as well as the capacity and administrative constraints, of those Members in implementing their commitments pursuant to the *SCM Agreement* in respect of the elimination of export subsidies;

On the basis of the commitment of those Members to eliminate the export subsidies in question not later than 31 December 2015, with no requests for extension beyond those foreseen pursuant to this Decision;

Decides to adopt the following procedures.

[1] Ministerial Decision on Implementation-Related Issues and Concerns, (WT/MIN(01)/17), paragraph 10.6.
[2] See documents G/SCM/W/535 and G/SCM/W/537 and addenda.

※Emphasis added

PROCEDURES FOR CONTINUATION OF EXTENSIONS PURSUANT TO ARTICLE 27.4OF THE SCM AGREEMENT OF THE TRANSITION PERIOD UNDER ARTICLE 27.2(b) OF THE SCM AGREEMENT FOR CERTAIN DEVELOPING COUNTRY MEMBERS

The SCM Committee shall follow the procedures set forth below in respect of the continuation of extensions pursuant to Article 27.4 of the *SCM Agreement* ("SCM Article 27.4") of the transition period under Article 27.2(b) of the *SCM Agreement* for certain programmes, identified in the Annex.[3]

1. Mechanism for continuation of extension

(a) A Member that wishes to seek a continuation, for calendar year 2008, of the extension under SCM Article 27.4 for a programme listed in the Annex, shall submit a request to that effect to the SCM Committee not later than 3 September 2007. The request also shall include a reference to the WTO document containing the corresponding updating notification covering calendar year 2006, which the Member shall have submitted to the SCM Committee pursuant to 1(d) of G/SCM/39.[4]

(b) Not later than 26 October 2007, Members of the SCM Committee shall agree to continue the extensions, for calendar year 2008, for programmes listed in the Annex in respect of which requests have been submitted pursuant to 1(a) and for which the Committee has verified, in its annual review conducted pursuant to G/SCM/39[5], that the transparency and standstill requirements under G/SCM/39 were fulfilled during 2006.

(c) As provided for in SCM Article 27.4, the continuation of extensions by the SCM Committee pursuant to these procedures shall be subject to annual reviews in the form of consultations between the Committee and the Members receiving continuations of extensions. These annual reviews shall be conducted on the basis of annual updating notifications from the Members in question, as referred to in 2(a). The purpose of the annual reviews shall be to verify that the transparency and standstill requirements set forth in 2 and 3 are being fulfilled.

(d) During the period 2008-2012, Members of the SCM Committee shall agree to continue the extensions pursuant to these procedures, subject to verification through annual reviews as provided for in 1(c) that the transparency and standstill requirements set forth in 2 and 3 are being fulfilled.[6] The "last authorized period" referred to in the last sentence of SCM Article 27.4 shall not extend beyond 31 December 2013, and the final two-year phase-out period provided for in the last sentence of SCM Article 27.4 shall end not later than 31 December 2015.

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[3] The programmes eligible for continuations of extensions under these procedures are programmes providing export subsidies in the form of full or partial exemptions from import duties and internal taxes for which the SCM Committee continued extensions of the transition period under SCM Article 27.4 for calendar year 2007 pursuant to the procedures in G/SCM/39.

[4] At the regular meeting of the Committee in April 2007, these Members were reminded to submit their updating notifications by 30 June 2007.

[5] The procedures in G/SCM/39 shall cease to be effective upon completion of this 2007 annual review.

[6] This extension mechanism shall cease to be effective upon completion in 2012 of the annual review by the Committee to continue the extensions for calendar year 2013, such that there will be no basis for requests for extension beyond those foreseen in this Decision.

(e) A Member receiving a continuation of an extension under these procedures shall take, from 1 January 2008, the necessary internal steps with a view to eliminating export subsidies under the programme before the end of the final two-year phase-out period provided for in the last sentence of SCM Article 27.4. These steps shall include consultations with relevant government bodies and organisations and any necessary technical and/or legal assessments. In addition, from 1 January 2008 and in no case later than 31 December 2009, the Member shall notify each beneficiary under the programme indicating that no export subsidies within the meaning of SCM Article 3.1(a) will be granted or maintained beyond the end of calendar year 2015.

(f) A Member receiving a continuation of an extension under these procedures shall provide, for transparency purposes, an action plan for eliminating export subsidies under the programme, as an integral part of the annual updating notification submitted for the annual review to be conducted in 2010.[7] As part of this review, the SCM Committee shall undertake a mid-period assessment of each programme for which it has continued an extension under these procedures. During this mid-period assessment, the SCM Committee shall take stock of the steps undertaken as of that point by the notifying Member pursuant to 1(e), and shall discuss the action plan provided by the Member.

(g) A Member receiving a continuation of an extension under these procedures may request the WTO Secretariat to provide technical assistance for eliminating export subsidies under the programme.

2. Transparency

(a) The annual updating notifications shall follow the agreed format for subsidy notifications under SCM Article 25 (found in G/SCM/6/Rev.1). Beginning with the updating notifications covering calendar year 2008, notifying Members also shall provide information regarding the actions they have taken pursuant to 1(e) and 1(f).

(b) During the annual reviews by the SCM Committee referred to in 1(c), notifying Members can be requested by other Members to provide additional detail and clarification with a view to maintaining transparency in respect of the scope, coverage and intensity of benefits (the "favourability") of the programmes in question[8] and the form of the subsidies provided thereunder; and in respect of the actions taken pursuant to 1(e) and 1(f). Any information provided in response to such requests shall be considered part of the notified information.

(c) A Member receiving a continuation of an extension under these procedures shall ensure transparency in respect of the final two-year phase-out period provided for in the last sentence of SCM Article 27.4 by submitting updating notifications under paragraph 2(a), which shall be subject to annual review by the Committee.

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[7] The action plan shall indicate how the Member intends to eliminate export subsidies under the programme not later than the end of the final two-year phase-out period provided for in the last sentence of SCM Article 27.4, including information as to legislative changes, administrative amendments and/or other procedures as may be necessary, and whether any of these actions have been undertaken or are in the process of being undertaken, including how the individual beneficiaries have been notified pursuant to 1(e).

[8] The scope, coverage and intensity of benefits of the programmes in question will be determined on the basis of the legal instruments underlying the programmes.

Standstill

(a) Through the end of the final two-year phase-out period provided for in SCM Article 27.4, the programmes for which extensions are continued under these procedures shall not be modified so as to make them more favourable than they were as at 1 September 2001, as specified in the notified information previously submitted pursuant to the procedures in G/SCM/39. The continuation of an expiring programme without modification shall not be deemed to violate standstill.

(b) The verification of standstill in respect of the scope, coverage and intensity of benefits (the "favourability") of the programmes shall be based on the notified information referred to in 1(c), 2(a), 2(b) and 3(a).

3. Product graduation on the basis of export competitiveness

Notwithstanding these procedures, Articles 27.5 and 27.6 shall apply in respect of export subsidies for which extensions are continued pursuant to these procedures.

4. Members listed in Annex VII(b) which reserved rights pursuant to the procedures in G/SCM/39

(a) This Decision does not prejudge rights of Annex VII Members.

(b) If, during the period 2008-2015, the per capita GNP of a Member that reserved rights under paragraph 6(b) of G/SCM/39[9] reaches the level provided for in Annex VII(b) of the *SCM Agreement* such that the Member is no longer included in Annex VII(b), that Member shall be able to make use of these procedures as from the date at which its per capita GNP reaches that level and for the remainder of that period. The effective date for the standstill requirement referred to in 3(a) shall be the year in which that Member's GNP per capita reaches the level provided for in Annex VII(b) such that it is no longer included in Annex VII(b).

[9] The Members that reserved rights, and the programmes in respect of which these rights were reserved, are identified in documents G/SCM/N/74/BOL & Suppl.1, G/SCM/N/74/HND, G/SCM/N/74/KEN, and G/SCM/N/74/LKA.

ANNEX

LIST OF PROGRAMMES ELIGIBLE FOR CONTINUATION OF EXTENSIONS UNDER THE PROCEDURES[10], AND DOCUMENT REFERENCES FOR THE EXTENSION DECISIONS BY THE SCM COMMITTEE COVERING CALENDAR YEAR 2007

Antigua & Barbuda
- Fiscal Incentive Act Cap 172 (December 1975) (G/SCM/50/Add.4)
- Free Trade and Processing Zone Act No. 12 of 1994 (G/SCM/51/Add.4)

Barbados
- Fiscal Incentive Programme (G/SCM/52/Add.4)
- Export Allowance (G/SCM/53/Add.4)
- Research & Development Allowance (G/SCM/54/Add.4)
- International Business Incentives (G/SCM/55/Add.4)
- Societies With Restricted Liability (G/SCM/56/Add.4)

Belize
- Fiscal Incentives Act (G/SCM/57/Add.4)
- Export Processing Zone Act (G/SCM/58/Add. 4)
- Commercial Free Zone Act (G/SCM/59/Add.4)
- Conditional Duty Exemptions Facility under Treaty of Chaguaramas (G/SCM/60/Add.4)

Costa Rica
- Free Zone Regime (G/SCM/61/Add.4)
- Inward Processing Regime (G/SCM/62/Add.4)

Dominica

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[10] Programmes for which the SCM Committee continued extensions of the transition period under SCM Article 27.4 for calendar year 2007 pursuant to the procedures in G/SCM/39. It is recalled that the eligibility criteria in G/SCM/39 on the basis of which the original extension decisions pursuant to those procedures (for calendar year 2003) were taken for the listed programmes were as follows (footnotes omitted):

> "Programmes eligible for extension pursuant to these procedures, and for which Members shall therefore grant extensions for calendar year 2003 [...], are export subsidy programmes (i) in the form of full or partial exemptions from import duties and internal taxes, (ii) which were in existence not later than 1 September 2001, and (iii) which are provided by developing country Members (iv) whose share of world merchandise export trade was not greater than 0.10 per cent, (v) whose total Gross National Income ("GNI") for the year 2000 as published by the World Bank was at or below US$20 billion, (vi) and who are otherwise eligible to request an extension pursuant to Article 27.4, and (vii) in respect of which these procedures are followed."

It is further recalled that, in respect of the above eligibility criteria, G/SCM/39 also provided that:

> "The criteria set forth in these procedures are solely and strictly for the purpose of determining whether Members are eligible to invoke these procedures. Members of the Committee agree that these criteria have no precedential value or relevance, direct or indirect, for any other purpose."

- Fiscal Incentives Programme (G/SCM/63/Add.4)

Dominican Republic

- Law No. 8-90 to "Promote the Establishment of New Free Zones and Expand Existing Ones" (G/SCM/64/Add.4)

El Salvador

- Export Processing Zones and Marketing Act, as amended (G/SCM/65/Add.4)

Fiji

- Short-Term Export Profit Deduction (G/SCM/66/Add.4)
- Export Processing Factories/Export Processing Zones Scheme (G/SCM/67/Add.4)
- The Income Tax Act (Film Making and Audio Visual Incentive Amendment Decree 2000) (G/SCM/68/Add.4)

Grenada

- Fiscal Incentives Act No. 41 of 1974 (G/SCM/69/Add.4)
- Statutory Rules and Orders No. 37 of 1999 (G/SCM/70/Add.4)
- Qualified Enterprises Act No. 18 of 1978 (G/SCM/71/Add.4)

Guatemala

- Exemption from Company Tax, Customs Duties and Other Import Taxes for Companies under Special Customs Regimes (G/SCM/72/Add.4)
- Exemption from Company Tax, Customs Duties and Other Import Taxes for the Production Process Relating to Activities of Managers and Users of Free Zones (G/SCM/73/Add.4)
- Exemption from Company Tax, Customs Duties and Other Import Taxes for the Production Process of Commercial and Industrial Enterprises Operating in the Industrial and Free Trade Zone (G/SCM/74/Add.4)

Jamaica

- Export Industry Encouragement Act (G/SCM/75/Add.4)
- Jamaica Export Free Zone Act (G/SCM/76/Add.4)
- Foreign Sales Corporation Act (G/SCM/77/Add.4)
- Industrial Incentives (Factory Construction) Act (G/SCM/78/Add.4)

Jordan

- Partial or Total Exemption from Income Tax of Profits Generated from Exports under Law No. 57 of 1985, as amended (G/SCM/79/Add.4)

Mauritius

- Export Enterprise Scheme (G/SCM/80/Add.4)
- Pioneer Status Enterprise Scheme (G/SCM/81/Add.4)
- Export Promotion (G/SCM/82/Add.4)
- Freeport Scheme (G/SCM/83/Add.4)

Panama

- Official Industry Register (G/SCM/84/Add.4
- Export Processing Zones (G/SCM/85/Add.4)

Papua New Guinea

- Section 45 of the Income Tax (G/SCM/86/Add.4)

St. Kitts and Nevis

- Fiscal Incentives Act No. 17 of 1974 (G/SCM/90/Add.4)

St. Lucia

- Fiscal Incentives Act No. 15 of 1974 (G/SCM/87/Add.4)
- Free Zone Act, No. 10 of 1999 (G/SCM/88/Add.4)
- Micro and Small Scale Business Enterprises Act, No. 19 of 1998 (G/SCM/89/Add.4)

St. Vincent & Grenadines

- Fiscal Incentives Act No. 5 of 1982, as amended (G/SCM/91/Add.4)

Uruguay

- Automotive Industry Export Promotion Regime (G/SCM/92/Add.4)

Annex II. The Guatemala Enforcement Plan, DR-CAFTA U.S.-Guatemala Labor Case

Mutually Agreed Enforcement Action Plan between the Government of the United States and the Government of Guatemala ("Enforcement Plan")

As a Party to the Dominican Republic-Central America-United States Free Trade Agreement (CAFTA-DR), Guatemala reiterates its ongoing commitment, consistent with the terms of the CAFTA-DR, to effectively enforce Guatemala's labor laws. In furtherance of this commitment, and in order to resolve the dispute, *Guatemala – Issues Relating to the Obligations Under Article 16.2.1(a) of the CAFTA-DR* (hereafter, CAFTA-DR Labor Dispute), Guatemala and the United States agree as follows:

A. Ministry of Labor Investigation of Alleged Labor Law Violations in Guatemala

1. Inter-Agency Information Exchange Agreement

1.1. The Ministry of Labor (MOL) shall have access to the most up-to-date information maintained by Guatemala related to ownership of enterprises, addresses of enterprise worksites, and operational status.

1.2. **On June 20, 2012,** Guatemala signed an Inter-Agency Cooperation Framework Agreement for the Exchange of Information among the MOL, the Ministry of Economy (MOE), and the Superintendency of Tax Administration (SAT) (Inter-Agency Cooperation Agreement), establishing in relevant part that: (i) the MOE shall provide to the MOL up-to-date information related to all enterprises, including each enterprise's address, operational status, any transfer of ownership, and any information related to cancellation of its registration; and (ii) the SAT shall provide to the MOL non-confidential tax information related to all enterprises, including information on enterprise closure.

1.3. **Within 30 days,** Guatemala shall prepare an addendum to the Inter-Agency Cooperation Agreement that adds the Social Security Institute (IGSS) as a party to the Inter-Agency Cooperation Agreement, requiring that the MOE and the SAT also provide to the IGSS the information referenced in (i) and (ii), above, and providing that each party shall: (i) have access to any IGSS, MOL, MOE, or SAT databases containing the above-referenced information related to enterprises; (ii) immediately exchange any such information received after the Inter-Agency Cooperation Agreement enters into force; and (iii) immediately inform the other agencies upon receipt of notice of any enterprise closure or dissolution and of indicators of impending enterprise closure or dissolution, such as failure to pay required taxes, significant decreases in exports or the purchase of raw materials for production, and failure to make required social security payments.

1.4. **Within 60 days,** Guatemala shall publish the final Inter-Agency Cooperation Agreement with the addendum on the MOL, MOE, SAT, and IGSS websites, and shall provide copies to all MOL, MOE, SAT, and IGSS personnel whose responsibilities could be affected by the Inter-Agency Cooperation Agreement.

1.5. **Within 60 days,** Guatemala shall designate the personnel within the MOL, MOE, SAT, and IGSS responsible for implementing the Inter-Agency Cooperation Agreement with the addendum, in particular those personnel responsible for managing or exchanging the information in accordance with the Inter-Agency Cooperation Agreement.

2. Police Assistance for MOL Inspectors

2.1. MOL inspectors shall seek police assistance to ensure that a worksite visit is carried out pursuant to the May 26, 2011, Ministerial Accord No. 106-2011, Guide on Procedures in Case of Resistance to Inspectors' Duty to Inspect, and in such cases, police assistance shall be provided upon request of the inspectors, pursuant to the January 10, 2013, Inter-Agency Agreement Related to the Procedure in Case of Resistance to the Work of Labor Inspectors between the Ministry of Interior (MOI) and the MOL (MOI-MOL Agreement).

2.2. Ministerial Accord No. 106-2011 provides that: (i) an MOL inspector shall seek police assistance to visit a worksite when: (a) "immediate action" is required, (b) an inspector is not permitted access to a worksite, (c) the inspector's life or safety is in danger, or (d) when the circumstances otherwise

merit;[1] (ii) if an inspector is denied access to a worksite, the inspector shall immediately submit a complaint to the appropriate Labor and Social Welfare Court (Labor Court); and (iii) if police assistance is not provided upon request, the Inspector General of Labor shall inform the MOI within three days of the request, and the MOI shall initiate the corresponding legal procedures.

2.3. The MOI-MOL Agreement establishes that police officers shall provide assistance to labor inspectors, upon request, to ensure that the worksite visit is carried out when immediate action is required, when an inspector is not permitted access to a worksite, when the inspector's life or safety is in danger, or when the circumstances otherwise merit.

2.4. **Within 30 days,** Guatemala shall publish the MOI-MOL Agreement on the MOI and MOL websites and shall inform all MOI and MOL personnel whose responsibilities could be affected by the MOI-MOL Agreement.

2.5. **Within 30 days,** the MOI, through the National Civil Police, shall issue an order instructing all police officers and their commanding officers to provide assistance to labor inspectors, upon request, in accordance with Guatemalan labor laws, Ministerial Accord No. 106-2011, and the MOI-MOL Agreement.

3. Allocation of Resources for MOL Labor Law Enforcement

3.1. Guatemala allocated additional resources for the MOL's enforcement of labor laws, including the hiring and training of 100 additional permanent labor inspectors in the MOL's Inspection Department and five additional attorneys for the MOL's Legal Advisory Office of the Inspectorate General of Labor (IGT). Guatemala's allocation of additional resources includes increased resources to conduct labor inspections throughout the country. Resources and inspectors were distributed to the places with the highest incidence of labor rights violations, based on information reported by the IGT.

3.1(a). **On August 16, 2012,** the MOL completed the hiring of 100 additional permanent inspectors in the Inspection Department.

3.1(b). **In September 2012,** the MOL completed the hiring of five additional attorneys in the Legal Advisory Office of the IGT.

3.1(c). **On December 12, 2012,** the MOL launched the Department of Guatemala metropolitan division of the IGT and its Supervisory Unit.

3.1(d). **In August 2012,** the MOL assigned each of the 100 additional labor inspectors to the places with the highest incidence of labor rights violations in the country based on the information reported by the IGT and in response to the most immediate needs, including the regions in which the agriculture and *maquila* sectors operate.

3.1(e). **On November 17, 2012,** the MOL completed the training of the 100 additional labor inspectors and the five additional attorneys.

3.1(f). **During the first week of December 2012,** the MOL acquired 20 vehicles to strengthen the work of the MOL, with a particular focus on helping IGT personnel reach the most remote and difficult to access areas, thereby facilitating their inspection work.

3.2. Guatemala shall provide, on an ongoing basis, the resources necessary for the MOL's effective enforcement of Guatemalan labor laws.

3.3. Guatemala shall provide, in its annual budget, the necessary resources for the MOL to conduct labor inspections throughout the country, including the regions in which the agriculture and *maquila* sectors operate, to ensure that the inspections can be undertaken effectively. These resources shall

[1] The requirement in Article 4 of Ministerial Accord No. 106-2011 for labor inspectors to seek police assistance to visit a worksite "when the circumstances otherwise merit" shall be interpreted to require a labor inspector to seek police assistance whenever a labor inspector is not permitted access to a worksite.

include the cost of maintaining an appropriate number of vehicles.

4. MOL Authority to Issue Fine Recommendations and Expedited Judicial Review

4.1. **Within 60 days,** the MOL shall prepare a legislative proposal to amend the Labor Code to grant the MOL the authority to issue fine recommendations and establish an expedited process for the judiciary to adopt MOL fine recommendations, unless they are not reasonable, collect fines, and order remediation of labor law violations. The legislative proposal shall consist of the following elements:

4.1(a). If an employer fails to remedy an alleged labor law violation within the timeframe prescribed by the MOL, the MOL shall, within five days of the timeframe's expiration, file a complaint with the appropriate Labor Court. The MOL's complaint shall indicate the identified labor law violation, the MOL's fine recommendation, and a request for the Labor Court judge to order remediation of the violation where the complaint is found to be valid.

4.1(b). Within three days of receiving the MOL's complaint, the Labor Court judge shall accept it, provided it satisfies the established procedural requirements, and issue an order notifying the employer of the complaint and setting a date for an oral hearing to be held within 15 days of the Labor Court judge's acceptance of the complaint.

4.1(c). The employer may choose not to contest the MOL's complaint and agree to pay the fine to the Labor Court, or it may contest the violation identified by the MOL and/or the MOL fine recommendation at an oral hearing.

4.1(c)(i). If the employer chooses not to contest the MOL's complaint, the employer shall inform the Labor Court judge in writing within five days of receiving the Labor Court judge's order. Upon receipt of the written notice, the Labor Court judge shall adopt the MOL fine recommendation, unless it is not reasonable, and issue an order requiring the employer to pay the fine within five days of receiving the order and to remedy the violation within a specified time period. The order shall indicate that if payment is made within five days, the fine amount shall be reduced by 50 percent, provided that the reduced fine is not less than the minimum fine established in the law, and shall order remediation of the violation within a specified time period. In such cases, the oral hearing would not be held.

4.1(c)(ii). If the employer chooses to contest the MOL's complaint at the oral hearing, the Labor Court judge, respecting due process and having received evidence, shall issue an order at the hearing that: (i) adopts the MOL's fine recommendation, unless it is not reasonable, or (ii) absolves the employer. If the Labor Court judge imposes a fine, it shall issue an order requiring the employer to pay the fine within five days of receiving the order and to remedy the violation within a specified time period.

4.1(c)(iii). If the employer does not submit a written document in which he does not contest the MOL's complaint and fails to appear at the oral hearing on the date set by the Labor Court judge, the Labor Court judge shall adopt the MOL fine recommendation at that same hearing, unless it is not reasonable, and issue an order requiring the employer to pay the fine within five days of receiving the order and to remedy the violation within a specified time period.

4.1(d). A party may appeal the Labor Court judge's order at the hearing or within three days of receiving notice of the order. Within two days of receiving notice of the appeal, the Labor Court judge shall refer the case to the corresponding Labor Court of Appeals, which shall issue a decision within ten business days. If the Labor Court of Appeals confirms the Labor Court judge's order adopting a fine, the Labor Court judge shall order the employer to pay the fine within five days of the date of receiving the Labor Court of Appeals' order and to remedy the violation within a specified time period.

4.1(e). Any final order issued by a Labor Court judge directing an employer to remedy a violation within a specified time period shall be transmitted to the Unit for Execution and Verification of Reinstatements and Special Procedures related to Labor Matters within the judiciary (Verification

Unit),[2] immediately after the expiration of the specified time period, to verify that the violation has been remedied within the specified period. The Verification Unit shall seek the assistance of the police, if necessary, and of the IGT in cases where the IGT's knowledge or expertise may be required or as otherwise needed. If the violation is not remedied within the specified time period, the Labor Court judge shall refer the matter to the corresponding Criminal Court for failure to obey a court order and shall take any action that is necessary to ensure compliance with the order.

4.1(f). If the employer does not pay a fine within the time period specified by the Labor Court judge, the Labor Court judge shall immediately issue an order calling for the necessary embargos or seizures of assets to ensure payment of the imposed fine. If the employer does not have sufficient assets to ensure payment of the fine, the Labor Court judge shall order the employer to include the amount of the fine as a debt in its accounting projections for the following year. If the violating employer fails to comply with such order, the Labor Court judge shall refer the matter to the corresponding Criminal Court for failure to obey a court order.

4.1(g). The Labor Court judge shall notify and provide copies of all final court orders to the MOL, as a party to the case.

4.2. **Within 60 days,** the President shall submit this legislative proposal to the Congress of Guatemala.

4.3. The Congress, upon receiving the legislative proposal, shall put it on the agenda for the purpose of complying with the procedures established in the Constitution of the Republic.

4.4. The Executive Branch of Guatemala shall make every effort to enact this proposed legislation within 180 days. If, once that period expires, the proposed legislation has not been enacted, the United States may request the panel to resume its work, and the provision set out in Section 18.4 of this Enforcement Plan, regarding termination of the process, shall not apply.

5. Standardized Timeframes for MOL Inspections

5.1. Guatemala, through the MOL, shall adopt and implement standardized timeframes for: (i) conducting labor inspections after the MOL receives complaints; (ii) remediation of violations identified by labor inspectors; and (iii) conducting verification visits to verify that employers have remedied the violations identified by labor inspectors consistent with any applicable timeframes set by the Labor Code.

5.2. **Within 90 days,** Guatemala shall prepare an MOL Ministerial Accord that establishes standardized timeframes for the items listed above.

5.3. **Within 110 days,** Guatemala shall publish on the MOL website these standardized timeframes and shall inform all MOL personnel whose responsibilities could be affected by the Ministerial Accord.

6. Labor Law Compliance for Enterprises Receiving Benefits under Decree No. 29-89; Revocation of Benefits

6.1. Guatemala shall strengthen the enforcement of Article 33(f) of Decree No. 29-89 of the Congress of the Republic, Law to Promote and Develop Export and Maquila Activity (Decree 29-89), which requires that all enterprises classified as exporters or *maquilas* under the Temporary Admission and Reimbursement of Duties Regime shall "comply with the laws of the country, particularly labor laws." While respecting due process, the benefits of these enterprises under Decree 29-89 shall be revoked for labor law violations.

[2] The Verification Unit was created pursuant to Accord No. 26-2012 to verify employer compliance with all Labor Court judge orders.

6.2. **Within 90 days,** Guatemala shall publish on the websites of the MOL, the MOE, and the judiciary, a Government Accord repealing Government Accord No. 196-96 and shall inform all MOL, MOE, and judicial personnel whose responsibilities could be affected by the changes. The new Government Accord shall require that:

6.2(a). If an enterprise receiving benefits under Decree 29-89 does not comply with the order of the appropriate Labor Court within the time period specified by that court, the Labor Court shall give notice to the MOE within five days of that failure to comply and provide the MOE with a copy of the order; and

6.2(b). Within five business days of receiving such notice from the appropriate Labor Court, the MOE shall immediately revoke the benefits the enterprise receives under Decree 29-89.

6.3. **Within 90 days,** Guatemala shall publish on the MOL website a Ministerial Accord requiring the MOL to conduct ongoing inspections of enterprises receiving benefits under Decree 29-89 and shall inform all personnel whose responsibilities could be affected by the Ministerial Accord. The Ministerial Accord shall require the MOL to conduct, for each enterprise receiving Decree 29-89 benefits:

6.3(a). At least one annual inspection to confirm the enterprise is complying with all applicable labor laws; and

6.3(b). Verifications, every 120 days, through the use of data tracking or other means, that the enterprise is not in violation of any MOL, Labor Court, or Criminal Court orders against the enterprise or its predecessor(s), in cases where employer substitution has been confirmed.

6.4. **Within 90 days,** Guatemala shall undertake the first annual inspections and verifications for all enterprises receiving benefits under Decree 29-89.

6.5. **Within 120 days and every 180 days thereafter,** Guatemala shall publish on the MOE website a list of enterprises that received benefits under Decree 29-89 during the prior 180 day period, and indicate which of those enterprises had Decree 29-89 benefits revoked as a consequence of violating Article 33(f) of Decree 29-89.

7. **Labor Law Compliance for Enterprises Receiving Benefits under Decree 29-89: Qualification Procedures**

7.1. Guatemala shall strengthen compliance with labor laws by enterprises receiving benefits under Decree 29-89, based on Article 33(f) of Decree 29-89, through the following actions:

7.2. **Within 60 days,** the MOE shall prepare an amendment to Chapter II ("Qualification Procedures") of Government Accord 533-89, which regulates Decree 29-89, that shall:

7.2(a). Require the MOE to publish on its website and in at least one nationally circulated daily newspaper the names of all enterprises applying for benefits under Decree 29-89 and provide the public with a period of 30 days from the date the names are published to submit comments to the MOE with respect to the enterprise's compliance with Article 33(f) of Decree 29-89. The MOE shall not approve an application for benefits until the 30-day comment period has closed. If the MOE receives information indicating that the enterprise, or any potential predecessor(s) within the meaning of Article 23 of the Labor Code, may be in violation of one or more labor obligations, it shall promptly provide this information to the MOL;

7.2(b). Require the MOE, before approving an application for benefits under Decree 29-89, either by an existing enterprise or an enterprise with respect to which the MOE receives information indicating that a potential predecessor within the meaning of Article 23 of the Labor Code may be in violation of one or more labor obligations, to request the MOL to confirm, in coordination with the Verification Unit, that the enterprise is not presently violating any labor laws or MOL, Labor Court, or Criminal Court orders, including against its predecessor(s) in cases where the judiciary has determined that employer substitution has occurred pursuant to Article 23 of the Labor Code. The MOE shall reject the application if such violations are confirmed;

7.2(c). Require each enterprise seeking to qualify for benefits under Decree 29-89 to attach to its application a sworn statement by the enterprise's Guatemalan legal representative, notarized by a Guatemalan notary public, stating that, as of the date of the application, the enterprise is in compliance with all labor obligations, including labor laws and MOL, Labor Court judge, and Criminal Court judge orders against the enterprise or its predecessor(s). The enterprise's Guatemalan legal representative may be prosecuted criminally for the offense of perjury if the application contains any false statements; and

7.2(d). Require each enterprise approved for benefits under Decree 29-89 to submit, by January 20 of each year, a sworn statement by the enterprise's Guatemalan legal representative, notarized by a Guatemalan notary public, stating that the enterprise has complied with its labor obligations during the prior year and provide that failure to submit the statement shall result in the termination of the benefits within 30 days of the January 20 deadline. The enterprise's Guatemalan legal representative may be prosecuted criminally for the offense of perjury if the application contains any false statements.

7.3. **Within 60 days,** the MOE shall publish this amendment to Chapter II on its website and shall inform all of its personnel whose responsibilities could be affected by the amendment.

Mechanism to Ensure Worker Payments upon Closure of Enterprises Receiving Benefits under Decree 29-89

7.4. **Within 30 days,** Guatemala, in cooperation with the United States, shall make a request that shall be submitted to the Inter-American Development Bank (IDB) and any other cooperating international institution, for the development of a project to establish a contingency mechanism that is commensurate with the extent of the potential need, and commercially and legally viable, to address cases of closures of enterprises receiving benefits under Decree 29-89, designed to ensure payments owed to workers.

7.5. Guatemala shall present the information required by each international institution, in order for the request to be considered, within 60 days from the date it was submitted.

7.6. The Executive Branch of Guatemala shall make every effort to implement the mechanism that results, which must be commensurate with the extent of the potential need and commercially and legally viable.

8. Labor Law Compliance upon Enterprise Closure

8.1. Guatemala shall establish procedures to confirm enterprise closures or dissolutions, or imminent closures or dissolutions, and take the necessary measures to obtain the payment of remuneration owed to workers in the case of closure or dissolution, including wages, indemnification, bonuses, overtime pay, and any other payments required by law.

Procedures Applicable to All Enterprises

8.2. **Within 30 days,** Guatemala shall prepare an MOL Ministerial Accord, requiring that:

8.2(a). The IGT shall initiate a labor inspection of an enterprise immediately upon receiving information of its closure or dissolution or of indicators of its impending closure or dissolution, including information obtained: (i) through the Inter-Agency Cooperation Agreement signed on June 20, 2012; (ii) from a worker's complaint; or (iii) directly by the MOL. The labor inspection shall include:

8.2(a)(i). In the case of a closure or dissolution or impending closure or dissolution in Guatemala City and the Department of Guatemala, inspectors from the Special Unit of Conflicts;

8.2(a)(ii). Notice within a period of 24 hours to the National Civil Police pursuant to Ministerial Accord 106-2011;

8.2(a)(iii). In the case of impending closure or dissolution, an assessment of the likelihood of such closure or dissolution and risk of non-payment of remuneration owed upon closure or dissolution, including by seeking Labor Court authorization under Labor Code Article 281(b) to review enterprise accounting books and by taking into account repeated instances of non-payment of remuneration owed to workers; and

8.2(a)(iv). Notice to the workers of the inspection results, through their representative(s), by posting them on the MOL website, or through other appropriate means.

8.2(b). If the IGT concludes, as a result of the inspection, that an enterprise presents a risk of non-payment of remuneration owed to workers at the time of closure or dissolution and that such closure or dissolution is ongoing or impending, or if the IGT concludes that an enterprise has closed or dissolved without paying remuneration owed to workers, the IGT shall undertake the following actions:

8.2(b)(i). Petition the appropriate Labor Court to embargo or seize assets to ensure payment of the remuneration owed to workers;

8.2(b)(ii). Immediately notify the IGSS so that it can verify compliance with certain employer obligations;

8.2(b)(iii). Order the employer to immediately make payment of all remuneration owed to workers upon closure or dissolution; and

8.2(b)(iv). If the IGT determines that an employer has failed to make the required payments within the timeframe provided, the IGT shall, within five days of the timeframe's expiration, file a complaint with the appropriate Labor Court judge, initiating the sanction process provided for in Section Four of this Enforcement Plan.

8.2(b)(v). The actions described in paragraph 8.2(b) and its subparagraphs shall be taken with respect to enterprises receiving benefits under Decree 29-89 as specified in paragraph 8.6 and its subparagraphs.

8.2(c). After an inspection, and upon a determination that enterprise closure or dissolution is ongoing or impending, the IGT shall undertake a preliminary determination of remuneration owed to workers, such as wages, bonuses, benefits, indemnifications, and any other payments required by law, to the workers who request it in accordance with the Labor Code.

8.3. **Within 60 days,** Guatemala shall publish this Ministerial Accord on the MOL website and shall inform all personnel of the MOL, MOE, and judiciary whose responsibilities could be affected by the Ministerial Accord.

8.4. **Within 90 days,** Guatemala shall train all labor inspectors and all other MOL personnel affected by this Ministerial Accord, which shall include training by a qualified governmental or non-governmental entity on reviewing accounting books to determine whether existing assets are sufficient to cover the remuneration owed to workers upon enterprise closure or dissolution.

Additional Procedures for Enterprises Receiving Benefits under Decree 29-89

8.5. Guatemala, through a Rapid Response Team (GRI) composed of the MOL, which coordinates it, the MOE, MOI, SAT, IGSS, and the judiciary, shall verify the imminent closure or dissolution of enterprises receiving benefits under Decree 29-89 through procedures established for this purpose and shall take the necessary measures to seek employer compliance with labor law obligations and attempt to prevent possible enterprise closures or dissolutions.

8.6. **Within 90 days,** Guatemala shall prepare an MOL Ministerial Accord for the establishment of the GRI, requiring that:

8.6(a). The IGT shall initiate the labor inspection described in subparagraph 8.2(a) of an enterprise receiving benefits under Decree 29-89 within 24 hours of receiving information of its

closure or dissolution or of indicators of its impending closure or dissolution. If the IGT verifies, as a result of the inspection, that an enterprise receiving benefits under Decree 29-89 presents a risk of non-payment of remuneration owed to workers at the time of closure or dissolution and that such closure or dissolution is impending, the MOL shall convene a meeting of the GRI within 48 hours to analyze the case. If the IGT verifies that such closure or dissolution has occurred, the processes described in subparagraphs 8.2(b) and 8.2(c) shall apply. If the GRI is convened, the MOL shall summon the employer to appear before the GRI within 24 hours of the initial GRI meeting to present relevant documentation, including the accounting books of the enterprise, unless, due to geographical distance of the enterprise, the employer is unable to appear within 24 hours, in which case the timeframe shall be no greater than 48 hours;

8.6(b). If the employer appears before the GRI, the GRI shall propose options to find a satisfactory solution to avoid the closure or dissolution of the enterprise and for the employer to ensure payment of remuneration owed to workers upon closure or dissolution if the closure or dissolution is not avoided. If the GRI, the employer, and the workers reach an agreement on a satisfactory solution, the IGT shall document it so as to generate an enforceable legal instrument, and the IGT shall monitor and follow up on compliance with the agreement;

8.6(c). If the employer does not comply with the summons to appear before the GRI or no agreement is reached as a result of the meeting, the IGT shall undertake a preliminary determination of remuneration owed to workers, unless such determination has already been undertaken, and shall take the actions described in subparagraph 8.2(b); and

8.6(d). If the IGT determines that the employer has failed to make the required payments within the timeframe established in the agreement or has otherwise failed to comply with the agreement, the IGT shall undertake a preliminary determination of remuneration owed to workers, unless such a determination has already been undertaken, and shall take the actions described in subparagraph 8.2(b).

8.7. **Within 90 days**, Guatemala shall publish this Ministerial Accord on the MOL, MOE, IGSS, SAT, and judiciary websites and shall inform all personnel whose responsibilities could be affected by this Ministerial Accord.

8.8. **Within 120 days,** Guatemala shall train all labor inspectors and all other MOL, MOE, IGSS, SAT, or judiciary personnel whose responsibilities could be affected by this Ministerial Accord.

9. Employer Substitution

9.1. Guatemala, through the MOL, shall develop, publish, and apply objective criteria for determining provisionally whether an employer substitution has occurred under Article 23 of the Labor Code. If the MOL determines provisionally that, based on the totality of circumstances, employer substitution has occurred, the MOL shall issue a provisional determination of the substitution and Guatemala shall apply Article 23 of the Labor Code.

9.2. **Within 60 days,** Guatemala shall prepare criteria for determining provisionally whether employer substitution has occurred under Article 23 of the Labor Code. The criteria shall include factors such as whether the facilities, machinery, equipment, workers, jobs, working conditions, production methods, and products or services produced or supplied by the new entity are the same or similar to those of the previous entity.

9.3. **Within 60 days,** Guatemala shall publish on the MOL website the criteria for determining provisionally whether employer substitution has occurred and shall inform all MOL and judiciary personnel whose responsibilities could be affected by the new criteria.

9.4. **Within 90 days,** Guatemala shall prepare an MOL directive, or similar legal instrument, to direct the application and administration of such criteria and shall inform all MOL personnel whose responsibilities could be affected by this directive.

9.5. **Within 90 days,** Guatemala shall: (i) publish on the MOL website a list of provisional employer substitution determinations issued by the MOL and subsequent final determinations issued by the

Labor Courts in the prior month, including the names of the predecessor and successor enterprises and the dates of the determinations, and thereafter update the list on a monthly basis; (ii) indicate on the MOL website, in the context of the list, that such employer substitution determinations may serve as evidence that employer substitution has occurred in any MOL and Labor Court proceedings involving the same employers; and (iii) provide copies of such final determinations to workers who request them.

B. Enforcement of Labor Court Orders

10. System for Tracking Compliance with Court Orders

10.1. **In September 2012,** Guatemala incorporated new fields into the standardized electronic case management system (the "Court Management System") to be used by all Labor Courts to effectively and systematically track: (i) employer compliance with Labor Court orders within the timeframes established by law; and (ii) the judicial measures taken to enforce such court orders. Guatemala shall maintain this Court Management System, ensure that it contains all information relevant to the enforcement of Labor Court orders and to actions taken against employers for failure to comply with Labor Court orders, and provide access to the Court Management System appropriate to the parties to the case, which includes the MOL in all cases, and to the MOE.

10.2. **Within 30 days,** Guatemala shall ensure, including through any necessary technical amendments, that this Court Management System includes, at a minimum, the following information:

10.2(a). All information that may be relevant to the enforcement of a Labor Court order, including: the names and the addresses of the parties; the case number; the procedural status of the case; the date(s) of any final orders; the Labor Code articles violated; any amount determined by the court to be owed to workers; applicable fine amount; the deadline for complying with the order; and the status of compliance, including the dates on which the Verification Unit assessed compliance and any findings thereof; and

10.2(b). All information concerning court actions taken against a party for failing to comply with a court order, including: the date on which the Labor Court attempted to embargo or seize the employer's assets to secure payment of any unpaid fines and/or remuneration due to workers and the result of such action; and whether the Labor Court has referred the employer's failure to comply with the court order to the corresponding Criminal Court and, if so, the date on which it did so and the results thereof.

10.3. **Within 90 days,** Guatemala shall ensure that all parties to a case have secure internet access to all information related to their case that is maintained in the Court Management System. Such access may be provided using an individual username and password.

10.4. **Within 60 days,** Guatemala shall ensure that the Labor Courts make the following information on closed cases publicly available, upon prior written request: case status; all final court determinations; the status of compliance with those orders; and all actions taken by the Labor Court to enforce Labor Court orders against a party found to have violated labor laws.

10.5. **Within 90 days,** Guatemala shall ensure that in those cases to which the MOE is not a party, the judiciary shall provide the MOE with read-only access to the information contained in the Court Management System through secure internet access, so that the MOE can verify the enforcement of court orders, as required in Sections Six, Seven, and Eight of this Enforcement Plan.

10.6. **Within 120 days,** Guatemala shall complete the training for all Labor Court personnel responsible for maintaining and updating the Court Management System.

11. Verification of Employer Compliance with Court Orders

11.1. **On July 20, 2012,** the Guatemalan Supreme Court issued Accord No. 26-2012, which created the Verification Unit within the judiciary to verify employer compliance with all Labor Court orders within the timeframes required by law. Accord 26-2012 requires the Verification Unit to document

electronically, and prepare monthly reports with statistics on, actions taken by the Verification Unit and the status of employer compliance with Labor Court orders.

11.2. **Within 30 days,** Guatemala shall ensure that the Verification Unit shall verify compliance with all Labor Court orders within the timeframes required by law, including orders for reinstatement, remediation of labor law violations, remittance of amounts owed to workers, and payment of fines assessed by the court.

11.3. **Within 30 days,** Guatemala shall prepare standardized procedures, criteria, and forms to be used by the Verification Unit and other Labor Court executors when verifying employer compliance with a Labor Court order.

11.4. **Within 60 days,** Guatemala shall publish and provide copies of the standardized procedures, criteria, and forms to all judicial personnel whose responsibilities could be affected by the changes, including all members of the Verification Unit and Labor Court executors.

11.5. **Within 120 days,** Guatemala shall assign sufficient resources to the Verification Unit to enable it to carry out its functions effectively.

12. Monitoring Judicial Enforcement of Labor Court Orders

12.1. Guatemala, through the judiciary, shall ensure that Labor Courts take the necessary measures required by law, within the timeframes required by law, to enforce Labor Court orders against employers found to have violated labor laws.

12.2. **Within 60 days,** Guatemala, through the judiciary, shall develop a program to monitor Labor Courts' enforcement of orders, which, at a minimum, shall include the following:

12.2(a). A review of all Labor Courts and Labor Courts of Appeal at least every 180 days to verify whether court orders were issued within the timeframes prescribed by law and whether all measures required by law were taken to ensure compliance with such orders, including increases in fines, embargos or seizures of assets, and referrals to the Public Ministry (PM) for failures to obey court orders, through periodic visits to the Labor Courts and Labor Courts of Appeal, as well as reviews of the Court Management System and the Verification Unit's monthly reports;

12.2(b). Designation of a coordinator and supervisor executor to conduct the periodic monitoring visits to the Labor Courts and Labor Courts of Appeal and reviews of the Court Management System and monthly Verification Unit reports and to prepare reports every 180 days documenting instances where Labor Courts and Labor Courts of Appeal fail to take measures required by law to enforce court orders, which shall include the date on which a court order was issued, the timeframe provided for compliance, and what measures were taken, if any, by the Labor Courts to enforce the order; and

12.2(c). The application of disciplinary procedures established in Title V, Chapters I and II, of the Judicial Career Law to judges who do not adopt measures required by law to enforce court orders.

12.3. **Within 75 days,** Guatemala shall publish on the website of the judiciary a description of the monitoring program, implement it by initiating the review of Labor Courts, and inform and provide copies to all Labor Court personnel whose responsibilities could be affected by the monitoring program, including Labor Court judges and the Office of the General Court Supervisor.

13. Application of Labor Code Articles 209, 379, and 380

13.1. Guatemala, through the judiciary, shall clarify the application of Labor Code Articles 209, 379, and 380 to improve the protection of workers actively engaged in protected associational activity, including but not limited to, union formation and collective bargaining.

13.2. **Within 45 days,** Guatemala, through the judiciary, shall prepare a training program to be provided to Labor Court judges and magistrates regarding the application of Labor Code Articles 209, 379, and 380, clarifying, at a minimum, that:

13.2(a). The protections established in Articles 379 and 380 take effect from the moment workers submit their list of demands to the relevant Labor Court, establishing a collective conflict;

13.2(b). The protections established in Article 209 take effect from the moment workers give notice, in any written form, to the IGT, directly or through regional offices with delegated authority, that they are forming a union, and that these protections exist for 60 days from the date of registration of the union, regardless of when or whether the relevant employer is notified;

13.2(c). A Labor Court shall, within 24 hours of receiving a complaint of unlawful dismissal in violation of the above provisions, issue immediate reinstatement orders for workers dismissed in violation of such articles and designate Labor Court executors to enforce such reinstatement orders against the employer; and

13.2(d). If an employer fails to comply with an order under Articles 209 and 379 within seven days, the Labor Court shall increase by 50 percent the penalty imposed. If an employer fails to comply with an order under Article 380 within seven days, the Labor Court shall double the penalty imposed, and where an employer still fails to comply within seven days after the Labor Court has doubled the penalty, the Labor Court shall immediately refer the matter to the Criminal Court for failure to obey the Labor Court order.

13.3. **Within 60 days,** Guatemala, through the Public Ministry, shall develop the legal procedure necessary to ensure effective criminal prosecution of cases referred by Labor Courts of employer failures to comply with Labor Court orders, in conformity with Articles 209, 379, and 380. The procedure shall comply with the timeframes established in the relevant labor laws and shall establish a notification mechanism to inform Labor Courts of the outcomes of referred cases, which shall also be recorded in the Court Management System referenced in Section 10.

13.4. **Within 90 days,** Guatemala shall publish on the websites of the Public Ministry and the judiciary the procedure described in the preceding paragraph and shall inform all Public Ministry and judicial personnel whose responsibilities could be affected by the procedure, including Labor Court judges and Criminal Court judges.

13.5. **Within 120 days,** Guatemala shall complete training of all relevant Labor Court personnel on the application of Labor Code Articles 209, 379, and 380.

13.6. **Within 120 days** Guatemala, through the judiciary, shall train all judicial personnel whose responsibilities could be affected by the procedure described above.

13.7. **Within 120 days,** Guatemala, through the Public Ministry, shall train all prosecutors and Public Ministry personnel whose responsibilities could be affected by the procedure described above.

C. General Provisions

14. Transparency and Tripartite Coordination on Enforcement Plan Implementation

14.1. Guatemala, through the MOL, shall present the content of this Enforcement Plan to the Tripartite Commission on International Labor Affairs, established to represent the distinct sectors on labor issues, in conformity with International Labor Organization Convention 144, and shall discuss implementation of the Enforcement Plan with the Tripartite Commission on an ongoing basis.

14.2. The institutions involved with implementing this Enforcement Plan shall publish its content on their websites, and for the purpose of transparency, shall receive and consider comments from interested parties and shall meet with interested parties as appropriate.

15. Publication of Labor Law Enforcement Statistics and Data

15.1. **Within 120 days and annually thereafter,** Guatemala shall publish on the MOL website:

15.1(a). Statistics on inspection visits conducted by the MOL in the preceding year, by region and sector (*i.e.*, commerce, industry, agriculture and services), as well as statistics on confirmed violations, their resolution, and referral of cases to the Labor Courts; and

15.1(b). Statistics on complaints or reports received by the IGT, in the Department of Guatemala and other departments, and the application of standardized timeframes for inspections.

15.2. **Within 120 days and every 180 days thereafter,** Guatemala shall publish a report on the judiciary's website, based on the information compiled from the Labor Courts' Court Management System, that shall include, at a minimum, the number of rulings issued to enforce labor laws and statistics on the following, with disaggregated data on cases of violations of Labor Code Articles 209, 379, and 380:

15.2(a). Labor Court verification of employer compliance with court-issued reinstatement orders within the legally established timeframes [Sections 4, 11];

15.2(b). Labor Court verification of employer remediation of identified labor law violations within the legally established timeframes [Sections 4, 11];

15.2(c). Labor Court verification of employer payment of fines assessed and amounts owed to workers within the legally established timeframes [Sections 4, 11];

15.2(d). Embargos or seizures of assets and other preventive measures taken by Labor Courts to ensure the payment of overdue fines assessed and amounts owed to workers [Section 4];

15.2(e). Labor Court referral to the PM of cases of failure to comply with court orders, including the total number of cases in which employers received criminal sanctions for failure to comply [Sections 4, 13];

15.2(f). Sanctions against Labor Court judges who have not undertaken all measures required by law, within the timeframes required by law, to enforce their orders [Sections 12, 13]; and

15.2(g). Sanctions against judicial personnel who have not followed procedures required by law for effective criminal prosecution of cases referred by Labor Courts of employer failure to comply with worker reinstatement orders [Section 13].

15.3. Guatemala shall make every effort to continuously improve the judiciary's website and update the information that is published, as well as the respective search options.

16. Verification of Enforcement Plan Implementation

16.1. Guatemala shall provide information at the end of July, October, January, and April, to publicize the progress of this Enforcement Plan. If a Party identifies a concern regarding the operation of this Enforcement Plan, the Parties shall promptly meet, in person or by other appropriate methods, to discuss the concern.

16.2. The Parties shall share information relevant to determining whether this Enforcement Plan is being implemented within the timeframes established.

16.3. Guatemala shall provide the United States with a copy of any instrument, mechanism, or procedure directly relevant to the implementation of this Enforcement Plan prior to its finalization and again upon issuance.

17. Support and Cooperation from the United States in Implementing the Enforcement Plan

17.1. The United States, upon request of Guatemala and as appropriate, shall support Guatemala's successful implementation of this Enforcement Plan by providing technical advice and information regarding best practices, sharing expertise, and assisting with outreach to international institutions.

18. Final Provisions

18.1. The United States and Guatemala shall jointly request the CAFTA-DR Labor Dispute Panel (Panel), established under CAFTA-DR Article 20.6 on August 9, 2011, to suspend its work for a period of six months from the date of the signing of this Enforcement Plan.

18.2. The United States and Guatemala shall review the operation of this Enforcement Plan and jointly request the Panel to extend the suspension for an additional six months, unless a Party considers that the Enforcement Plan has not been implemented in the timeframes set out herein.[3]

18.3. A Party may request the Panel to resume its work only: (a) if it considers that this Enforcement Plan has not been implemented in the timeframes set out in this Enforcement Plan; or (b) in the circumstance described in Section 4.4.

18.4. The United States shall terminate the Panel proceeding one year from the date of the signing of this Enforcement Plan, provided it considers that this Plan has been implemented in the timeframes set out herein.

18.5. The timeframes referenced in this Enforcement Plan shall commence on the date this Enforcement Plan is signed by both Parties or, if the Parties sign this Enforcement Plan on different days, on the date this Enforcement Plan is signed by the second Party.

18.6. Unless otherwise specified in this Enforcement Plan, all timeframes referenced in this Enforcement Plan shall consist of calendar days, not business or working days.

18.7. This Enforcement Plan shall enter into force once it is signed by both Parties.

18.8. The English and Spanish texts of this Enforcement Plan are equally authentic.

[3] For greater certainty, the Parties' joint request(s) to the Panel to suspend its work in paragraphs 18.1 and 18.2 shall specify that the Panel shall resume its work: (i) automatically at the end of the six-month suspension, unless otherwise directed by joint request of the Parties; or (ii) at any time upon request of either Party.

IN WITNESS WHEREOF, the undersigned, being duly authorized by their respective Governments, have signed this Agreement.

For the Government of the United States of America:

Ambassador Miriam E. Sapiro

Deputy United States Trade Representative

Date April 25, 2013

For the Government of the Republic of Guatemala:

Sergio de la Torre Gimeno

Minister of Economy

Date Abril 26/2013