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The Dominican Republic came late to the Central America Free Trade Agreement (CAFTA) party, but ratified it nonetheless, largely because, as President Leonel Fernandez was to say later, the country had no other market for its goods. But now the country is in some jeopardy of not being aboard when the treaty comes into effect in January 2006. The issue is fiscal reform (see NotiCen, 2005-09-08), with the Congress and the presidency at odds on the question.

On Dec. 2, the Chamber of Deputies, where the opposition Partido Revolucionario Dominicano (PRD) dominates, passed a fiscal-reform law that the government says does not compensate for the resources lost to the treasury from tariffs and a 13% import tax (comision cambiaria) bargained away in the CAFTA negotiations.

Temistocles Montas, presidential technical secretary, said the reform package only guarantees income to the government of US$761.2 million, short of the US$906.2 million the government says it needs. "The government cannot afford the luxury of accepting a fiscal reform under these terms, nor does it have the possibility of reducing spending programmed for the coming year in view of the accords agreed to with the International Monetary Fund (IMF)," said the secretary.

The government must now look to the Senate, where the PRD also rules, to amend the bill. Otherwise, said Montas, there will be no choice but to reinstate the 13% tax, "and that automatically removes us as a country from the free-trade agreement with the United States and Central America."

The government was blindsided by a closed-door session of PRD deputies with their party president, Sen. Ramon Alburquerque, wherein they modified an agreement previously reached between the government and Alfredo Pacheco, president of the lower chamber. The law they passed raises the income tax until 2009 by 5% to 30%, imposes a 17% tax on new car sales, a 10% tax on premium gasoline, a 15% tax on diesel, and creates a 1.5% gross receipts tax, the sum of all of which leaves the administration short more than US$200 million for the coming fiscal year.

Blaming the PRD, Montas said that, by preventing participation in CAFTA, the law would cost the Dominican Republic US$1 billion. He also projected the loss of 166,000 maquila jobs and untold foreign investment. Secretary of the Presidency Danilo Medina put the number of lost jobs at 265,000. Before the vote, Medina called upon lawmakers to recognize that the reform is not "the caprice of the government that it wants to reform some tax laws to gain resources, it is an obligation of the free-trade agreement." He told reporters that, when CAFTA was negotiated, lawmakers knew that the treaty "topples taxes, topples resources to the state, and you who live by traveling around the country know that the needs of the people are immense and the resources very scarce, so there is no [other] way to help those in need." He predicted that, if the legislature did not come through, "we are definitely going to lose a lot of jobs."

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The difference in the number of jobs hanging in the balance may be the result of Medina's including future jobs as well as current ones. He said that the Consejo Nacional de Zona Franca has qualified 43 new foreign operations in the maquila sector scheduled to start operations when CAFTA comes into existence. The government had been looking for a package that would have bolstered its income from taxes on goods and services, alcoholic beverages, publicity, real property, and other productive sources.

That opportunity lost, it was left for Montas to predict a popular reaction to the congressional action. "I believe the population is going to perceive very clearly that, facing the challenge the country has of entering into the free-trade agreement, the government did what it had to do, and now it is up to the PRD to assume its responsibility," he said. "The PRD got the country involved in the free-trade agreement and doesn't want to assume its responsibility."

Government must meet expectations on several fronts

The government is under pressure both from the US and from the IMF to set conditions for CAFTA and also to secure approval of an IMF loan agreement. About a week before the vote, US Ambassador to the Dominican Republic Hans Hertell strongly criticized the government's slowness in taking the steps for implementing CAFTA. It is useful to recall that the US has had a very bad year internationally in many areas, and President George W. Bush had just suffered a thundering defeat in trying to restart Free Trade Area of the Americas (FTAA) negotiations in Argentina (see NotiCen, 2005-11-10 and NotiSur, 2005-12-02).

The US also has every reason to expect additional humiliation at the December meeting of the World Trade Organization (WTO) culminating Doha Round meeting in Hong Kong. CAFTA is their only success, very narrowly won, and Hertell needs the agreement implemented. Yet, in a speech to the American Chamber of Commerce on Nov. 23, the ambassador took the country to task, telling his listeners that the Dominican Republic's entry was "not guaranteed."

In addition to inaction on CAFTA, the ambassador also noted an increase in the movement of drugs through the country and a growing "culture of impunity" in a context of scant government transparency. He said that the embassy was mandated by law to report on these matters, and a negative report could affect CAFTA entry. Hertell's statement was the second of its kind in recent days.

Earlier, USAID resident director Elena Brineman also linked corruption and lack of transparency to CAFTA prospects. The US rhetoric brought official response. Armed Forces Minister Adm. Sigfrido Pared Perez said that the US had not managed to curtail entry of drugs to its own territory. Adm. Ivan Pena Castillo, the country's anti-drug chief, defended his country's performance, saying its successes were matched by few others. Mario Vinicio Castillo, the president's drug advisor, asked why Hertell had been so "permissive" about drug traffic during the previous administration, when, he implied, the situation was much worse.

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Topping off the irate response, Reinaldo Pared, secretary-general of the ruling Partido de la Liberacion Dominicana (PLD), said Hertell had "overstepped the boundaries" of appropriate diplomatic behavior. The other source of pressure on the government, the IMF, completed its third review of the Dominican Republic's program in mid-November. The review was favorable on balance, as had been the first and second reviews in mid-October. But this time, said Guy Meredith, mission chief for the country, "discussions focused on measures needed to underpin the envisaged fiscal adjustment. These include implementing a revenue-neutral tax reform consistent with early entry into DR-CAFTA."

The setback in the reform package appears set to impede progress to the next step, submission of the government's Letter of Intent to the IMF. The government has a total disbursement from the IMF of US$665 million at stake. Before the derailment of the reform package, the Dominican Republic was looking at a rosy economic picture for the near term.

The Economic Commission for Latin America and the Caribbean (ECLAC) had projected 7% growth for the year, and the organization's executive secretary Jose Luis Machinea said growth should continue at that rate next year, but he emphasized on Dec. 4 that this would depend on CAFTA and on the fiscal reform that would enable it. He was in the country for a multiday Seminario Desarrollo y Politicas Economicas: Experiencia Internacional y Lecciones Aprendidas. But whether these projections would translate into benefits for ordinary Dominicans was quite another matter.

Also present at the seminar was Jorge Mattar, an ECLAC specialist from Mexico. He added a caveat based on his experience with NAFTA, telling the media that CAFTA includes asymmetries that must be recognized during the negotiation and again when the treaty is implemented. He warned that a trade agreement of itself is not enough to overcome poverty and that the private sector, the public, and civil society must see that the promise of free trade translates into the general welfare.

Meanwhile another participant, Jose Luis Aleman, who sat on a panel on social policy as a key to development, said that the Dominican Republic's social budget is a "tragedy" and that the country pursues a "clownish" policy. He said the country needed reforms to make life and commerce more humane and the application of policies that favor people, especially in education and health.

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