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Caribbean Basin Economic Development and the Section 936 Tax Credit

Richard L. Bernal and Stephen E. Lamar

The U.S. government's recent repeal of Section 936 of the U.S. tax code has disconcerted Caribbean countries and raised questions as to its effects on U.S. interests in the region. The privately financed Caribbean loan program that stems from the Section 936 credit has significantly enhanced economic development of the Caribbean Basin and has contributed to a steady increase in the growth of trade between the region and the United States over the past 10 years. Jamaican Ambassador Richard L. Bernal and Stephen E. Lamar examine the importance of the tax credit and loan program and offer policy recommendations for meeting both U.S. and Caribbean interests in light of the recent repeal.

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CARIBBEAN BASIN ECONOMIC DEVELOPMENT AND THE SECTION 936 TAX CREDIT

Richard L. Bernal and Stephen E. Lamar

Introduction

In 1986, as part of a major overhaul of the U.S. tax code, the U.S. Congress made a valuable source of private sector financing available for Caribbean economic development.¹ Less than 10 years later, as part of a series of measures to balance the U.S. federal budget and enact a package of tax cuts for small businesses, the Congress approved legislation to terminate this source of funds for the Caribbean.²

The pool of investment capital for the Caribbean has actually been generated through the investment of profits of U.S. companies operating in Puerto Rico under a tax credit contained in Section 936 of the U.S. tax code.³ These profits were made available to entrepreneurs and investors, who used the funds to finance investment and capitalize projects throughout the Caribbean. As a result, although Section 936 has been seen primarily as a tool to promote growth and employment in Puerto Rico, it emerged as a key financing source for investment and economic development throughout the Caribbean.

What has not been fully understood in the debate over the Section 936 repeal is the importance that Section 936 has held for the Caribbean and, as a result, for U.S. economic and strategic interests (a summary of the uses and effects of Section 936 is depicted in Chart 1). While the repeal was effected to offset the budgetary impact of small business and adop-

tion tax credits, it has inadvertently reversed a major policy supporting U.S.-Caribbean economic relations. It has eliminated the incentive structure behind the Caribbean loan program, causing a significant financing gap that will have a detrimental effect on U.S.-Caribbean trade relations and on Caribbean economic development.

This paper examines the operation of Section 936 as it has functioned to the benefit of the Caribbean and to the benefit of U.S. interests in the region. Specifically, the first section outlines the parameters of the general debate over the Section 936 tax credit. The second section describes the rationale for the Section 936 loan program as an essential complement to the original Caribbean Basin Initiative (CBI). The third section explains the working of the program, and the fourth section identifies ways in which the program has stimulated economic development and promoted regional stability. The final section reviews policy recommendations to preserve Caribbean and U.S. economic development in light of the demise of the Section 936 Caribbean loan program.

The term "Section 936" refers either to a provision in the U.S. tax code or to the credit contained in that provision. The Caribbean loan program is the mechanism through which loans, sometimes referred to as 936 loans, are made available to eligible Caribbean Basin countries. This program is also known as the Caribbean lending program

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or the Caribbean Development Program, the latter of which is the official name given by the Puerto Rican government.

The Section 936 tax credit itself was made available to businesses that operated or invested in Puerto Rico (or other U.S. territories). To minimize their potential tax exposure, these "Section 936 companies" retained most of their profits in financial institutions in Puerto Rico. Section 936 provided that interest and investment derived from these profits would be exempt from federal taxes. In addition, by virtue of an amendment enacted as part of the Tax Reform Act of 1986, the Section 936 tax credit was modified to permit the use of these funds for loans to certain Caribbean Basin countries. Although this Caribbean loan program was subject to criteria established by the U.S. and Puerto Rican governments, the funds were generated solely by private sector firms using the Section 936 tax credits and were loaned at the discretion of financial institutions.

Background on Section 936 and Its Impact on Puerto Rico

Despite the importance of this program for the Caribbean, the debate over its credit has been overshadowed by the larger debate over the use of Section 936 as an effective tax stimulus for Puerto Rico's development.⁴ In fact, in the past five years, Section 936 has generated considerable controversy as different groups in Puerto Rico and throughout the United States have offered competing views over the effectiveness of the credit in furthering economic goals, especially job creation, in Puerto Rico. As a result, the fortunes of the Caribbean loan program have been directed by the debate surrounding the overall Section 936 credit.

Perhaps the biggest source of controversy has arisen from the perception that Section 936 disproportionately benefits large pharmaceutical corporations, which include some of the largest credit recipients. The Treasury Department estimated that in 1989 the average

pharmaceutical worker in Puerto Rico earned \$30,400, while the tax expenditure for each pharmaceutical job created equaled more than \$66,000.⁵ The Treasury Department and others in Congress have used such statistics to claim that the tax burden of Section 936 far exceeded the benefit in terms of jobs created. They have also been the driving force behind proposals of the Clinton administration and the Puerto Rican government to redesign the credit as a wage-based credit.⁶

A similar argument has emerged over the role of Section 936 in isolating or distinguishing Puerto Rico from the rest of the United States. This sensitivity has often colored the ongoing debate in Puerto Rico over the island's political identity and the future of its commonwealth status with the United States. This means that Section 936 often emerges as a potent campaign issue in Puerto Rican politics.⁷ Puerto Rico's Resident Commissioner, Carlos Romero Barcelo, has argued forcefully that Section 936 has encouraged companies to think of Puerto Rico as a foreign country. He argued that Section 936 has not been necessary to establish a competitive presence in Puerto Rico and that Section 936 should be phased out, preferably in exchange for the granting of health care benefits enjoyed by other U.S. citizens, such as Medicaid.⁸ Conversely, proponents of continued commonwealth status for Puerto Rico have argued for the retention of Section 936 by arguing that loss of the tax credit could lead to a 50-percent rise in unemployment in the island.⁹ The U.S. business communities in Puerto Rico and in the United States have argued that the program is necessary to attract investment. They also point to the number of jobs created in Puerto Rico to show the program's economic benefit on the island.¹⁰ At the same time, organized labor groups have argued that Section 936 has encouraged U.S. firms to close factories in the United States in favor of Puerto Rican facilities. They have insisted that the Section 936 credit be eliminated or scaled back to emphasize the linkage with wages paid.¹¹

While controversies over the credit's effectiveness and ambiguous levels of support from Puerto Rico have made the credit vulnerable, the prospect of recouping foregone tax revenues has probably been the largest motivator for attacks on the program. Under U.S. budget laws, any changes in tax policy that would increase the budget deficit must be offset by other changes so there will be a net neutral effect of all the changes on the budget deficit. This means that any tax cuts or program cuts must be offset by increasing taxes in other areas or by repealing or scaling back tax credits.¹² By providing a credit to U.S. companies that do business in Puerto Rico, the government is foregoing tax revenue that would be generated by those companies. If collected, this revenue could be applied against the budget deficit or be used to fund other Federal programs.

The Section 936 tax credit has been reduced on two separate occasions since the Clinton administration assumed power because of this budget requirement. The credit was first scaled back in 1993 to help raise \$3.8 billion (over a five-year period) to offset changes wrought by President Clinton's tax plans during the first year of his administration.¹³ Two years later, to help pay for Republican tax cuts in the Balanced Budget Act of 1995 (HR 2491), Congress approved a plan to repeal Section 936 and phase out its benefits over a 10-year period.¹⁴ Although this legislation ultimately was vetoed by President Clinton in December 1995, many of the Section 936 provisions reemerged in the spring of 1996 in the Small Business Job Protection Act of 1996 (HR 3448). In that bill, the Section 936 repeal generates about \$10.5 billion of additional tax revenues over a 10-year period, providing about 80 percent of the offsets for a legislative package, including a raise in the minimum wage, a series of small business tax credits, an adoption tax credit, and a number of other tax changes.¹⁵ President Clinton signed that bill into law on August 20, 1996, thereby effectively repealing Section 936.¹⁶

The Caribbean loan program became a casualty of these attacks on Section 936. While the Caribbean loan program survived the 1993 changes, its viability was eliminated as part of the repeal provisions in HR 3448 in 1996. Section 1601(c)(2) of HR 3448 calls for the repeal of qualified possession source investment income (QPSII) — which supports the Caribbean loan program — for tax years beginning after December 31, 1995, or earned after June 30, 1996.¹⁷ The net effect of this modification is to eliminate the incentive that makes the Caribbean loan program work, while encouraging the funds that formed the basis of the Caribbean loan program to be invested elsewhere.¹⁸

The U.S. Congress belatedly acknowledged the effect of the repeal on the Caribbean by stating as much in the Conference Report accompanying HR 3448, but it did little to temper the impact of this action on the Caribbean. In that report, Congress admitted that “the repeal of the credit for QPSII will have the effect of eliminating a provision that has supported economic development and trade-related growth in the Caribbean Basin and served U.S. interests in that region,” but stated that “the repeal should not be interpreted as a loss of interest in the region.”¹⁹ In so doing, Congress implicitly recognized that the dismantling of a key U.S.-Caribbean policy tool was effected without due consideration of whether such a policy change was warranted or would advance either U.S. or Caribbean interests.

The Interrelationship Between the Caribbean Basin Initiative and Section 936

The Section 936 Caribbean loan program has come to play an integral role in fulfilling the original intent of the Caribbean Basin Initiative (CBI), which was launched by the United States in 1982 to promote stability through economic growth in the Caribbean Basin, a region consisting of island countries within the Caribbean and countries bordering the Caribbean, including those in Central

America and a few in South America. The CBI proposal grew out of a perception that adverse terms of trade, changing market conditions, and the persistence of undemocratic regimes in Grenada, Nicaragua, and Cuba would undermine the social and political stability of Caribbean countries, thereby eroding U.S. security interests in the region.²⁰ As proposed, the program envisioned a series of trade preferences, tax incentives, and technical and financial assistance to promote private investment and the growth of a revitalized export sector throughout the Caribbean. The rationale in 1982 was that reducing poverty through economic development and the strengthening of democratic institutions and practices would counteract the influence of communist elements in the Western Hemisphere. In short, by forging a closer link between the Caribbean Basin countries and the United States, Washington would maintain its traditional influence in the region.²¹

Trade Preferences Under the CBI

Congress responded to the Reagan administration's CBI proposal by enacting the Caribbean Basin Economic Recovery Act (CBERA) of 1983, which became effective on January 1, 1984.²² That act and subsequent legislative and administrative modifications implemented over the following decade eliminated or reduced duties and improved quota access to the U.S. market for most products from eligible Caribbean Basin countries. Eventually, the CBI was extended to encompass most products, although it continues statutorily to exclude textiles and apparel, footwear, luggage, watches, tuna, and petroleum products.

The CBI program has also created a number of miscellaneous trade provisions to support or regulate individual imports from CBI countries. The CBI established a framework governing market access into the United States for Caribbean and Central American sugar, beef, fruit, vegetable,²³ and ethanol²⁴ exports to the United States and established several mechanisms to link Caribbean exports,

including exports of rum and coffee, with similar products from Puerto Rico and the United States.²⁵ In addition, the CBI exempts beneficiary country products from cumulation rules used to calculate dumping and determine if an imported product is materially injuring a U.S. industry.²⁶ In general, by virtue of these trade preferences for CBI countries, the CBERA provided beneficiary CBI countries preferential access to the U.S. market not enjoyed by other developing nations.

Supporting Executive Branch Programs

Since the mid-1980s, other U.S. government agencies have responded to the passage of the CBERA by making a number of aid and financing programs available to eligible Caribbean Basin countries. These programs, which have complemented CBI trade preferences to varying degrees, have been administered by the U.S. Agency for International Development (USAID), the Overseas Private Investment Corporation (OPIC), the Trade and Development Agency (TDA), the U.S. Department of Agriculture (USDA), the State Department, and the Export-Import Bank (Eximbank) of the United States. Moreover, under the Enterprise for the Americas Initiative (EAI), the U.S. government has supported Caribbean economic development by providing debt relief to several Caribbean Basin countries²⁷ and contributing to the Inter-American Development Bank's Multilateral Investment Fund.²⁸

Tourism Promotion

In addition, as part of the CBI legislation, Congress enacted several programs to promote tourism in the Caribbean. Section 222 of the CBERA authorizes U.S. taxpayers to deduct the cost of conventions held in the countries that have signed Tax Information and Exchange Agreements (TIEA) with the United States.²⁹ Sections 232 and 233 of the Caribbean Basin Economic Recovery Expansion Act (CBEREA) of 1990 required the Commerce Department to study the regional

tourism industry and authorized the establishment of customs pre-clearance facilities.³⁰

Deficiencies in the CBI Program

While these CBI-targeted programs provided an important framework under which an enhanced U.S.-Caribbean economic partnership could be created, they failed to address three key elements of that partnership.

Financing Constraints. First, none of these programs provided a sustainable mechanism through which Caribbean investments could gain access to private capital. This was especially critical for the Caribbean countries, many of which suffered from extensive credit shortages and large debt burdens during the early 1980s.³¹ This was a significant constraint in that, although the trade provisions of the CBERA established a pattern of export incentives, they did not necessarily facilitate capital formation, which was critical as a catalyst for the formation of export enterprises.³² While the original CBERA proposals contained a financing provision, the version that was ultimately enacted by the Congress in 1983 had left out those provisions.³³ As a result, although access to the U.S. market improved with the passage of the CBERA, many Caribbean enterprises were not able to take immediate advantage of that improved access. In fact, during the first four full years of the CBERA, from 1984 through 1987, U.S. imports from CBERA countries actually declined by more than 30 percent, even though duties on those imports were lowered.³⁴ It was not until 1992 that U.S. imports from the Caribbean Basin actually surpassed the import level established in 1984.³⁵

U.S. official assistance flows helped close some of the financing gap in the Caribbean Basin by making funds available for public sector programs or the implementation of trade-based economic reform measures. These programs, however, did not adequately address the credit needs of the private sector, particularly of small- and medium-sized entrepreneurs throughout the region. Moreover, as U.S. fiscal realities began to affect the foreign

aid budget, official development assistance actually played a declining role in supporting Caribbean economic development, even at the public sector level. In 1984, U.S. assistance and export credits to the 24 Caribbean Basin countries equaled \$1.262 billion. By 1994, the level of assistance had dropped to just over \$544 million, a decline of more than \$700 million.³⁶ See Table 1 for more information on declining U.S. bilateral aid flows to the Caribbean Basin region.

Uncertainty. A second constraint of the original CBI is that the program by itself had been unable to generate a significant level of investment flows into the region. For the first six years, the CBI faced a 12-year sunset, making it difficult to attract long-term investment.³⁷ Although the program has since been made permanent, Congress can modify or eliminate it easily without any recourse by Caribbean countries. The administration also enjoys the ability to remove a beneficiary country from the CBI program if that country fails to meet the eligibility criteria. Similarly, strong domestic protectionist pressures make it difficult to modify the CBI to respond to changes in the U.S.-Caribbean trading regime. For example, although the implementation of new trading regimes under the General Agreement on Tariffs and Trade (GATT) and the North American Free Trade Agreement (NAFTA) have eroded many of the trade preferences contained in the basic CBI program, Congress has been unable to enact legislation to rectify these growing imbalances.³⁸

Product Coverage. A third weakness of the CBI is that it excludes some products and industries, such as apparel and footwear, in which the region has a comparative advantage. Such product exclusion not only heightens investor insecurity in the program, by reminding them that the program exists at the discretion of the U.S. Congress, but it also inadvertently channels investment away from those products for which the Caribbean enjoys good export prospects.

Ironically, because Caribbean production has shifted into those industries specifically

excluded from the CBI, Caribbean exporters are now paying higher average duties than they were paying in 1984. A recent U.S. International Trade Commission (USITC) report shows that the average duty paid for CBI imports was 1.9 percent in 1984 but 11.5 percent in 1994. The USITC attributes this steady increase in the average duty to the changing product mix of Caribbean exporters away from "lower duty items such as petroleum products to higher duty goods, such as wearing apparel."³⁹ Unfortunately, the dynamic shift in production in the Caribbean, combined with the inflexibility of the CBERA, means that the CBERA duty provisions alone have had a decreasing impact in support of Caribbean Basin economic development.

Section 936 as a Response to the CBERA

To a large degree, the Section 936 Caribbean loan program has helped compensate for the shortcomings of the CBERA. Section 936 funds, which first became available to the Caribbean in 1988, have filled a needed gap by providing a growing source of private sector financing and by enabling Caribbean countries to adjust to the disciplines of market-oriented reforms.⁴⁰ Similarly, Section 936 helped alleviate uncertainties of economic development in the region by establishing a secure source of capital that could be made available for medium- and long-term financing. Because Section 936 funds can be used to finance investment in industries excluded under the CBERA, such as petroleum, textiles and apparel, they have also helped ensure development in these sectors.

Moreover, Section 936 funds have advanced the original goals of the CBERA, especially at the level of the private sector. By fostering the use of foreign private capital in the development of a domestic private sector, the Caribbean loan program established a working partnership between Caribbean and foreign business communities. Since many of the Caribbean countries were working to stimulate their private sectors and undertake pri-

vatization schemes at this time, such a partnership has provided a tangible contribution to Caribbean economic growth. As the program has created jobs and fostered trade linkages throughout the region, it has secured a role for the private sector in bolstering social and political stability.

How the Program Has Worked

In short, the Section 936 Caribbean loan program encouraged private funds to be invested in certain Caribbean Basin countries. It accomplished this through a multi-tier process that depended upon the active participation of U.S. firms investing in Puerto Rico and upon the participation of the Puerto Rican government, the U.S. Treasury Department, and the Caribbean Basin countries themselves (see Chart 1 for a pictorial overview).

CBI Eligibility and the Tax Information Exchange Agreement (TIEA)

To be eligible to receive loans generated from the Section 936 credit, Caribbean Basin countries were required to satisfy two basic criteria.⁴¹ First, the country had to be designated as a beneficiary under the Caribbean Basin Economic Recovery Act.⁴² Of the 28 countries that the U.S. president may designate as CBERA beneficiaries, 24 countries have been so designated.⁴³ The four undesignated countries include Anguilla, Cayman Islands, Suriname, and Turks and Caicos Islands; Cuba is not included in the list of designated CBERA beneficiary countries. Second, the country was required to sign a Tax Information and Exchange Agreement (TIEA) with the United States.⁴⁴ To date, 10 CBI beneficiaries have signed the TIEAs: Barbados (1984), Jamaica (1986), Grenada (1987), Dominica (1988), Dominican Republic (1989), Trinidad and Tobago (1990), St. Lucia (1991), Costa Rica (1991), Honduras (1991), Guyana (1992).⁴⁵ Several others — including Haiti, El Salvador, Nicaragua, Guatemala, and Belize — have commenced discussions with the United States but have not yet signed

TIEAs and, therefore, have not been able to access this facility.⁴⁶

The TIEA is a mutual and reciprocal obligation to exchange information with the United States relating to the enforcement of tax laws.⁴⁷ In signing a TIEA, a country undertakes the following commitments:⁴⁸

1. Tax information can only be provided on a government to government level and cannot be withheld because of nationality or local nondisclosure laws,
2. Information must be in a form admissible to U.S. and host government courts, and
3. Governments must guarantee a method to require the reporting of tax information.

Caribbean governments that sign TIEAs agree to provide U.S. tax authorities with significant access to the tax filings and fiscal practices of their companies and citizens, and they may also obtain reciprocal access to U.S. tax records. In addition, ratification of a TIEA made a CBI beneficiary eligible to receive Section 936 funds while making U.S. individuals able to deduct expenses of attending conventions in Caribbean Basin countries that have signed a TIEA. Despite these mutual benefits, negotiations of TIEAs often meet with political objections or raise sensitive questions⁴⁹ about sovereignty in Caribbean countries.⁵⁰ One of the issues raised by Caribbean Basin governments is that TIEAs may inhibit the development of offshore banking centers in the Caribbean, particularly since the agreements require the elimination of many banking secrecy laws and instruments.⁵¹ As a result of the concerns, some Caribbean governments that signed the TIEAs believe they were doing so in a *quid pro quo* arrangement under which they would gain benefits, such as access to Section 936 funds.⁵²

The Private Sector Role: The Tax Credit Incentive

The Section 936 funds themselves were channeled to Caribbean Basin countries as a result of the incentive structure behind the overall Section 936 credit. Through the Section 936 mechanism, firms had an inducement to accumulate profits in Puerto Rico, while financial institutions were then permitted to apply those funds to Caribbean Basin investments.

The 936 Credit in Puerto Rico. As noted earlier, Section 936 has provided U.S. businesses two kinds of credits for their operations in Puerto Rico and other U.S. insular possessions, such as Guam, American Samoa, and the Virgin Islands. First, they received a tax credit on the income they earned from "active" business operations, such as manufacturing. Second, they received a credit on the income earned from qualified investments made with the profits of the active business operations. This income is more commonly known as "qualified possession source investment income" (QPSII). To qualify as a "936 firm," a company must have been able to demonstrate that 80 percent of its income over a three-year period was derived from operations in Puerto Rico or other U.S. possessions and that at least 75 percent of its income was derived from active business operations, as opposed to passive investments.

In establishing a two-part credit on federal income taxes for companies doing business in Puerto Rico, Congress created a dual incentive: first, to attract firms to Puerto Rico to create jobs and, second, to induce them to keep their profits there to establish a source of liquidity.⁵³ In general, Section 936 has been credited with supporting one in 10 jobs in Puerto Rico as well as over \$15 billion in financial assets, which are available for public sector, commercial, and individual needs.⁵⁴

Section 936 has been modified a number of times. In 1993, the U.S. Congress and administration took measures to strengthen the linkage between tax benefits and employ-

ment creation in Puerto Rico. As part of the Omnibus Budget Reconciliation Act of 1993, the credit was subjected to a series of limitations to encourage firms to calculate the amount of active business credit based on the level of wages they pay — not on the income they earn. No changes were made at that time to the QPSII element of the credit, although both the House of Representatives and the Senate had explored proposals to limit the QPSII tax credit.⁵⁵

Nevertheless, several analysts suggested that changes in the overall credit during 1993 did affect QPSII by altering the incentive through which firms generated funds for QPSII accounts. Some predicted as much as a 35 to 40 percent drop by 1998 of available QPSII funds.⁵⁶ They noted that the incentive under the pre-1993 scheme was directed at making profits, while the incentive under the 1993 plan was modified to promote the paying of wages. This change removed the tax incentive on making a profit, which was the foundation for the QPSII funds. Without that incentive working properly, companies were not rewarded for maintaining active contributions to their QPSII accounts.

Most recently, in the Small Business Job Protection Act of 1996, Congress repealed the Section 936 credit for taxable years beginning after December 31, 1995.⁵⁷ Although Congress established a 10-year grandfather period for existing users of the active portion of the credit, the value of the credit is phased out completely over the 10-year period. As noted above, the element of the credit providing for QPSII income was not included in the phase-out period. Furthermore, Congress codified the provisions governing the grandfather period and the phase-out period in a new section 30A of the Internal Revenue Code.⁵⁸

The 936 Credit in the Caribbean. While the credit has remained targeted on Puerto Rico, the Tax Reform Act of 1986 changed the QPSII provision to permit the use of QPSII funds to finance qualifying projects — either active business assets or development projects — in eligible Caribbean Basin countries. The

1986 Act and a subsequent modification made by the CBERA of 1990 require the Puerto Rican government to “take such steps as may be necessary to ensure that at least \$100 million” of QPSII income is used in new CBI projects each year.

Through these changes, Congress effectively created a “window” for Caribbean financing, using funds created through this credit. These modifications established a facility — the Section 936 Caribbean loan program — to allow banks and other lending institutions to use the invested profits of Section 936 companies to finance Caribbean economic development. At the same time, these modifications created a way for other companies, both U.S. and foreign, to obtain low-cost financing for their Caribbean projects. This lending program was possible because the tax-free status of the underlying funds allowed banks and other financial intermediaries to charge lower interest rates than would otherwise have been available on the market for Caribbean projects. The Puerto Rican State Department estimated that Section 936 loans were made available at 1 to 2 percentage points below commercial rates, resulting in a 20-percent savings of financing costs.⁵⁹ Under this system, U.S. firms were still able to make a healthy profit while investors in Caribbean countries could gain access to capital at affordable rates.⁶⁰

A basic model that emerged allowed firms to deposit their funds in Puerto Rican commercial or merchant banks, which could then loan those funds to investors or developers in the Caribbean. In addition, several development institutions, including the Government Development Bank of Puerto Rico (GDB), the Puerto Rico Economic Development Bank, and the Commonwealth Development Corporation Puerto Rico, Inc. (CDCPR), were empowered to make Section 936 loans available to eligible borrowers.

A number of financing schemes, supported to varying degrees by the public sector, have been developed to help both investors and borrowers maximize their use of the 936 funds. In 1990, the Puerto Rican government

chartered the Caribbean Basin Financing Authority (CARIFA) to finance medium- and large-sized projects in eligible CBI countries. CARIFA, a public corporation that is guaranteed by the Puerto Rican government, can issue bonds or provide loan guarantees for qualified projects. Since 1990, CARIFA bond issues have financed over \$650 million in investment in 12 projects in seven of the eligible Caribbean countries. Jamaica, Trinidad and Tobago, and Honduras have been the largest beneficiaries of CARIFA bond financing.⁶¹

In contrast, a second financing scheme focused on small enterprises. In 1991, a group of 28 U.S. companies operating in Puerto Rico under Section 936 established the Caribbean Basin Partners for Progress, Ltd. (CBPP) to provide loans to small- and medium-sized projects (of up to \$10 million per project). Since its inception, the CBPP has been one of the major success stories of the Caribbean loan program, primarily by channeling funds to a large number of small projects throughout the region. During the last four years, CBPP has been involved in roughly half of all Section 936 loans, making a total of 63 loans with an average loan amount of \$556,538.⁶²

A third financing scheme through which Section 936 funds have been used to support economic development in the Caribbean Basin is an indirect financing mechanism known as the "twin-plant" program. Under this program, which has been encouraged both by the Puerto Rican government and the CBERA,⁶³ a company was able to use Section 936 funds to establish two plants — one plant in Puerto Rico and one plant in a partner Caribbean country — to produce a single product. The Puerto Rican government has encouraged such production sharing ventures as a way of taking advantage of complementary Puerto Rican and Caribbean technology and skills. In general, because Caribbean labor rates are cheaper than in Puerto Rico, the labor-intensive phases of joint production ventures tend to be located in the Caribbean partner countries.⁶⁴ The program differs from the rest of the Caribbean loan program in one critical way. The partner CBI country was not

required to be a signatory to the TIEA, primarily because the intention of the twin-plant mechanism was to facilitate investment in Puerto Rico. As a result, the twin-plant initiative has permitted Section 936 funds to be used to support economic development, albeit at extremely low levels, in four non-TIEA countries. In total, complementary production with Puerto Rico has played a part in nearly one-third of all Section 936 loan projects.⁶⁵

Puerto Rican and U.S. Government Regulations

The other elements of the Section 936 partnership included the Puerto Rican government and the U.S. Treasury Department, which established the regulations and guidelines and in some cases made the approvals for financing using Section 936 funds. Ironically, as the program emerged into a private-to-private financing mechanism, the involvement of the Puerto Rican and U.S. governments often inadvertently complicated the process.

The Treasury Department's role consisted of establishing parameters for the program and taking the lead in negotiating and implementing the Tax Information and Exchange Agreements. The Treasury Department issued a number of regulations governing the basic Section 936 credit and the use of funds under the Caribbean loan program. In general, Treasury regulations define qualified projects, in which Section 936 funds may be invested, as "lawful industrial or commercial activity that is conducted as an active trade or business in a qualified Caribbean Basin country." Additional regulations outline due diligence procedures, define eligible financial institutions, and establish financing and application requirements. By way of example, a recent Treasury regulation on the Section 936 Caribbean loan program, which was issued on May 13, 1992, specified the following general guidelines and eligibility criteria for development projects, including privatizations:⁶⁶

1. Acquisition of real property is eligible only if acquired in connection with a government-backed development project or USAID or OPIC-approved privatization.
2. Section 936 funds can be used for construction, rehabilitation, improvement, or upgrading of real property.
3. Privatizations are eligible for 936 financing as long as the government owned the asset for a three-year period prior to privatization and had completely divested itself of all ownership during the privatization.
4. Projects must have a neutral or positive impact on the Puerto Rican economy and a positive impact in the CBERA country.
5. The borrower must take title of property being financed and must use the property predominantly in a CBERA country.
6. Section 936 funds can be used for following development projects and expenditures:
 - a. transportation, communication, and sewage facilities;
 - b. industrial parks (including power plants);
 - c. oil and gas exploration;
 - d. purchase of machinery and farming equipment;
 - e. tourism development; and
 - f. incidental expenditures (including up to 3.5 percent of cost of arranging financing).

In addition, the Department of Treasury and the Office of Management and Budget (OMB) have issued guidance from time to time as to how Section 936 funds can be used in connection with other U.S. government financing mechanisms and guarantees, including the Overseas Private Investment Corporation (OPIC). Since January 1993, the OMB has prohibited the use of U.S. government guarantees to finance Section 936 funds.

This decision was prompted by a concern that U.S. taxpayer guarantees for tax-exempt funds amount to a "double dip" at the taxpayers' expense.⁶⁷ Many borrowers of Section 936 funds decried this decision, largely because the lack of U.S. government guarantees made financing difficult to obtain for small to medium projects.⁶⁸

For its part, the Puerto Rican government, using the authority in Section 936(4), created a Caribbean Development Program through which it promulgated regulations governing the application for and disbursement of such funds to qualified Caribbean Basin projects. In general, the Puerto Rican government exercised this authority to maximize the way in which Section 936 funds would benefit Puerto Rico. Although Section 936(4)(d) mandated the Puerto Rican government to channel at least \$100 million to the Caribbean annually, the Puerto Rican government had considerable flexibility in determining how those funds were to be channeled. For example, throughout 1993, in response to changes proposed to Section 936 by Congress and the Clinton administration, the Puerto Rican government issued a series of regulations to restrict and modify the use of Section 936 funds for Caribbean countries. Initially, out of concern that Section 936 might be terminated or significantly weakened, the Puerto Rican government froze new applications on May 19, 1993, for Section 936 loans to the Caribbean in excess of \$5 million.

The purpose of this step was twofold. First, it provided a breaking mechanism to prevent large projects from exhausting available 936 resources if the credit were terminated. Second, it sent a political signal to Caribbean heads of state to lobby for the preservation of Section 936 QPSII credits. In fact, Puerto Rican Governor Rossello pledged to double the \$200 million per year lending commitment if Caribbean countries lobbied to save Section 936.⁶⁹ Many Caribbean Basin countries lobbied to preserve Section 936, and Rossello eventually made good on this pledge. He announced a doubling of the commitment several months after President

Clinton signed into law a compromise preserving much of the Section 936 credit as part of the 1993 Omnibus Balanced Budget Act.⁷⁰

In addition, the Rossello administration issued a new set of regulations in 1993 that established lending limits on many 936 loans to the Caribbean. Under the new guidelines, which also streamlined the application process, new loans were subject to the following limitations:⁷¹

1. A \$75 million cap on new projects.
2. A prohibition on financing of tourism projects that fail to meet one of the following three criteria:
 - a. the project is under \$1 million,
 - b. the project is certified by the Puerto Rican government as not competing with the Puerto Rican tourism industry, or
 - c. the investor develops a tourism project in Puerto Rico equivalent to 150 percent of the cost of the proposed Caribbean tourism project. (This criteria was dubbed the "twin bed" policy.)

At the time, both limitations came under sharp criticism from Caribbean leaders and businesses.⁷² Some felt that the per project cap of \$75 million would kill a number of mega-projects that were already in the pipeline or force those projects to seek co-financing elsewhere. Although funding for large-scale projects remained relatively constant through 1995, it is possible that a number of large deals were never consummated because of the cap. Since the restrictions took effect, only three large-scale projects were funded: a \$101 million power project in Jamaica and two \$75 million oil and gas projects in Trinidad and Tobago. Before the restrictions, however, four projects were funded at or above the \$75 million level.⁷³

Other criticisms were leveled at the tourism restrictions, including the so-called "twin bed" policy, which required the 150 percent co-investment in Puerto Rico. Whether it was intended to stimulate such co-

investment or discourage tourism development in the Caribbean, the new policy effectively killed Section 936 funding for large-scale resort ventures and may have actually acted as a catalyst for small-scale tourism projects. From 1988 until 1993, when the regulations were implemented, five of the nine tourism projects funded with 936 loans exceeded the \$1 million threshold. During the next two years, although the overall number of tourism projects increased to 12, only two projects exceeded \$1 million.⁷⁴

Benefits of the Program to the United States and the Caribbean⁷⁵

By all accounts, the Section 936 Caribbean loan program has been an overall success. Through 1995, the program supported 178 projects in the 10 TIEA countries. On loans of \$1.28 billion, the program has generated an estimated \$2.08 billion in investment and nearly 37,000 jobs. This figure is slightly higher when the non-TIEA countries, through the twin-plant program, are factored into the equation.⁷⁶ Table 2 provides further information on the use of Section 936 funds in TIEA countries. Table 3 reprints the Puerto Rican State Department's list (as of December 29, 1995) of CBI projects financed with Section 936 loans.

Since it was made available to the Caribbean, the Caribbean loan program has made a significant contribution to the economic development of the entire Caribbean Basin and to the United States by providing financing to facilitate increased trade and investment. Overall, the impact of this provision has been considerable since it has resulted in increased U.S.-Caribbean trade and investment and has promoted economic growth, employment, and more effective cooperation throughout the region. There are three major ways in which the Caribbean loan program has had positive tangible impacts on the region: It has 1) expanded U.S.-Caribbean trade, 2) promoted greater development of the Caribbean, and 3) promoted greater regional stability.

Expanded U.S.-Caribbean Trade

The Caribbean loan program provided a source of capital to allow businesses to take advantage of CBERA trade opportunities. In many ways, 936 funds have been the fuel of the CBI engine. The result has been an unprecedented expansion of trade between the Caribbean and the United States with the following results:⁷⁷

1. Currently, the U.S.-Caribbean commercial relationship supports more than 300,000 jobs in the United States and tens of thousands more throughout the Caribbean. During the past decade, the Caribbean Basin relationship has created roughly 18,000 jobs per year in the United States. (See Table 4 for more information on employment generation in the CBI.)
2. The Caribbean Basin is now the tenth-largest export market for the United States, surpassing countries such as China and Singapore.
3. The Caribbean Basin is one of the few regions in the world where U.S. exporters maintain trade surpluses (see Table 5 for more information). In 1995, the tenth consecutive year for which the United States recorded a trade surplus with the Caribbean Basin, that surplus equaled \$2.6 billion.
4. In 1995, U.S. exports to the region surpassed \$15.3 billion, resulting in a 160 percent increase in U.S. exports during a 10-year period. Although the benefits have been concentrated in Florida and other coastal areas, every state in the union has benefited from this relationship.
5. In 1995, U.S. imports from the region reached \$12.6 billion, completing a 10-year growth rate of nearly 100 percent.

This beneficial trade-based relationship has flourished primarily because of natural complementarities that exist between the United States and the Caribbean. Many Caribbean economies do not have the capacity to pro-

duce capital goods or high-tech equipment, while the United States finds itself in a less favorable position to manufacture labor-intensive products that can compete on the world market. To tap the resources of both the United States and the Caribbean, many firms have set up production facilities in both regions. As a result, there has emerged a substantial trade interdependence between the 24 CBERA nations and the United States. In practical terms, approximately 60 cents of each dollar spent by investors or consumers in the Caribbean Basin is ultimately used to purchase U.S. goods and services. In comparison, only about 10 cents of each dollar spent in Asia is spent on U.S. products.⁷⁸

Linking the regional trade figures to the Caribbean loan program provides clear evidence of the impact of the program on the United States. Through 1995, the program generated more than \$2 billion of investments in the CBI region. Since 60 cents of each of those investment dollars has found its way back to the United States, Section 936 funds have generated about \$1.2 billion in U.S. exports over the last eight years. Using the Commerce Department figure that each \$1 billion in new exports generates an additional 20,000 U.S. jobs,⁷⁹ this level of exports has generated about 24,000 U.S. jobs.

Aside from simply generating stronger trade between the United States and the Caribbean, resulting in more jobs in both regions, the Caribbean loan program has helped bring about a number of specific benefits that have contributed to the overall development of the Caribbean Basin region.

Promoted Caribbean Development

As the Caribbean economies undergo major economic changes and adopt export-oriented growth policies led by the private sector, their need for investment funds becomes acute. Countries in the Caribbean have been able to draw on the pool of capital from Section 936 funds to promote growth through the expansion of private investment and to finance critical public sector develop-

ment projects. Section 936 financing has helped strengthen the economies of each eligible Caribbean Basin country. Section 936 funds have financed investments that have been critical in the creation of jobs, the installation of productive capacity, and the production of goods and services. The specific ways in which 936 funds contributed to Caribbean development and thereby increased U.S.-Caribbean trade are through a) increased investment, b) improved infrastructure, c) privatized public enterprises, d) increased foreign exchange earnings, e) expanded food supply, and f) increased employment. These contributions to development and increased U.S.-Caribbean trade are discussed below.

Increased Investment. During the past decade, many Caribbean governments have implemented comprehensive economic reform programs that involved the removal of barriers and impediments to the operation of the market. These changes resulted in the creation of economies oriented toward the private sector that depend upon diverse sources of investment to accelerate and sustain economic growth. Section 936 funds have been important in funding public sector development projects, including privatizations and private sector investments since 1988. These funds have been particularly valuable because they were available in foreign exchange and, therefore, alleviated the foreign exchange constraints faced by many Caribbean nations. Table 6 shows that 936 funds were the third-largest source of capital inflows in TIEA signatory countries in 1993, accounting for nearly 16 percent of total inflows during that year.

These funds took on an added importance because U.S. official development assistance and economic support to the Caribbean Basin have declined precipitously since the mid-1980s. Section 936 funds have helped fill this gap and, in so doing, have supported vital development efforts. As noted before, Table 1 shows how aid to Caribbean Basin countries has declined by 56.89 percent from 1984 to 1994. This funding drop-off is even more pronounced for the TIEA countries, which have

experienced a 72.52 percent decline in aid during the same period.

Improved Infrastructure. The resources provided by 936 funds have made substantial contributions to rehabilitating and upgrading infrastructure, enhancing the productivity of private investments, and improving export competitiveness. For example, the trans-Caribbean telephone cable system and a series of modernization projects within the Barbados and Grenada telephone companies were financed through Section 936 funds. Such activities strengthen the region's communication links and provide the countries with state-of-the-art service and equipment, thus stimulating more effective commercial discourse. Moreover, Air Jamaica received \$51 million in 936 funds to acquire two aircraft that are now used for high density flights between Jamaica and the United States. Trinidad and Tobago has seen much of its loan portfolio of 936 funds used on infrastructure for natural gas exploration and petroleum-related construction to help it develop its abundant fossil fuel resources.

Privatized Public Enterprises. Money from the 936 loan facility has helped to fund privatization programs, which are key to the long-term health of the private sector and which reduce the drain of scarce fiscal resources from government budgets. By supporting privatization schemes, Section 936 funds have facilitated reforms to reduce the presence of government in the economy and stimulate the activity of public enterprise. Privatizations have been especially important in tourism development. Hotel privatization programs, such as the Wyndham Rose Hall in Jamaica, led to more efficient management, expanded employment, and significant increases in revenue generated by that property.

Increased Foreign Exchange Earnings. The 936 funds have provided foreign exchange inflows that have helped stabilize regional exchange rates while cutting foreign exchange costs of needed external financing. Moreover, many 936-financed projects have generated additional foreign exchange earnings by

expanding export capacity through improved efficiency in the tourism sector, such as the refurbishing of Mallards Beach and Americana Hotels in Jamaica. In traditional sectors, such as the reorganization of the wood and sugar processing industries in Honduras; or in assembly industries, such as textile and apparel manufacture in Costa Rica and the Dominican Republic.

Expanded Food Supply. Section 936 funds have been used for small-holder farms as well as large estates and have supported investment in agricultural and food processing. In particular, the agricultural sector has been able to utilize these funds to expand its productive capacity, such as the expansion and modernization of broiler meat and hatching egg facilities in Costa Rica and the establishment of a cardboard box factory in Dominica to supply that country's banana industry and manufacturing sector. As these industries develop, Caribbean Basin countries become more self-sufficient in food products while producing higher value-added goods.

Increased Employment. As noted above, the projects financed with 936 funds both in the public and private sector have directly, and through their multiplier effects, created thousands of new jobs across a range of skill categories. Employment creation for many Caribbean Basin countries, some of which have unemployment levels of 20 to 30 percent, has a powerful symbolic and tangible effect on national development.

Promoted Regional Stability

The Section 936 Caribbean lending facility served as a suitable policy mechanism to enhance social and political stability and bolster democratic traditions and institutions throughout the region. In fact, this view was embraced as one of the driving rationales for the CBERA program and for the extension of the Caribbean loan program to the CBERA. In the findings of the Caribbean Basin Economic Recovery Expansion Act of 1990, which set the \$100 million floor for Caribbean investment using Section 936 funds, the U.S. Congress reaffirmed that "a stable political

and economic climate in the Caribbean region is necessary for the development of the countries in that region and for the security and economic interests of the United States."⁸⁰

Specifically, by fostering employment and economic opportunity in Caribbean countries, the Caribbean loan program played a role in discouraging migration from the Caribbean Basin to the United States. From 1981 to 1988, emigration from Caribbean Basin countries to the United States represented 47 percent of all emigration in the Western Hemisphere, more than three times the region's share of the hemisphere's population.⁸¹ In the 1990s, emigration (for the United States, immigration) problems continued to be an important factor in U.S.-Caribbean relations, as the United States had to deal with twin immigration crises from Haiti and Cuba, two of the most economically disadvantaged countries in the region.

Economic stability also strengthens the ability of Caribbean countries to fight narcotics and drug trafficking. While counter-narcotics programs should focus on accepted strategies — destruction of crops and processing facilities, interdiction efforts, public education, and the criminalization of money laundering — more attention and resources must also be devoted to providing jobs and economic activity as an alternative to involvement in drug trafficking.⁸² In Jamaica, Section 936 funds have been particularly effective at targeting low-income residents, both in providing employment opportunities and in improving their access to social services. For example, the construction of 750 low-cost prefabricated housing units, which were manufactured in Puerto Rico and assembled and installed in Jamaica, added significantly to the low-income housing stock while creating local jobs.

On a related note, the Caribbean loan program, by encouraging the signing of Tax Information and Exchange Agreements, directly supported efforts to fight drug traffickers by discouraging money laundering and tax evasion. It also encouraged Caribbean govern-

ments to adopt good governance and transparency reforms, furthering a key U.S. policy goal in the region. As Caribbean countries develop cooperative relationships with the United States and establish a precedent for the sharing of information on tax cases, they will gain confidence and develop mechanisms needed to confront international drug traffickers and money launderers. By taking such actions, Caribbean countries will also be more likely to resist the kinds of narco-corruption that have plagued many poorer countries.

Recommendations and Outlook

Clearly, the loss of the Section 936 Caribbean loan facility will create a large gap in Caribbean financing needs, undermining a number of policy objectives in the overall U.S.-Caribbean economic relationship.⁸³ Although the U.S. Congress has now enacted a law to phase out Section 936 over ten years and to eliminate immediately the credit element that finances Caribbean development, it can still develop a policy to compensate for the loss of this program. In fact, Congress has left the door open for such a possibility by declaring in the report accompanying the Section 936 repeal language that “The Conferees continue to support efforts furthering stable commercial and economic relations in that region.”⁸⁴ Congress and the current administration can take several important steps in this regard.

Reestablish a Tax-Based Caribbean Financing Facility Independent of Any Residual Puerto Rico Tax Credits

As it was financed through the Puerto Rican tax credit and was administered by the Puerto Rican government, the Section 936 Caribbean loan program was often seen primarily as a “Puerto Rican issue.” Accordingly, it was often lost in the debate over Puerto Rican economic development or political affiliation with the United States. Members of the U.S. Congress and the Clinton administration typically viewed Section 936 and all its ele-

ments by assessing the credit’s impact on Puerto Rico. As long as the Puerto Rican government was willing to defend Section 936, the entire credit program had a good chance for survival. When the Puerto Rican government decided otherwise, some members of Congress chose to adopt the Puerto Rican government’s recommended changes, a politically expedient alternative.

While it is important to recognize and maintain Puerto Rican-Caribbean economic and trade links, that relationship should not serve as the guardian for the entire U.S.-Caribbean relationship. The program evolved as an offshoot of a minor Puerto Rico-based lending facility to become a major source of financing for the Caribbean region. Any effort to revive the Section 936 Caribbean loan facility should recognize it as a Caribbean Basin institution. Not only will such a modification distance the Caribbean loan program from Puerto Rican politics in Washington, D.C., but also it will insulate the Caribbean from the public debate over the impact of pharmaceutical companies and the wage credit in Puerto Rico.

A stronger Caribbean identity could be fostered by shifting the QPSII provisions (which provided the incentive behind the Caribbean lending program) to another location in the U.S. tax code, severing the link with the Puerto Rican tax credit. As noted, the 10-year phase out of the Section 936 credit is effected by repealing Section 936 and creating a new Section 30A Puerto Rican Economic Activity Credit. While this “new” credit is expected to be discontinued after ten years, it serves to remove the Puerto Rican credit from the Section 936 nomenclature. A similar device could be employed in the resurrection of the QPSII provisions, through the creation of a “Section 30B Caribbean Basin Enterprise Facility” to emphasize the Caribbean nature of the program. In this way, individuals, whether they are business officials or tax legislators in Congress, will develop a better understanding of and appreciation for this program’s impact on the Caribbean.

Maintain Caribbean-Puerto Rican Economic Linkages

At the same time, the Caribbean-Puerto Rican trade partnership should be encouraged and strengthened. With exports of \$811.1 million to the Caribbean during 1995, Puerto Rico remains one of the largest suppliers of goods and services to the Caribbean. In fact, were Puerto Rico a state, it would be the fifth-largest exporting state to the Caribbean, after Florida, Texas, Louisiana, and North Carolina.⁸⁵ One way to accomplish strong Caribbean-Puerto Rican links would be through the retention of the twin-plant program. Although such a program is targeted at Puerto Rican economic growth, the twin-plant relationship is an important element of the Caribbean-Puerto Rican trade partnership. Combining Puerto Rican technology and skills with Caribbean labor would generate employment in both Puerto Rico and the Caribbean and enable Puerto Rican industries to manufacture more competitive products for the U.S. and international markets. Even though the current credit that supports the twin-plant program has been repealed, such twin plants are still encouraged by the CBERA, which permits the use of Puerto Rican value-added to count toward CBI rule-of-origin requirements.⁸⁶ Moreover, the Puerto Rican government could continue to support twin plants through a Puerto Rican government tax credit.

Seek Alternative Administration of the Section 936 Caribbean Loan Program

A problem related to Section 936 was that Puerto Rican authorities did not always administer it according to the best interests of the Caribbean Basin. To be fair, the Rossello administration fought to support the Section 936 Caribbean loan program, most recently by recommending the retention of a Caribbean loan facility as part of an overhaul of Section 936;⁸⁷ it also doubled the size of the Caribbean lending program. However, the 1993 near-cessation of lending operations and the subsequent imposition of caps and lending prohibitions suggested that the Caribbean

lending program was subordinate to Puerto Rican economic goals. Some observers questioned whether the Puerto Rican government saw the Caribbean lending program as an inconvenience.⁸⁸

If the program is to be continued as a viable mechanism for the Caribbean, it must be administered so that Caribbean interests are a priority. The U.S. Congress and Clinton administration should explore moving the administration of the Caribbean loan program to an established multilateral financial institution, such as the Inter-American Development Bank. Alternatively, to reinforce the private sector nature of the facility, the program could be administered by a private entity or a consortium of banks. The Caribbean Basin Partners for Progress program provides a good precedent for such an operation.

Broaden the Participation of Other CBI Countries

Any efforts to revive this Caribbean loan program should also involve efforts to encourage other CBI countries to become beneficiaries of the program. Broadening the participation will strengthen the CBI and further U.S. goals of economic development and political stability in the region. Putting the program on a sound, permanent basis will likely reduce much of the uncertainty that has been associated with it. Such an action would encourage countries to complete negotiations on the TIEA, while signaling those who have already negotiated an agreement that the underlying diplomatic obligations remain sound.

Diversify Caribbean Financing Sources

A long-term goal must also involve the diversification of Caribbean Basin financing sources. The U.S. Congress's ability to eliminate nearly 20 percent of private sector financing for 10 Caribbean Basin countries underscores the need for broader and more varied sources of investment capital. While a revived or reconstituted Caribbean loan program is important, tax credit-based programs

can easily be amended by U.S. congressional action and, therefore, are not very stable. The United States can play a role in helping to diversify Caribbean funding vehicles by supporting the creation of equity funds through such entities as OPIC and the Trade and Development Agency. The United States and other developed countries can also advance these efforts through their continued support of multilateral financing facilities, such as the Multilateral Investment Fund (MIF), the InterAmerican Investment Corporation, and the International Financial Corporation (IFC). Similarly, care must be taken to ensure that aid programs in the region can be restructured to accommodate this financing gap.

Strengthen Collateral U.S.-Caribbean Trade Relationship

It is imperative that any effort to rebuild Caribbean Basin financing mechanisms be undertaken only in the context of broader U.S.-Caribbean relations.⁸⁹ Currently, the Clinton administration and the Congress appear unable to take a holistic approach to the range of Caribbean issues and are developing U.S.-Caribbean policy in a piecemeal approach. Ideally, a plan to salvage the Caribbean loan program would be harmonious with other policies to improve Caribbean Basin products' access to the U.S. market vis-à-vis NAFTA⁹⁰ or with an agreement that would preserve Caribbean market share in the European Union's (EU) banana market.⁹¹

Conclusion

Ironically, President Clinton approved the repeal of the Section 936 Caribbean loan program exactly six years after President Bush approved the law establishing the \$100 million per year floor for the Section 936 Caribbean loan program. By allowing such an important Caribbean program to be dismantled as a result of an unrelated budget debate, the U.S. government has inadvertently signaled diminished U.S. interest in the region.

U.S. and Caribbean interests would be better served by looking for ways to strengthen healthy U.S.-Caribbean ties. U.S. and Caribbean policymakers should work toward reversing this most recent action so that a more effective Caribbean loan program can be established. Moreover, business leaders throughout the region should develop alternative financing sources to broaden the funding base to support economic development in all Caribbean Basin countries. Finally, the United States should take a fresh look at Caribbean trade initiatives to bolster the U.S.-Caribbean relationship in order to respond to recent changes in the international trade regime.

The U.S. Congress has long recognized the United States' ongoing interest in promoting stable economic relations with the Caribbean. The Caribbean Section 936 lending program was a prime manifestation of that interest, as it operated according to the original intentions of the U.S. Congress. By making a significant contribution to financing investments in the Caribbean, the program stimulated economic development, expanded U.S.-Caribbean trade, and supported regional stability and cooperation. Ensuring continued access to such financial resources for Caribbean countries is vital, not only in sustaining Caribbean prosperity but also in maintaining a sound and stable U.S.-Caribbean partnership.

NOTES

1. See Section 28 U.S.C. 936(d)(4) added by § 1231(c) of PL 99-514, October 22, 1986.
2. See Section 1601 of Conference Report (104-737) to accompany the Small Business Job Protection Act of 1996 (HR 3448), Government Printing Office, Washington, D.C., August 1996.
3. According to Senator Daniel Patrick Moynihan (D-NY), the Section 936 credit was originally enacted to "encourage American investment in the Philippines." Administration's Tax Proposals, Hearings Before the Senate Finance Committee (S. Hrg 103-199), U.S. Senate, Washington, D.C., Spring 1993. The emphasis of the credit, which is derived from a provision in the Revenue Act of 1921, has now evolved so that it primarily benefits Puerto Rico, and, to a lesser extent, other U.S. insular possessions of Guam, the U.S. Virgin Islands, and Samoa. *Puerto Rico and the Section 936 Tax Credit*. (GAO/GGD-93-109), General Accounting Office, Washington, D.C., June 1993.
4. During Senate Finance Committee hearings on the Section 936 proposals in the Spring of 1993, 15 of 18 witnesses who testified on the Section 936 program focused their remarks on the impact of Section 936 on Puerto Rico. The other three — including two Caribbean ambassadors — spoke primarily of the impact on the Caribbean. Administration Tax Proposals, Hearings Before the Senate Finance Committee (S. Hrg 103-199), U.S. Senate, Washington, D.C., Spring 1993.
5. Testimony of Samuel Sessions, Deputy Assistant Secretary of Treasury, Administration Tax Proposals, Hearings Before the Senate Finance Committee (S. Hrg 103-199), U.S. Senate, Washington, D.C., Spring 1993.
6. In 1993, both the Clinton administration and the administration of Puerto Rican Governor Pedro Rossello advanced proposals to create a wage-based credit in the Section 936 tax credit. In 1995 and 1996, as part of the continuing debate on Section 936, both the Clinton and Rossello administrations advanced further proposals to strengthen the wage credit element of the credit.
7. *Caribbean Update* reports that the President of the Popular Democratic Party criticized Governor Rossello for "encouraging the elimination by the U.S. Congress of Section 936." "Special Focus on Puerto Rico," *Caribbean Update*, Vol. 12, No 8, September 1996.
8. Testimony of Carlos Romero Barcelo, Resident Commissioner, Administration Tax Proposals, Hearings Before the Senate Finance Committee (S. Hrg 103-199), U.S. Senate, Washington, D.C., Spring 1993.
9. Testimony of Victoria Muñoz, President, Popular Democratic Party, Administration Tax Proposals, Hearings Before the Senate Finance Committee (S. Hrg 103-199), U.S. Senate, Washington, D.C., Spring 1993.
10. Statement of Arturo Carrión, on behalf of Puerto Rico 936 Private Sector Coalition, and statement of Puerto Rico Manufacturer's Association. Administration Tax Proposals, Hearings Before the Senate Finance Committee (S. Hrg 103-199), U.S. Senate, Washington, D.C., Spring 1993.
11. Statement of Amalgamated Clothing and Textile Workers Union and statement of Richard Leonard of the Oil, Chemical, and Atomic Workers International Union, AFL-CIO, Administration Tax Proposals, Hearings Before the Senate Finance Committee (S. Hrg 103-199), U.S. Senate, Washington, D.C., Spring 1993.
12. Such budget laws have hindered passage of other key legislation, including recent trade bills, by requiring legislators to build support for an offset package as well as the original legislation. See Stephen Lamar, "GATT: Looking at the Benefits," *The Washington Times*, June 24, 1994.
13. Joint Committee on Taxation Staff Estimates of Provisions in Conference Report to HR 2264 and Conference Report (103-213) to accompany The Omnibus Budget Reconciliation Act of 1993 (HR 2264), Government Printing Office, Washington, D.C., August 4, 1993.
14. Conference Report (104-350) for the Balanced Budget Act of 1995 (HR 2491), Government Printing Office, Washington, D.C., November 1995.
15. Conference Report (104-737) to accompany the Small Business Job Protection Act of 1996 (HR 3448).
16. See PL 104-188. 110 Stat. 1755.
17. See Section 1601 of Conference Report (104-737) to accompany the Small Business Job Protection Act of 1996 (HR 3448), Government Printing Office, Washington, D.C., August 1996, 76-83.
18. Moody's investor services, as reported by *Caribbean Update*, notes that "...U.S. corporations are expected to accelerate the repatriation of their profits." "Special Focus on Puerto Rico," *Caribbean Update*, Vol. 12, No 8, September 1996.
19. Conference Report (104-737) to accompany the Small Business Job Protection Act of 1996 (HR 3448), August 1, 1996, 292.
20. President Ronald Reagan, "Address Before the Permanent Council of the Organization of American

States," *Weekly Compilation of Presidential Documents: Administration of Ronald Reagan* Vol. 18, No. 8 (Mar 1, 1982) 217-223.

21. U.S. Department of State, "Background on the Caribbean Basin Initiative," Special Report No. 97, March 1982.

22. See Section 19 U.S.C. 2701 *et seq.*, as originally enacted by PL 98-67, Title II, August 5, 1983. The original expiration date of September 30, 1995, was deleted to make the CBI program permanent in PL 101-382, the Caribbean Basin Economic Recovery Expansion Act of 1990, enacted on August 20, 1990.

23. See Section 213 of the CBERA. PL 98-67, codified at 19 U.S.C. 2701.

24. See also Section 423 of the Tax Reform Act of 1986 (PL 99-514), codified at 19 U.S.C. 2703.

25. See Section 214 of the CBERA, codified at 19 U.S.C. 2701.

26. See Section 224 of the Caribbean Basin Economic Recovery Expansion Act of 1990 (PL 101-382).

27. Under the Enterprise for the Americas Initiative (EAI) — Part IV of the Foreign Assistance Act of 1961 (PL 87-195), which was added by Section 602(a) of the Jobs Through Exports Act of 1992 (PL 102-549) — the United States can reduce the bilateral debt owed by eligible Latin American and Caribbean countries. To date, two CBERA countries — Jamaica and El Salvador — have participated in the program to reduce almost \$750 million worth of bilateral AID and PL 480 debt. See *The Operation of the Enterprise for the Americas Facility*. Report to Congress, Department of Treasury, Washington, D.C., May 1996.

28. The Multilateral Investment Fund (MIF) was established to channel funds to help stimulate small enterprise and private sector development in Latin America and the Caribbean. In 1991, the United States pledged \$500 million over five years to the MIF. As of FY 1996, however, U.S. contributions totaled only \$293.8 million. Jamaica was the first country to receive financing through the MIF. See *International Financial Institutions: U.S. Leadership Making a Difference — FY 1997 Budget Request*. Department of Treasury, Washington, D.C., 1996.

29. See Section 222 of the CBERA, which amends Section 274 of the Internal Revenue Code.

30. See Sections 232 and 233 of CBEREA of 1990. Codified at 19 U.S.C. 2701.

31. Stephen A. Quick, "The International Economy and the Caribbean: The 1990s and Beyond" *The Caribbean Basin: Economic and Security Issues Joint*

Economic Committee Print (S. Print 102-110), Government Printing Office, Washington, D.C., January 1993.

32. The U.S. International Trade Commission *Annual Report on the Impact of the Caribbean Basin Economic Recovery Act on U.S. Industries and Consumers* (Pub. No. 2225) states that "overall, levels of new investment in beneficiary countries in the [CBI] region remain disappointingly low." As quoted in Stephen A. Quick, "The International Economy and the Caribbean: The 1990s and Beyond," *The Caribbean Basin: Economic and Security Issues Joint Economic Committee Print* (S. Print 102-110), Government Printing Office, Washington, D.C., January 1993.

33. Vladimir N. Pregelj, "U.S. Foreign Trade and Investment Policy in the Caribbean Basin Region," *The Caribbean Basin Economic and Security Issues. Joint Economic Committee Print* (S. Print. 102-110), Government Printing Office, Washington, D.C., 1993, 332.

34. *Caribbean Basin Economic Recovery Act: Impact on U.S. Industries and Consumers: Ninth Report 1994*, (Pub. No. 2927). U.S. International Trade Commission, September 1994, 10.

35. *Caribbean Basin Economic Recovery Act: Impact on U.S. Industries and Consumers: Ninth Report 1994*, (Pub. No. 2927). U.S. International Trade Commission, September 1994, 10, 17. Much of the initial drop in U.S. imports from CBERA countries was caused by a 75 percent drop in U.S. petroleum and petroleum products imports during the first four years of the program. However, CBERA exports of other manufactured goods, including textile and apparel, were not able to compensate for this drop in oil exports until after the program had been functioning for several years.

36. *U.S. Overseas Loans and Grants: Series of Yearly Data. Volume II. Latin America and Caribbean. Obligations and Loan Authorizations. FY 1996-FY 1994*. Agency for International Development, Washington, D.C., 1996.

37. Stephen A. Quick, "The International Economy and the Caribbean: The 1990s and Beyond," *The Caribbean Basin: Economic and Security Issues Joint Economic Committee Print* (S. Print 102-110), Government Printing Office, Washington, D.C., January 1993.

38. In May 1996, the U.S. International Trade Commission found that "The outlook for U.S. apparel production-sharing trade with CBI countries is somewhat clouded by the uncertain prospects for approval of NAFTA parity legislation for the region. Although many CBI countries have lower labor costs than Mexico and, recently, shipping costs for CBI apparel

trade have fallen sharply, the possibility exists that CBI countries will no longer be economically competitive in apparel assembly without enhanced preferential access to the U.S. market. The phase out of U.S. apparel quotas under the WTO Agreement on Textiles and Clothing (ATC) will gradually erode the preferential market access that CBI countries now enjoy under Guaranteed Access Levels (GALs) and expose the region to heightened competition in the U.S. market from low-cost exporting countries in the Far East whose shipments are currently under quota." *Production Sharing: Use of U.S. Component and Materials in Foreign Assembly Operations*, 1991-1994. (Pub. No. 2966), U.S. International Trade Commission, Washington, D.C., May 1996.

39. *Caribbean Basin Economic Recovery Act: Impact on U.S. Industries and Consumers: Tenth Report 1994*, (Pub. No. 2927), U.S. International Trade Commission, September 1995, 11-12.

40. See letter from 12 Caribbean Ambassadors to Dan Rostenkowski, Chairman of the House Ways and Means Committee, July 16, 1993. "936 funds are an important catalyst for economic development in the Caribbean Basin, contributing to the many efforts underway to establish healthy, free market oriented economies...."

41. Section 936 (4)(b) defines "qualified Caribbean Basin country" as "any beneficiary country (within the meaning of section 212(a)(1)(A) of the Caribbean Basin Economic Recovery Act) which meets the requirements of the clauses (i) and (ii) of section 274(h)(6)(A) and the Virgin Islands."

42. The Caribbean Basin Economic Recovery Act establishes a series of mandatory and discretionary criteria that must be satisfied before a country can be designated as a beneficiary country.

43. The 24 beneficiary countries are Antigua and Barbuda, Aruba, The Bahamas, Barbados, Belize, Virgin Islands, Costa Rica, Dominica, the Dominican Republic, El Salvador, Grenada, Guatemala, Guyana, Haiti, Honduras, Jamaica, Montserrat, Netherlands Antilles, Nicaragua, Panama, St. Kitts and Nevis, St. Lucia, St. Vincent and the Grenadines, and Trinidad and Tobago.

44. Daubón suggests that the TIEA was a *quid pro quo* of the Treasury Department to gain Treasury's approval of the Section 936 program. Daubón further contends that Treasury established onerous terms in the TIEA precisely to scare off CBI countries, thus making them ineligible for the Section 936 program. Ramón E. Daubón, "Section 936 as a Development Resource in the Caribbean: Suggestions for a More Effective Policy," *Migration Impacts of Trade and Foreign Investment. Mexico and Caribbean Basin Countries*, (Boulder: Westview Press) 1991.

45. Elena Suarez and José Contreras, "Analysis of Section 936 CBI Investments and Caribbean Basin Loan

Disbursements," *Caribbean Latin American Action*, Washington, D.C., July 1994.

46. Discussions with Mark Siegleman, Country Desk Officer, Office of Latin America and the Caribbean, U.S. Department of Commerce, and Rick Cardenas, Internal Revenue Service, June 1996.

47. *Caribbean Basin Economic Recovery Act: Impact on U.S. Industries and Consumers. Seventh Report 1991* (Pub. No. 2553), U.S. International Trade Commission, September 1991, 1-11.

48. *Caribbean Basin Economic Recovery Act: Impact on U.S. Industries and Consumers. Seventh Report 1991* (Pub. No. 2553), U.S. International Trade Commission, September 1991, 1-11.

49. Letter from six TIEA CBI Ambassadors to Senator Daniel Patrick Moynihan, May 24, 1993. "In order to reap the benefits of accessing 936 funds, these countries have amended their laws and endured lengthy ratification processes to enact TIEAs."

50. Ramón E. Daubón, "Section 936 as a Development Resource in the Caribbean: Suggestions for a More Effective Policy," *Migration Impacts of Trade and Foreign Investment. Mexico and Caribbean Basin Countries* (Boulder: Westview Press) 1991.

51. Information obtained in interview with officials from Nicaraguan Ministry of the Economy, February 1995.

52. "Statement on Section 936 Programme" Issued by Ministers of the Caribbean Community and Central America, May 28, 1992. In that statement, Ministers reviewed the signing of the TIEAs as a condition for gaining access to Section 936 funds and then stated that they "consider any change in the programme would not only reflect a breach of commitment, but would create grave uncertainty in the private sector and significantly debilitate the economy of the CBI countries."

53. Section 936 companies can repatriate their profits to the mainland and face no U.S. penalties or additional taxes. However, Puerto Rico charges a "tollgate" tax of 10 percent on companies that repatriate profits in the year when the profits are made. Companies can avoid this tollgate tax and continue to enjoy tax-free status under QPSII by reinvesting their profits in Puerto Rican financial instruments. *Tax Policy: Puerto Rico and the Section 936 Tax Credit*, Report No. GAO/GGD-93-109, United States General Accounting Office, Washington, D.C., 1993, 41.

54. The Puerto Rico Bankers Association reports that QPSII funds exceeded \$15 billion in mid-1995. "Special Focus on Puerto Rico" *Caribbean Update* Vol. 12, No. 8, September 1996.

55. The House proposed prohibiting the QPSII tax credit on QPSII earned from assets exceeding 80 per-

cent of the tangible business investment in Puerto Rico of a particular 936 firm. The Senate proposed an across-the-board cut of 2.5 percent that would affect both QPSII and active income tax credit. See *Conference Report* (103-213) for Omnibus Budget Reconciliation Act of 1993 (HR 2264), U.S. Government Printing Office, Washington, D.C., 1993, 622-31.

56. "Country Focus: Caribbean Basin" *Washington Export Letter*, Washington, D.C., August 1994.

57. See Section 1601 of the *Conference Report* (104-737) for the Small Business Job Protection Act of 1996 (HR 3448), Government Printing Office, Washington, D.C., August 1996.

58. Some sources believe that the establishment of the grandfather credit in a new code section paves the way for the extension of the credit in future years. *Caribbean Update* quotes the *San Juan Star* (August 3, 1996) as quoting House Budget Committee Chairman John Kasich as holding out the possibility of "reformulating the program so we can help the people of Puerto Rico." Cited in "Special Focus on Puerto Rico," *Caribbean Update*, Vol. 12, No. 8. September 1996.

59. *Statistical and Graphical Summary. Caribbean Development Program* (as of December 29, 1995). Bureau for Caribbean Affairs, Department of State of the Government of Puerto Rico, San Juan, Puerto Rico. December 29, 1995, 2-3.

60. Richard L. Bernal, "A U.S. Caribbean Tax Lifeline." *Journal of Commerce*, April 16, 1993.

61. *Statistical and Graphical Summary. Caribbean Development Program* (as of December 29, 1995). Bureau for Caribbean Affairs, Department of State of the Government of Puerto Rico, San Juan, Puerto Rico. December 29, 1995, 3, 9.

62. *Statistical and Graphical Summary. Caribbean Development Program* (as of December 29, 1995). Bureau for Caribbean Affairs, Department of State of the Government of Puerto Rico, San Juan, Puerto Rico. December 29, 1995, 3-4.

63. Section 212(a) of the CBERA contains several provisions that permit value added from Puerto Rico to count toward CBERA rule of origin requirements, thus facilitating CBERA assembled goods made of Puerto Rican inputs to enter the United States duty free.

64. *Caribbean Basin Economic Recovery Act: Impact on U.S. Industries and Consumers. Seventh Report 1991*, (Pub. No. 2553), U.S. International Trade Commission, September 1991, 1-12.

65. *Statistical and Graphical Summary. Caribbean Development Program* (as of December 29, 1995), Bureau for Caribbean Affairs, Department of State of the Government of Puerto Rico, San Juan, Puerto Rico. December 29, 1995, 3, 7.

66. "Requirements for Investments to Qualify Under Section 936(d)(4) as Investments in Qualified Caribbean Basin Countries," Internal Revenue Service. Sec. 1.936-10(c)(4)-(5) as discussed in *Caribbean Basin Economic Recovery Act: Impact on U.S. Industries and Consumers. Seventh Report 1991*, (Pub. No. 2553), U.S. International Trade Commission, September 1991, 1-10.

67. "Guarantees of tax-exempt obligations are an inefficient way of allocating Federal resources. Assistance to the borrower, through the tax exemption and the guarantee, provides interest savings to the borrower that are smaller than the tax revenue loss to the government. Thus, the cost to the taxpayer is greater than the benefit to the borrower." *Policies for Federal Credit Programs and Non-Tax Receivables. Circular No. A-129* (Revised), Office of Management and Budget, Washington, D.C., January 1993.

68. *Caribbean Basin Economic Recovery Act: Impact on U.S. Industries and Consumers. Seventh Report 1991*, (Pub. No. 2553), U.S. International Trade Commission, September 1991, 1-10.

69. In a May 21, 1993 letter to Caribbean heads of state, Puerto Rican Secretary of State Baltasar Corrada del Rio urged, "I should like to take this opportunity officially to invite you to deliver to the United States Department of State or directly to the United States Senate and United States House of Representatives... whatever message you find most accurately reflects the importance that the Section 936 Caribbean leading program has had for the economic development of your country."

70. "Section 936 Caribbean Lending Program: government of Puerto Rico Policy and Procedure," Department of State of Commonwealth of Puerto Rico, San Juan, PR, September 14, 1993.

71. "Qualified Caribbean Basin Loans Regulation" No. 5002, Issued by the Commonwealth of Puerto Rico, Office of the Commissioner of Financial Institutions, Financial Board, Economic Development Administration, December 7, 1993.

72. Doreen Hemlock, "Rossello Sets New Limits on 936 lending to the Caribbean," *San Juan Star*, September 15, 1993; and Doreen Hemlock, "Caribbean Basin Heads Object to PR 936 Lending Policy," *San Juan Star*, September 24, 1993.

73. *Statistical and Graphical Summary. Caribbean Development Program* (as of December 29, 1995), Bureau for Caribbean Affairs, Department of State of the Government of Puerto Rico, San Juan, Puerto Rico, December 29, 1995.

74. *Statistical and Graphical Summary. Caribbean Development Program* (as of December 29, 1995), Bureau for Caribbean Affairs, Department of State of the Government of Puerto Rico, San Juan, Puerto Rico, December 29, 1995.

75. Except where noted, this section is based on the testimony of Richard L. Bernal, "The Role of 936 Funds in Economic Development of Caribbean Countries," delivered before the House Ways and Means Committee on April 1, 1993 (Hearings Before the Committee on Ways and Means — Serial 103-27) and the Senate Finance Committee on April 27, 1993 (Hearings Before the Committee on Finance — S. Hrg 103-199), Washington, D.C., 1993.
76. Figures for the ten TIEA countries include the projects that are financed through the twin-plant mechanism and through direct 936 loans to CBI countries. *Statistical and Graphical Summary. Caribbean Development Program* (as of December 29, 1995), Bureau for Caribbean Affairs, Department of State of the Government of Puerto Rico, San Juan, Puerto Rico, December 29, 1995.
77. Statistics drawn from remarks delivered at the Heritage Foundation by Richard L. Bernal, April, 1996 from official statistics of U.S. Department of Commerce.
78. Richard L. Bernal, "A Jamaican's Case for Trade Parity with NAFTA," *The Wall Street Journal*, March 22, 1996.
79. See Stephen E. Lamar, "Statement Submitted to the House Ways and Means Trade Subcommittee," Hearing on U.S. Trade Competitiveness and Workforce and Education Training, August 2, 1996.
80. Section 202 (1) of the Caribbean Basin Economic Recovery Expansion Act of 1990 (PL 101-382; Title II). Codified at 19 U.S.C. 2701.
81. "Testimony of Peter Johnson, Executive Director, C/LAA," Hearings Before the Committee on Ways and Means — Serial 103-27 (Washington, D.C.: Government Printing Office, 1993).
82. General John Sheehan makes the parallel point that a serious disruption in the Eastern Caribbean banana trade — as a result of a diminution of EU banana preferences — could undermine economic growth in the Eastern Caribbean and encourage increased illegal drug trafficking. See Thomas Lippman, "An Appeal for a Banana Peace," *The Washington Post*, June 6, 1996.
83. *Caribbean Update* reports that the Caribbean loan program, which "has been a source of hundreds of millions of dollars of low-interest loans for the Caribbean, is likely to dry up." Cited in "Special Focus on Puerto Rico," *Caribbean Update*, Vol. 12. No 8. September, 1996.
84. *Conference Report* (104-737) to accompany the Small Business Job Protection Act of 1996 (HR 3448), August 1, 1996, 292.
85. Adjustments to data from U.S. Census Bureau by Foreign Trade Division, Massachusetts Institute of Social and Economic Research, University of Massachusetts, 1996.
86. See Section 212 (a) of the CBERA.
87. "Government of Puerto Rico Position Statement and Governor Pedro Rossello's Job Creation Alternative for Puerto Rico" Puerto Rico Federal Affairs Administration, January 1996.
88. In questions directed at former Resident Commissioner Antonio Colorado, on the Caribbean Section 936 program, Congressman Charles Rangel (D-NY) notes that "Initially you [the Puerto Ricans] fought it because that was just an intrusion on your rights." (Hearings Before the Committee on Ways and Means — Serial 103-27), Government Printing Office, Washington, D.C., 1993.
89. During a Senate Finance Committee mark-up of HR 3448 on June 12, 1996, Senator Bob Graham (D-FL) expressed concern that the phaseout of the Section 936 program was being contemplated at a time when the Committee was unable to move forward on NAFTA parity. See also "Carib Jobs in Danger," *The Jamaican Weekly Gleaner*, May 31 - June 6, 1996.
90. Caribbean countries are facing unequal market access vis-à-vis Mexico's exports to the United States because of preferences that NAFTA accords to Mexico. NAFTA parity proponents envision an extension of the CBI framework to bring Mexican and Caribbean exports to the United States to a level playing field. See Richard L. Bernal, "A Jamaican's Case for Trade Parity with NAFTA," *The Wall Street Journal*, March 22, 1996 and Richard L. Bernal, "Caribbean Nations Need NAFTA, Too." *The Washington Times*, October 1, 1993. For a more extensive discussion, see Richard L. Bernal, "Statement Prepared for the U.S. International Trade Commission in Response to Requests for Comments on the 11th Annual Review of the CBERA," Washington, D.C., July 31, 1996, or Richard L. Bernal, "Statement Submitted to the U.S. Trade Representative," Washington, D.C., July 15, 1996.
91. The EU banana issue refers to a dispute between the United States and the European Union over the EU banana import policies and procedures, which give preferences to bananas exported from former colonies, including certain English-speaking Caribbean Basin countries. See Bob Herbert, "Banana Bully," *The New York Times*, May 13, 1996. See also Richard L. Bernal, "Fighting a Banana Battle Now Will Mean, U.S. Will Lose Lots of Trade Later," Letter to the Editor, *The Washington Times*, August 24, 1995.

Chart 1.
Structure of Section 936/CBI Loan Program

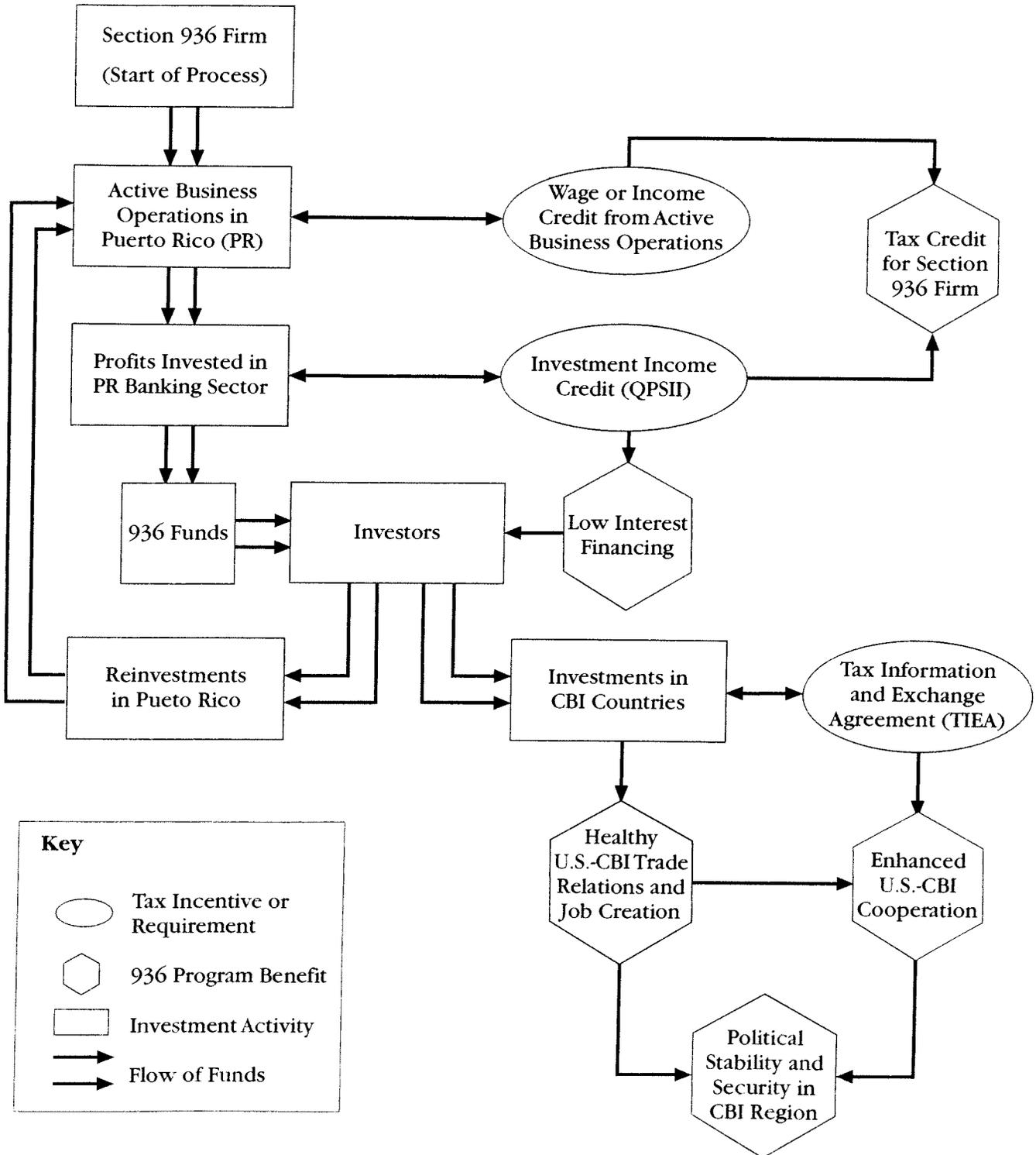


Table 1
U.S. Assistance to CBI Beneficiary
and TIEA Countries
(millions of US dollars; fiscal year basis)

Country	1984	1988	1992	1994	Percent Change
Bahamas	0.0	0.1	1.1	0.7	n.a.
Barbados	4.4	0.0	0.0	0.1	-97.73
Belize	6.0	15.4	10.2	4.0	-33.33
Costa Rica	181.1	120.6	33.0	12.2	-93.26
Dom. Republic*	104.5	59.9	24.3	91.4	-12.54
El Salvador	412.5	395.6	291.4	57.2	-86.13
Grenada	49.4	0.1	0	0.1	-99.80
Guatemala	20.2	141.6	62.9	67.8	235.64
Guyana	0.0	7.0	8.0	9.5	n.a.
Haiti	47.6	40.3	51	106.0	122.69
Honduras	172.7	198.1	95.7	47.8	-72.32
Jamaica	116.2	82.3	80.0	32.6	-71.94
Nicaragua	0.1	0.4	74.9	93.1	93,000.00
Panama	25.8	1.2	27.1	6.6	-74.42
Trinidad and Tobago	39.0	0.1	0.5	0.1	-99.74
Central American Regional	15.5	58.6	12.4	6.9	-55.48
Caribbean Regional	66.8	46.1	29.6	7.9	-88.17
Total CBI	1,261.8	1,167.4	802.1	544.0	-56.89
Total TIEA	734.1	514.2	271.1	201.7	-72.52

Note: Countries included are based on CBI Beneficiary status as of 1996. TIEA countries have signed Tax Information Exchange Agreements.

Source: *U.S. Overseas Loans and Grants: Series of Yearly Data, Volume II Latin America and Caribbean, FY 1946 - FY 1994.*

* Dominican Republic figures for 1994 include \$71.7 million in capitalized interest on prior loans.

Table 2
Section 936 Investment Activity in Eligible
Caribbean Basin Countries¹
(1988 — 1995)

CBI Country	Date Eligible	Qualified Loans ²	Total Investment ²	No. of Projects	CBI Jobs Created
Barbados	1984	51.1	52.1	7	249
Costa Rica	1991	70.3	231.7	44	11,618
Dominica	1988	2.1	2.1	1	50
Dominican Republic	1989	168.7	273.9	75	19,524
Grenada	1987	12.0	17.8	6	273
Guyana	1992	0.6	0.9	1	n.a.
Honduras	1991	168.3	215.2	16	3,633
Jamaica	1986	434.8	577.9	19	1,194
St. Lucia	1991	1.5	2.0	2	30
Trinidad and Tobago	1990	367.0	709.0	7	223
Totals		1,276.4	2,082.6	178	36,794

¹ Eligible Caribbean Basin Initiative (CBI) countries are countries who have signed a Tax Information Exchange Agreement (TIEA) with the United States. "Date eligible" indicates the date the country signed the TIEA.

² Figures for Qualified Loans and Total Investments are calculated in millions of dollars.

Source: *Statistical and Graphic Summary* (as of December 29, 1995), Caribbean Development Program, Bureau of Caribbean Basin Affairs, Department of State of Puerto Rico.

Table 3
Financing Program of the Caribbean Basin Initiative
PROJECTS LISTED BY CALENDAR YEAR
(not including complementary plants)
(in US dollars)

Projects Financed with Qualified Funds in 1988

Project	Country	Industry	Jobs Created in CBI	Loans of Qualified Funds	Total Investment	Bank
ABC Container*	Dominica	Paper & Allied Products	50	2,100,000	2,100,000	Citibank
UDC Transhore	Jamaica	Low income housing	n.a.	8,700,000	8,700,000	GDB
TOTAL	2		50	10,800,000	10,800,000	

Projects Financed with Qualified Funds in 1989

Project	Country	Industry	Jobs Created in CBI	Loans of Qualified Funds	Total Investment	Bank
Air Jamaica	Jamaica	Services	30	51,000,000	57,000,000	Drexel
Transcaribbean Cable	Jamaica	Services	n.a.	17,000,000	17,000,000	Chase
TOTAL	2		30	68,000,000	74,000,000	

Projects Financed with Qualified Funds in 1990

Project	Country	Industry	Jobs Created in CBI	Loans of Qualified Funds	Total Investment	Bank
Barbados Tel. Co.	Barbados	Infrastructure	n.a.	13,000,000	13,000,000	Scotiabank
Sapphire Beach	U.S.V.I.	Tourism	200	9,135,000	9,135,000	Citibank
Rosehall Montego Bay	Jamaica	Tourism	n.a.	10,000,000	35,400,000	Chase
Jamaica Tel. Co. I	Jamaica	Telecommunications	125	22,000,000	22,000,000	Scotiabank
Metaldom	Dom. Rep.	Metals & related products	240	27,500,000	27,500,000	Scotiabank
Seaboard	Dom. Rep.	Infrastructure	24	18,000,000	22,500,000	Chase
Phoenix Park	Trinidad	Petroleum refining	50	80,000,000	80,000,000	Citibank
TOTAL	7		639	179,635,000	209,535,000	

Note: *Exceptions: Although Searle Costa Rica, Inc. and ABC Container are complementary plants located in Costa Rica and Dominica, respectively, they are included in this list because these projects are also "qualified investments" financed with qualified funds.

Table 3 continued
PROJECTS LISTED BY CALENDAR YEAR
(not including complementary plants)

Projects Financed with Qualified Funds in 1991

Project	Country	Industry	Jobs Created in CBI	Loans of Qualified Funds	Total Investment	Bank
Barbados Tel. Co. Ltd.	Barbados	Infrastructure	132	22,000,000	22,000,000	Bankers Trust Caribe
Inversiones Cen-Am	Costa Rica	Agribusiness	140	300,000	600,000	Partners/Chase/LAAD
Searle Pharmaceuticals*	Costa Rica	Chemical & allied prods.	33	1,628,000	2,000,000	Citibank
Grenada Telephone	Grenada	Telecommunications	40	8,000,000	8,220,000	Bankers Trust Caribe
Alcan	Jamaica	Metal & allied prods.	n.a.	60,000,000	60,000,000	Citibank
Alpart	Jamaica	Metal & allied prods.	75	60,000,000	60,000,000	Paine Webber
Jamaica Broilers	Jamaica	Food	83	3,000,000	3,079,000	Citibank
Jamaica Grande Ltd.	Jamaica	Tourism	100	27,000,000	27,000,000	Chase
Bratex Dom.	Dom. Rep.	Apparel & textiles	400	520,000	1,025,000	Partners/Chase
Caribex Dominicana	Dom. Rep.	Food Processing	100	1,620,000	1,620,000	Citibank
Fiesta Bavaro Hotel	Dom. Rep.	Tourism	305	22,000,000	36,455,900	Central BankCorp/BBV
Hotel Embajador	Dom. Rep.	Tourism	17	2,500,000	3,246,100	Bco. Com. de Mgúez/BBV
NSS	Dom. Rep.	Electronics	200	4,500,000	4,500,000	Citibank
Texaco Trinidad	Trinidad	Petroleum exploration	n.a.	20,000,000	20,000,000	Scotiabank
TOTAL	14		1,625	233,068,000	249,746,000	

Note: *Exceptions: Although Searle Costa Rica, Inc. and ABC Container are complementary plants located in Costa Rica and Dominica, respectively, they are included in this list because these projects are also "qualified investments" financed with qualified funds.

Projects Financed with Qualified Funds in 1992

Project	Country	Industry	Jobs Created in CBI	Loans of Qualified Funds	Total Investment	Bank
Barbados Bottling Co.	Barbados	Industrial machinery	n.a.	950,000	950,000	Partners/CFSC
Bondhus	Barbados	Fabricated metal prods.	27	150,000	320,000	Partners/Chase/CFSC
Chiquita Brands	Costa Rica	Agribusiness	7,200	38,000,000	130,000,000	Bankers Trust Caribe
Estructuras de Concreto	Costa Rica	Concrete products	165	2,500,000	3,627,900	Citibank
Inversiones Zeta	Costa Rica	Infrastructure	220	5,000,000	5,500,000	Citibank
Paraiso Verde	Costa Rica	Agribusiness	100	900,000	9,000,000	Partners/Chase/LAAD
Texaco Costa Rica, S.A.	Costa Rica	Retail Trade	240	4,049,000	4,049,000	Citibank
Adhotel	Honduras	Tourism	50	980,000	980,000	Partners/BASA
CAHSA	Honduras	Agribusiness	150	999,000	999,000	Partners/LAAD
INDEMA	Honduras	Wood & wood products	475	550,000	550,000	Partners/LAAD
INDEMA II	Honduras	Wood & wood products	255	200,000	200,000	Partners/LAAD
Rio Nance	Honduras	Agribusiness	14	250,000	250,000	Partners/LAAD
Jamaica Inter Telecom.	Jamaica	Telecommunications	594	6,000,000	8,472,000	Scotiabank
Jamaica Tel. Co. II	Jamaica	Telecommunications	125	6,086,000	10,360,000	Scotiabank
Jamaica Tel. Co. III	Jamaica	Telecommunications	n.a.	5,400,000	49,900,000	Scotiabank
Caribbulk	Dom. Rep.	Agribusiness	6	999,900	1,596,400	Partners/Chase
Amoco Oil	Trinidad	Natural gas production	113	75,000,000	100,000,000	First Boston/Chase
Mobil Oil	Trinidad	Petroleum exploration	n.a.	35,000,000	46,000,000	Scotiabank
TOTAL	18		9,734	183,013,900	364,754,300	

Table 3 continued
PROJECTS LISTED BY CALENDAR YEAR
(not including complementary plants)

Projects Financed with Qualified Funds in 1993

Project	Country	Industry	Jobs Created in CBI	Loans of Qualified Funds	Total Investment	Bank
American Flower Corp.	Costa Rica	Agribusiness	10	400,000	1,500,000	Partners/LAAD
Calypso	Costa Rica	Tourism	6	350,000	466,666	Partners/Banex
Catanzaro	Costa Rica	Tourism	30	650,000	650,000	Partners/PIC
Coopesa	Costa Rica	Metal & related prods.	120	500,000	500,000	Partners/PIC
INCESA	Costa Rica	Tile manufacturing	92	999,000	999,000	Partners/PIC
Lovable Brassiere	Costa Rica	Apparel	400	600,000	600,000	Partners/PIC
Lago Azul	Costa Rica	Agribusiness	11	400,000	1,100,000	Partners/LAAD
Papayas del Pacifico	Costa Rica	Agribusiness	119	550,000	550,000	Partners/LAAD
Piñales de Santa Clara	Costa Rica	Agribusiness	110	300,000	600,000	Partners/LAAD
Tico Verde	Costa Rica	Agribusiness	100	900,000	900,000	Partners/LAAD
Wamers	Costa Rica	Apparel	600	3,000,000	3,825,000	Scotiabank
Demerara Oxygen Co.	Guyana	Chemical & allied prods.	n.a.	600,000	857,000	Partners/CFSC
Hondex	Honduras	Agribusiness	30	900,000	900,000	Partners/LAAD
Hondutel I	Honduras	Telecommunications	300	75,000,000	91,000,000	Chase
Hondutel II	Honduras	Telecommunications	150	76,000,000	100,000,000	Citibank
Inalma	Honduras	Agribusiness	36	113,000	224,000	Partners/LAAD
Olga de Villanueva	Honduras	Apparel	1,500	4,000,000	4,000,000	Scotiabank
Santa Elena	Honduras	Agribusiness	85	110,000	178,000	Partners/LAAD
Viveros Tropicales	Honduras	Agribusiness	40	500,000	721,000	Partners/LAAD
Texaco Caribbean, Inc.	Jamaica	Retail trade	15	2,150,000	2,150,000	Citibank
Agrolasa	Dom. Rep.	Agribusiness	179	588,000	850,000	Partners/LAAD
America Mills	Dom. Rep.	Apparel	200	1,000,000	2,600,000	Chase
Bratex II	Dom. Rep.	Apparel	490	1,500,000	3,200,000	Chase
Caribex II	Dom. Rep.	Food processing	n.a.	810,000	810,000	Citibank
Caribex Dominicana	Dom. Rep.	Agribusiness	68	350,000	500,000	Partners/LAAD
Central Romana	Dom. Rep.	Agribusiness	n.a.	4,000,000	6,000,000	Chase
Domex	Dom. Rep.	Agribusiness	47	400,000	721,000	Partners/LAAD
Metaldom II	Dom. Rep.	Metal & related prods.	n.a.	2,500,000	2,500,000	Scotiabank
Metaldom III	Dom. Rep.	Metal & related prods.	700	13,000,000	25,000,000	Scotiabank
Procesadora Mejía	Dom. Rep.	Agribusiness	1,143	999,000	1,580,000	Partners/LAAD
Rancho Cayman	Dom. Rep.	Agribusiness	25	400,000	400,000	Partners/LAAD
East Winds Beach Hotel	St. Lucia	Tourism	30	500,000	1,000,000	Partners/CFSC
National Gas Co.	Trinidad	Infrastructure	60	7,000,000	7,900,000	Citibank
TOTAL	33		6,696	202,069,000	263,881,666	

Table 3 continued
PROJECTS LISTED BY CALENDAR YEAR
(not including complementary plants)

Projects Financed with Qualified Funds in 1994

Project	Country	Industry	Jobs Created in CBI	Loans of Qualified Funds	Total Investment	Bank
Accesorios Plásticos	Costa Rica	Plastic products	n.a.	360,000	360,000	Partners/Banex
Desarrollos Hoteleros	Costa Rica	Tourism	460	650,000	36,300,000	Partners/Transamerica
El Sapo Dorado	Costa Rica	Tourism	2	170,000	278,000	Partners/Banex
Empaques Santa Ana	Costa Rica	Cardboard manftg.	120	650,000	4,000,000	Partners/Banex
Envases Comeca	Costa Rica	Metal product:	n.a.	500,000	650,000	Partners/Banex
Hacia Adelante Ltda.	Costa Rica	Tourism	37	650,000	2,000,000	Partners/PIC
Hules Técnicos	Costa Rica	Rubber manftg.	21	500,000	680,000	Partners/Banex
Inv Agro Lomas Platanar	Costa Rica	Agribusiness	21	350,000	742,000	Partners/Banex
Playas Tamarindo	Costa Rica	Tourism	n.a.	500,000	1,471,000	Partners/Banex
Swiss Travel Service	Costa Rica	Tourism	10	350,000	669,000	Partners/Banex
ELCATEX	Honduras	Textiles	423	5,200,000	9,200,000	Bank of Boston
Hoteles de Honduras	Honduras	Tourism	53	700,000	2,300,000	Partners/BASA
Texaco Caribbean, Inc.	U.S.V.I.	Retail trade	18	2,350,000	2,350,000	Citibank
Holiday Inn	Jamaica	Tourism	100	28,000,000	32,000,000	Bankers Trust
Jamaica Private Power	Jamaica	Energy	40	101,000,000	144,000,000	First Boston
Power Sun Jamaica	Jamaica	Toursim	7	950,000	3,300,000	Partners/Eagle
Agric. Nueva Esperanza	Dom. Rep.	Agribusiness	31	400,000	855,000	Partners/LAAD
Benjamin & Gil Abreu	Dom. Rep.	Agribusiness	20	200,000	200,000	Partners/LAAD
Bratex III	Dom. Rep.	Apparel	1,101	6,000,000	8,086,691	Chase
Camelia Agroindustrial	Dom. Rep.	Agribusiness	55	456,000	3,000,000	Partners/LAAD
Caribbean Catering Serv	Dom. Rep.	Food services	60	975,000	1,875,000	Partners
Cherobi Agroindustrial	Dom. Rep.	Agribusiness	45	445,000	1,900,000	Partners/LAAD
Exportadora Japonesa	Dom. Rep.	Agribusiness	16	200,000	413,000	Partners/LAAD
Miguel Marrero	Dom. Rep.	Agribusiness	8	200,000	452,000	Partners/LAAD
Telepuerto San Isidro	Dom. Rep.	Telecommunications	150	32,000,000	32,000,000	Chase
Texaco Caribbean, Inc.	Dom. Rep.	Retail trade	207	5,500,000	5,500,000	Citibank
Malabar Beach	Sta. Lucia	Tourism	n.a.	999,000	1,000,000	Partners/CFSC
Amoco Trinidad Oil Co.	Trinidad	Natural gas production	n.a.	75,000,000	225,000,000	Bank of Nova Scotia
Enron Gas & Oil Trinidad	Trinidad	Gas & oil production	n.a.	**75,000,000	231,000,000	Citibank/Scotiabank
TOTAL	29		3,005	340,255,000	751,581,691	

Note: **Citibank financed \$31 million and Scotiabank financed \$44 million of the total \$75 million of this loan.

Table 3 continued
PROJECTS LISTED BY CALENDAR YEAR
(not including complementary plants)

Projects Financed with Qualified Funds in 1995

Project	Country	Industry	Jobs Created in CBI	Loans of Qualified Funds	Total Investment	Bank
Barrel III	Barbados	Telecommunications	0	15,000,000	15,000,000	Citibank
Cabaña Tortuga, S.A.	Costa Rica	Tourism	0	300,000	300,000	Partners/Banex
Parador Quepos	Costa Rica	Tourism	72	500,000	4,000,000	Partners/CPI
Piña Tica	Costa Rica	Agribusiness	50	600,000	4,589,000	Partners/Transamerica
PPLP	Costa Rica	Plastic products	6	850,000	1,000,000	Partners/Transamerica
Price Waterhouse	Costa Rica	Service	0	400,000	1,300,000	Partners
Recyplast	Costa Rica	Plastic products	38	950,000	2,400,000	Partners/Banex
Ticofruit	Costa Rica	Agribusiness	72	950,000	4,343,000	Partners/Banex
Bratex IV	Dom. Rep.	Apparel	515	3,000,000	4,655,109	Chase
Rafael Rodríguez	Dom. Rep.	Agribusiness	12	200,000	200,000	Partners/LAAD
Punta Cana	Dom. Rep.	Tourism	100	1,500,000	5,000,000	Bilbao Vizcaya
Sociedad Filpo y Almonte	Dom. Rep.	Agribusiness	55	400,000	2,097,000	Partners/LAAD
Telepuerto San Isidro (TRICOM)	Dom. Rep.	Telecommunications	150	14,000,000	14,000,000	Chase
Grentel	Grenada	Telecommunications	13	4,000,000	6,434,000	Nova Scotia
Deli-Honduras	Honduras	Agribusiness	42	800,000	2,273,000	LAAD
Derivados de la Madera	Honduras	Wood and wood prods.	30	999,000	1,400,000	LAAD
Telecommunications of Jamaica Limited (TJL) I	Jamaica	Telecommunications	0	25,000,000	30,800,000	Nova Scotia
Telecommunications of Jamaica Limited (TJL) II	Jamaica	Telecommunications	0	1,546,169	6,675,000	Nova Scotia
TOTAL	18		1,155	70,995,169	106,466,109	

Key:

Banex	Banex International in Panama
BASA	Banco Atlántida, S.A.
BBV	Banco Bilbao Vizcaya
CFSC	Caribbean Financial Services Corporation
Eagle	Eagle Merchant Bank of Jamaica
GDB	Government Development Bank
LAAD	Latin American Agribusiness Development Corporation
Partners	Caribbean Basin Partners for Progress, Ltd.
PIC	Private Investment Corporation
Transamerica	Transamerica Bank & Trust Company, Ltd.

Source: Reprinted from *Statistical and Graphical Summary*, Caribbean Development Program, Bureau for Caribbean Basin Affairs (as of December 29, 1995), Department of State of Puerto Rico, San Juan, Puerto Rico.

Table 4
Number of U.S. Workers Dependent
on Trade with the Caribbean
Basin Nations

Year	Total Number of U.S. Workers*	Number of New U.S. Jobs Created per Year
1985	118,840	—
1986	127,240	8,400
1987	138,120	10,880
1988	153,800	15,680
1989	165,800	12,000
1990	191,380	25,580
1991	200,260	8,880
1992	225,262	25,002
1993	248,552	23,290
1994	268,814	20,292
1995	306,120	37,306

Average Annual Job Creation: 18,731

* Assuming that \$1 billion in U.S. exports creates 20,000 U.S. trade-related jobs.

Sources: U.S. Department of Commerce.
U.S. International Trade Commission.
Updated: April 22, 1996

Table 5
U.S.-CBI Trade Statistics (1985 - 1995)
(millions of US dollars)

Year	U.S. Imports	U.S. Exports	Annual Export Trade Growth	Balance
1985	6,687	5,942	—	-745
1986	6,065	6,362	7.1%	297
1987	6,039	6,906	8.6%	867
1988	6,061	7,690	11.4%	1,629
1989	6,637	8,290	7.8%	1,653
1990	7,525	9,569	15.4%	2,044
1991	8,372	10,013	4.6%	1,641
1992	9,627	11,263	12.5%	1,636
1993	10,378	12,428	10.3%	2,050
1994	11,495	13,441	8.1%	1,946
1995	12,673	15,306	13.8%	2,633

Average Annual U.S. Export Growth: 9.96%

Note: 1995 marked the 10th straight year of U.S. trade surpluses.

Sources: U.S. Department of Commerce.
U.S. International Trade Commission.
Updated: April 22, 1996

Table 6
Loans Disbursed in
TIEA Signatory Countries In 1993¹
(in thousands of US dollars)

Financial Source	Total
Caribbean Development Bank (CDB)	25,300
Caribbean Financial Services Corporation (CFSC)	3,498
Central American Bank for Economic Integration (CABEL)	83,300
Commonwealth Development Corporation (CDC)	51,752
Export Development Corporation (EDC)	54
European Investment Bank (EIB)	37,513
German Investment and Development Company (DEG)	3,507
International Development Association (IDA)	85,918
International Finance Corporation (IFC)	26,800
Inter-American Development Bank (IDB)	302,200
Inter-American Investment Corporation (IIC)	9,920
Latin American Agricultural Development Bank (LAAD)	10,482
Latin American Export Bank (BLADDEX)	239,990
Overseas Economic Cooperation Fund (OECF)	1,115
Overseas Private Investment Corporation (OPIC)	14,000
Netherlands Development Finance Company (FMO)	4,550
World Bank (IBRD)	169,773
Subtotal	1,069,672
Section 936 Funds	202,539
Total (including Section 936)	1,272,211
Section 936 Percent of Total	15.92 %

¹ TIEA Countries include Barbados, Costa Rica, Dominica, Dominican Republic, Grenada, Guyana, Honduras, Jamaica, St. Lucia, Trinidad and Tobago.

Source: Analysis of Section 936 CBI Investments and Caribbean Loan Disbursements, Caribbean Latin American Action.