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COMMENT

NORTH AMERICAN FREE TRADE: MEXICO, CANADA AND THE UNITED STATES

INTRODUCTION

On June 10, 1990, President Bush and Mexican President Carlos Salinas de Gortari agreed to lay the groundwork necessary to move towards a Mexico-United States free trade agreement ("FTA"). Linking the Mexico-U.S. agreement with the 1989 FTA between Canada and the U.S. would likely increase the \$52 billion yearly flow of goods between the three nations and create thousands of new jobs.¹ The new market consisting of 385 million people and a gross national product of \$5.5 trillion would be free of most trade restraints and create a highly integrated trade network capable of competing with the 1992 European Economic Community and the Asian Pacific Basin.² A successful FTA with Mexico would mark the second step, following the FTA with Canada, toward President Bush's eventual goal of having a "hemispheric free trade zone all the way from the Arctic to the tip of South America."³

For years, analysts have speculated about the possibility of free trade in North America: among Mexico, Canada, and the United States. They did not, however, seriously discuss Mexico's involvement until the U.S. and Canada officially approved the United States-Canada FTA⁴ ("Canada FTA") on January 1, 1989, and until March 1990, when a U.S. newspaper article reported that Mexico and U.S. cabinet officials had agreed to negotiate a free-trade pact.⁵

The U.S. and Mexico announced on February 5, 1991, that Canada would be joining the Mexico-U.S. talks concerning the pos-

1. *New Study Shows that a U.S./Mexico Free Trade Agreement Will Bring Increased American Wages and Economic Growth*, P.R. News Wire Assoc., Feb. 27, 1991, available in LEXIS, Nexis Library, Omni File.

2. The Asian Pacific Basin includes Australia, New Zealand, Japan, and other major economic powers in southeast Asia. Samuel Bettwy, *National Security Interests in the Pacific Basin*, 81 A.J.I.L. 288 (1987).

3. Jack Lesar, *quoting* Commerce Secretary Robert Mosbacher, UPI, Oct. 25, 1990, available in LEXIS, Nexis Library, Omni File.

4. The Canada-United States: Free Trade Agreement, Dec. 22, 1987, 27 I.L.M. 281 (entered into force Jan. 1, 1989) [hereinafter Canada FTA].

5. Peter Truell, WALL ST. J., Mar. 27, 1990, at A3.

sibility of free trade,⁶ however, the impact of Canada's involvement will be insignificant compared to the ramifications of Mexico-U.S. free trade.⁷

The existence of the Canada FTA demands that Mexico look into its effects. The Canada FTA calls for tariffs between the two countries to move to zero by January 1, 1999. At that time, because the Canada FTA will protect Canadian exports from future U.S. non-tariff barriers,⁸ Mexican products will not benefit from the same protection and will face discrimination in the U.S. market. Therefore, Mexico's motivation to become involved in an FTA is greatly enhanced.

The ineptness of the General Agreement on Tariffs and Trade ("GATT")⁹ to regulate today's sophisticated and complex trade relations has prompted the negotiation of bilateral trade pacts, such as free trade agreements. FTAs have several benefits over the GATT: (1) they can "address specific bilateral concerns, (2) foster increased trade between countries, and (3) enhance trade relationships."¹⁰ The United States currently has an FTA agreement with both Israel¹¹ and Canada.¹² With the failure of the Uruguay Round of

6. On February 5, 1991, President George Bush, Mexican President Carlos Salinas de Gortari and Canadian Prime Minister Brian Mulroney officially announced their intention to pursue a North American free trade pact. Upendra Nath Mishra, *Mexican, U.S., Canadian officials to Talk Trade*, UPI, Feb. 14, 1991; see also transcript of *World News Tonight With Peter Jennings*, Feb. 5, 1991, available in LEXIS, Nexis Library, Omni File.

7. Compared to Mexico-U.S. trade and Canada-U.S. trade, "[t]rade between Mexico and Canada is of minute proportion. It may be expected to expand when trade barriers are removed, but one is hard put to assess the scope and nature of this expansion." M. Mordechai E. Kreinin, *North American Economic Integration*, 44 LAW & CONTEMP. PROBS. 7, 31 (1981).

"Total two way trade between Mexico and Canada was \$2.4 billion in 1989 with Mexican exports approximately twice those of Canadian. Canadian exports were divided chiefly among food, live animals, manufactured goods and machinery and transportation equipment, while those of Mexico concentrated in machinery and transportation equipment." *Review of Trade Investment Liberalization Measures by Mexico and Prospects for Future United States Mexican Relations, Phase II: Summary of Views on Prospects for Future United States-Mexican Relations*, USITC Pub. 2326, Inv. No. 332-282 at 1-26 n.92 (Oct. 1990) [hereinafter Phase II].

8. Non-tariff barriers can be described as: "[M]easures and practices, public or private, other than a customs tariff, operated in a country, or by a common agreement in two or more countries, which have directly or indirectly, the effect of hindering the sale in that country or in those countries of goods or services from other countries and/or of artificially facilitating the sale of goods or services originating in that or those countries." R. MIDDLETON, *NEGOTIATING ON NON-TARIFF DISTORTIONS OF TRADE*, 3 (1975).

9. General Agreement on Tariffs and Trade, *opened for signature* Oct. 30, 1947, 61 Stat., 55 U.N.T.S. 194 [hereinafter GATT].

10. Mary E. Peters, *Free Trade Area Agreements as the Economic and Legal Solution to Bilateral Trade Relationships: The Case of Japan*, 28 COLUM. J. TRANSNAT'L L. 499, 499 (1990).

11. United States-Israel Free Trade Area Implementation Act of 1985, June 11, 1985, U.S.-Israel, 99 Stat. 83, 24 I.L.M. 653 [hereinafter Israel FTA].

12. Canada FTA, *supra* note 4.

the GATT negotiations, it is likely that both Mexico and the U.S. will speedup the process of moving towards an FTA.

A new FTA encompassing all of North America would be novel for two important reasons. First, and most significant, it would include the United States and Canada which are industrialized countries and Mexico which is a developing country.¹³ Second, because the U.S. economy is approximately ten times the size of Canada's and almost twenty-two times that of Mexico's,¹⁴ it would dominate the free trade area to an extent which is unknown in other regional grouping.

No longer is the question, "should the United States and Mexico enter into a free trade agreement?" but rather, "when can a free trade agreement involving Mexico be established?" This paper discusses the role of free trade agreements in world trade and the major issues surrounding the proposed North American FTA. Part I describes the basic framework of FTAs under the GATT and their effects on world trade. Part II gives a brief overview of the existing U.S. free trade agreements involving Israel and Canada. Part III discusses the negotiating process of a free trade agreement. Part IV discusses the areas of interest and the likely impact a North American FTA would have on Mexico, the U.S., and Canada. Finally, Part V considers a proposed framework for a North American FTA. The paper concludes that a North American FTA involving Mexico would be beneficial to all countries involved, with Mexico benefiting most, and that new trilateral FTA between Mexico, Canada, and the U.S. would be the preferable type of agreement.

I. FREE TRADE AREA AGREEMENTS

A. *Why Free Trade Agreements?*

"A free trade area consists of two or more countries that agree to eliminate tariffs and non-tariff barriers on substantially all trade between them."¹⁵ The purpose of an FTA is to increase the efficiency of production and to amass the welfare benefits from trade where efficiencies vary between countries.¹⁶ In theory, an FTA acts as a bilateral mechanism to further liberalize world trade.

When negotiating an FTA, countries must determine in what areas and to what degree the FTA will displace or modify existing

13. "All other integration schemes in the world involve customs unions or FTAs countries at equal stages of development, among either industrialized or developing." See Kreinin, *supra* note 7, at 16.

14. *Id.*

15. Carol Bilzi, *Recent United States Trade Arrangements: Implications for the Most-Favored-Nation Principle and United States Trade Policy*, 17 *LAW & POLICY IN INT'L BUS.* 209, 223 (1985).

16. Sidney Weintraub, *The North American Free Trade Debate*, 13 *THE WASH. Q.* 119 (1990).

national laws.¹⁷ FTAs usually focus upon legally based discrimination between countries such as tariffs, quotas, rules of origin, government procurement and national treatment of imports.¹⁸ However, an FTA may also regulate non-tariff barriers as well. "An FTA is most likely to be beneficial if its members have high tariffs before integration, low tariffs on nonmembers after integration, and if nonmembers have high tariffs on members."¹⁹ With these conditions present, there is the opportunity for trade creation, economies of scale, and less potential for trade diversion.

When entering into an FTA, countries must evaluate the benefits and costs of the agreement. The benefits are wider markets for national production. The costs include the destruction of industries and agriculture because of their loss of competitiveness once trade protection is eliminated through the FTA.

B. *The GATT and Free Trade*

The primary legal mechanism governing multilateral trade agreements and trade relations among the western world is the GATT.²⁰ The most-favored nation ("MFN") principle, also known as nondiscrimination, is the cornerstone of the GATT.²¹ Essentially, the MFN concept is a commitment of nondiscrimination whereby one member country agrees to treat all other member countries equally.²² Any trade advantage given to one country must also be given to all other GATT contracting countries²³ and any "bilateral trade actions automatically become multilateral in effect."²⁴ Conversely, the MFN concept dictates that any disadvantage or trade restriction imposed on one country must also be

17. Peters, *supra* note 10, at 501.

18. *Id.*

19. *The Likely Impact on the United States of a Free Trade Agreement with Mexico*, USTIC Pub. 2353, Inv. No. 332-297, (Feb. 1991) [hereinafter FTA Impact].

20. The principal obligations imposed by the GATT on its members are: (1) to accord most-favored nation treatment to other members; (2) to observe the maximum tariff levels set out in GATT member's schedules of concessions, GATT, *supra* note 9, art. II (schedules of concessions); (3) to limit, and in some circumstances, to abstain from imposing certain non-tariff barriers to trade, *Id.* art. XVI. The Contracting Parties is the name of the GATT decision-making body that operates when the individual GATT members act jointly. *Id.* art. XXV(I); and (4) to use a specified set of dispute resolution procedures when trade conflicts arise. Dispute settlement under the GATT involves consultation and negotiation among governments. *Id.* arts. XIX(2),(3), XXII, XXIII(1), XXVIII(1)-(3). Contracting Parties can also become involved in dispute resolution. *Id.* arts. XXIII(2), XXVIII(4).

21. Bilzi, *supra* note 15, at 214.

22. Bilzi, *supra* note 15, at 215, *citing*, K. RYAN, INTERNATIONAL TRADE LAW 3 (1975).

23. See Ndiva Kofele-Kale, *The Principle of Preferential Treatment in the Law of GATT: Toward Achieving the Objective of an Equitable World Trading System*, 18 CAL. W. INT'L. L. J. 291, 296-97 (1988). See also Wilfried Lutkenhorst, *GATT - Caught Between Self-Destruction and Reform*, 4 INTERECONOMICS 178 (1984).

24. Bilzi, *supra* note 15, at 215.

imposed on all other countries in the same manner.²⁵ Under the GATT, MFN treatment is unconditional and extends automatically without the need for further negotiations among the GATT members.²⁶

FTAs abrogate the GATT MFN principle by allowing members of the FTA to treat each other more favorably than nonmembers. However, GATT negotiators maneuvered around this problem by creating a special exception²⁷ for FTAs and customs unions under Article XXIV.²⁸ This article allows GATT members to remove trade barriers against countries that have adopted an FTA without eliminating trade barriers against nonmember countries.²⁹ Thus, Article XXIV of the GATT provides a general exception to MFN requirements and overrides the MFN obligation when free trade agreements are at issue.³⁰

FTAs and the GATT represent two differing philosophies regarding world trade. GATT supporters tend to base their economic view of the world on the efficiency of free trade and the concept of comparative advantage. FTA supporters, although not against free trade in many cases, frequently see a more activist role for the government and other sectors of the economy. FTA supporters tend to base their economic world view on concepts such as strategic trade. This theory differs from the traditional concept in that trade

25. Ruth E. Olson, *GATT - Legal Application of Safeguards in the Context of Regional Trade Arrangements and its Implications for the Canada-United States Free Trade Agreement*, 73 MINN. L. REV. 1488, 1492 (1989), citing Kofele-Kale, *supra* note 23, at 297.

26. GATT, *supra* note 9, art. I, para. 1.

27. "The rationale for this deviation is that such arrangements actually increase freedom of trade and improve world efficiency, although they are still not as desirable as multilateral agreements." Bilzi, *supra* note 15, at 225, citing JOHN S. LAMBRINIDIS, *THE STRUCTURE, FUNCTION AND LAW OF A FREE TRADE AREA* 240 (1965).

28. Bilzi, *supra* note 15, at 225. For an FTA to qualify under the GATT Article XXIV exception, it must meet several requirements. First, both countries must be members of the GATT. GATT, *supra* note 9, art. XXIV, para. 5. Second, the agreement must not provide for duties and tariffs "higher or more restrictive than those existing in the parties' nations prior to the agreement. *Id.* art. XXIV, para. 5(b). Third, if the FTA calls for a transition period from the time of the agreement until free trade takes effect, the agreement must include "a plan and schedule for the formation of . . . [the] free-trade area within a reasonable length of time." *Id.* art. XXIV, para. 5(c). The "plan and schedule" and "reasonable length of time" requirements are subject to several limitations. See Kenneth W. Dam, *Regional Economic Arrangements and the GATT: The Legacy of a Misconception*, 30 U. CHI. L. REV. 615, 618 (1963). Forth, the FTA must eliminate "duties and other restrictive regulation of commerce . . . on substantially all the trade between the constituent territories in products originating in such territories." GATT, *supra* note 9, art. XXIV, para. 8(b). Lastly, the parties to the FTA must notify the Contracting Parties of the GATT and provide them with the information necessary for them to evaluate the arrangement. *Id.* art. XXIV, para. 7(a).

29. GATT, *supra* note 9, art. XXIV.

30. A free-trade agreement is an agreement between two or more territories "in which the duties and other restrictive regulations of commerce . . . are eliminated on substantially all trade between the constituent territories in products originating in such territories." *Id.* art. XXIV, para. 8(b).

polices, investment strategies, government activities, and so forth can create or alter a nation's comparative advantage in the global economy.³¹ A comparison of the principles and characteristics of the GATT and FTAs is summarized in the table below.

| <u>GATT PRINCIPLES AND CHARACTERISTICS</u> | <u>FTA PRINCIPLES AND CHARACTERISTICS</u> |
|--|--|
| 1. Trade is based on the principle of nondiscrimination. | 1. Trade is based on the principle of discrimination. |
| 2. All members are bound to grant as favorable treatment to each other as they give to any other member, i.e., most-favored nation status. | 2. Nations within the FTA share special preferences not granted to nations outside the FTA. |
| 3. To the maximum extent possible, protection should be provided only through tariffs. | 3. Protection is often provided through quantitative restrictions as well as tariffs. |
| 4. Basic ideas include economic liberalism, multilateralism and free trade based on comparative advantage. | 4. Basic ideas include economic nationalism or regionalism, bilateralism, and trade often based on strategic trade theory and neomercantilism. |
| 5. The system is designed as a community open to all who are willing to follow membership rules. | 5. The FTA may not be open to all who wish to join and are willing to follow membership rules. |
| 6. The goal is to build a unified and integrated global system. | 6. A FTA may function as an exclusive club that generates a "them versus us" psychology. |
| 7. Under Article XXIV, the system provides a means to determine if a regional trading bloc is consistent with the GATT. | 7. In the view of some advocates, FTAs are a way of building a stronger multilateral system in the long run. ³² |

C. *Free Trade Agreements and World Trade*

To understand FTAs, it is important to understand the potential impact they may have on the world economy.³³ World trade can be viewed in terms of trade creation and trade diversion.

31. Marc Levinson, *Is Strategic Trade Fair Trade?*, ACROSS THE BOARD, June 1988, at 47.

32. Richard S. Belous & Rebecca S. Hartley, *Regional Trading Blocs: An Introduction*, in THE GROWTH OF REGIONAL TRADING BLOCS IN THE GLOBAL ECONOMY 1, 3 (1990) (Richard S. Belous & Rebecca S. Hartley eds., 1990).

33. The conventional analysis of regional trading blocs, free trade agreements, and customs unions is usually based on the pioneering work of economist of Jacob Viner. See JACOB VINER, THE CUSTOMS UNION ISSUE (1961).

“When a multilateral system like the GATT is expanded, the net result is growth in trade creation, which is viewed by most trade experts as beneficial for all members of the trading system, the net result is a combination of trade creation - a benefit - and trade diversion - a cost.”³⁴

Advocates of FTAs argue that they facilitate trade creation. Trade creation can be described as follows:

Imports from member countries increase, displacing higher cost domestic goods. The resources that are released in the home country can be used in activities that produce greater value. In addition, consumers increase consumption of the less expensive imports and decrease less valued consumption of other goods. This process, called trade creation, increases welfare.³⁵

As this trade creation increases, consumers, companies, and governments have a greater chance of giving their business to the most efficient producer of a specific good or service.³⁶

Opponents of FTAs generally argue that they create trade diversion. Trade diversion can be described as follows:

Imports from member countries increase, displacing lower cost imports from nonmember countries that still face trade barriers. Consumers actually pay less for the imports, but the loss to the country from reduced tariff revenue and rents to protected domestic industries exceeds the benefit to consumers on imports that would have been purchased from nonmember countries in the absence of the FTA. This process is called trade diversion.³⁷

When trade diversion occurs, consumers, companies, and governments do not always have an opportunity to use the most efficient producer of a specific good or service.³⁸

D. *Costs and Benefits of a Free Trade Agreement*

Whether an FTA is beneficial to the world trading system depends on whether the benefits outweigh the costs. The costs of an FTA are easily seen. FTAs “increase the possibility of a breakdown in the multilateral trading system. There is no doubt that this could happen if [FTAs] become too inward-focused and thus end up slowing overall world trade.”³⁹ However, FTA advocates argue that FTAs, although they may be costly at first, are beneficial to the step-by-step process of “easing . . . world trade back to a full-blown

34. Belous & Hartley, *supra* note 32, at 7.

35. FTA Impact, *supra* note 19. For a thorough discussion on the effects of FTAs see generally Viner, *supra* note 32.

36. Belous & Hartley, *supra* note 32, at 3.

37. FTA Impact, *supra* note 19, at 2-1.

38. *Id.*

39. Richard V.L. Cooper, *Blocs: Making the Best of a “Second-Best” Solution*, in *THE GROWTH OF REGIONAL TRADING BLOCS IN THE GLOBAL ECONOMY* 30, 32 (Richard S. Belous & Rebecca S. Hartley eds., 1990).

multilateral trading system, which we currently do not have."⁴⁰

Because FTAs generate trade diversion as well as trade creation, many experts view them as a "second best" and inferior alternative to expanding the GATT system to cover more issues and to include more signatories.⁴¹ However, compared to the difficulty of reforming the GATT, FTAs or other types of regional trading blocs appear to be the easy solution to international trade problems because it is usually easier to negotiate a bilateral agreement than a multilateral one.

When two or more countries agree on an FTA between them, it does not mean that they place less importance on the GATT. "On the contrary, an effective trade policy . . . must rely on both the FTA and the multilateral trading system."⁴² An FTA gives a country preferential access to specific markets while the GATT offers significant gains in access to the markets of other countries. Each offers gains that the other cannot provide.⁴³

II. FREE TRADE AGREEMENTS AT WORK

The FTAs formed since World War II have had mixed results. The more successful FTAs, such as the European Free Trade Association, tend to be among countries that are at comparable levels of development, are at more advanced levels of development, and are located in close geographic proximity.⁴⁴ The United States currently has FTAs with Israel and Canada. A review of these FTAs

40. *Id.*

41. *Id.* at 35.

42. Maureen A. Farrow & Robert C. York, *Regional Trade and Trends: A North American View from the Inside Out*, in *THE GROWTH OF REGIONAL TRADING BLOCS IN THE GLOBAL ECONOMY* 76, 86 (Richard S. Belous & Rebecca S. Hartley ed., 1990).

43. Countries who agree upon a regional trading arrangement such as an FTA are "able to make gains through bilateral negotiations that could not realistically be achieve[] through multilateral negotiations, no matter how successful they prove to be." For example an FTA can:

1. offer complete elimination of all tariffs, while the Uruguay Round calls for across-the-board cuts of only 35 percent;
2. eliminate many non-tariff barriers that have proved difficult to contain through the GATT;
3. include trade and many services and certainly with a greater degree of coverage than could be achieved through the GATT, where concessions must be balanced among all the major bargaining parties;
4. deal with specific trade disputes;
5. include trade related investment rules; and
6. create novel binational institutions to deal with trade disputes in general and countervail and anti-dumping cases in particular.

Id. at 86-87. It is hard to argue that these provisions could be obtained through multilateral negotiations. "The advantage of comprehensive bilateral agreements is that a gain in one sector can be balanced against a loss in another so that a net gain can be achieved by both parties." *Id.* at 87.

44. See generally Jeffrey J. Schott, *More Free Trade Areas?*, in *FREE TRADE AREAS AND U.S. TRADE POLICY* 1 (Jeffrey Schott ed., 1989).

reveals both strengths and weaknesses that should be kept in mind when drafting FTAs in the future.

A. *The United States-Israel Free Trade Agreement*

The United States-Israel FTA ("Israel FTA") was established in 1985.⁴⁵ It allows American producers and manufacturers to freely compete in Israel, while at the same time allow Israeli manufacturers unimpeded access to the U.S. market.⁴⁶

Prior to the implementation of the Israel FTA, the United States granted Israel preferential treatment on over ninety percent of Israeli imports which entered the United States duty free under the Generalized System of Preferences ("GSP") program. However, because of growing protectionism in the United States, Israel was concerned that it might lose access to the U.S. market. Therefore, Israel looked to the Israel FTA as a method of sustaining its favorable trading relationship with the United States.⁴⁷ The U.S. also looked favorably towards an Israel FTA in the hope that it would counterbalance Israel's FTA with the European Economic Community.⁴⁸

In order to qualify under the terms of the Israel FTA, a product must meet the rules of origin requirement. The requirement will be satisfied if the product is imported directly from the exporting country or from a third country, and as long as the product does not enter the commerce of the third country. The Israel FTA gradually eliminates tariffs over a ten year period and four separate classes were provided for products in which tariffs were reduced in stages.⁴⁹

Along with the reduction of tariffs on products, the Israel FTA also reduces non-tariff barriers and eliminates unduly burdensome import licensing requirements.⁵⁰ Both the U.S. and Israel are required to waive their "buy national" restrictions on government

45. Israel FTA, *supra* note 11.

46. Because of the deterioration of Israel's economy and massive capital flight between 1983 and 1985, Israel believed that the Israel FTA was a solution to its economic problems.

47. Sandra Ward, Note, *The U.S.-Israel Free Trade Area: Is It GATT Legal?*, 19 GEO. WASH. J. INT'L L. & ECON. 199, 200-01 (1985).

48. U.S. industry applauded the Israel-FTA because metal working, machine tools and many electronic components became duty-free when the FTA took effect. Duties on U.S. computers were reduced to those accorded the European Economic Community. Cherie Loustanaou, *U.S. Free Trade Area Agreement*, BUS. AM., Aug. 31, 1987, at 2.

49. *Id.* at 3. Each class has its own implementation schedule where duties are reduced in stages. Duties for products in class one were immediately reduced to zero; duties for products in class two reached zero on January 1, 1989; duties in group three will reach zero on January 1, 1995; and duties in group four will reach zero on January 1, 1995.

50. Israel FTA, *supra* note 11, art. 12 at 661.

agency purchases, with contract values over \$50,000, on all articles or services presently covered by the GATT Procurement Code ("GPC").⁵¹ Moreover, Israel agreed to sign the Subsidies Code of the GATT and eliminate its export subsidy programs on processed agricultural products and industrial goods within six years. Lastly, because of the international movement towards promoting liberalized trade in services, the Israel FTA incorporated a commitment by both countries to publicize laws or regulations that discriminate against a service exported by either country.⁵²

Along with changing domestic laws and regulations, the Israel FTA modifies the GATT as between the Israel and the United States.⁵³ For example, Article 5 of the agreement alters the application of the safeguards provision of GATT Article XIX and mandates consultations before either country can protect industries seriously injured, or threatened with serious injury by increased importation.⁵⁴ In addition, Article 10⁵⁵ limits Israel's GATT rights as a developing country to impose duties to protect its infant industries and Article 11⁵⁶ allows the U.S. and Israel to apply temporary restrictions upon serious balance of payments situations.⁵⁷ In spite of these modifications, the Israel FTA affirms the remaining provisions of the GATT⁵⁸ and provides that GATT provisions will prevail in the event of inconsistencies between the Israel FTA and prior agreements between the two countries.⁵⁹ The Israel FTA also provides for a dispute resolution mechanism to resolve disputes arising under the agreement and establishes a Joint Committee to supervise the agreement's implementation.⁶⁰

However, the Israel FTA did not achieve certain goals, such as the establishment of a bilateral panel to review U.S. application of countervailing duty⁶¹ and anti-dumping,⁶² or an exclusion from

51. *Id.* art. 15 at 662.

52. *Id.* art. 16 at 663.

53. Peters, *supra* note 10, at 503.

54. Israel FTA, *supra* note 11, art. 10 at 660.

55. *Id.*

56. *Id.* art. 11 at 660-61.

57. However, "acceptable countermeasures under the Israel FTA are more restrictive than those under articles XII and XVIII of the GATT." Peters, *supra* note 10, at 503.

58. Treaty of Friendship, Commerce and Navigation, Apr. 3, 1954, U.S.-Israel, 5 U.S.T. 550. *See also* Peters, *supra* note 10, at 503.

59. Israel FTA, *supra* note 11, art. 3 at 658. The Israel FTA also affirms the Israel-U.S. Treaty of Friendship, Commerce and Navigation, 5 U.S.T. 550. U.S. statutes, unless specifically altered, prevail in a conflict with the Israel FTA and such conflicting provisions of the Israel FTA are void. U.S.-Israel Free Trade Area Implementation Act of 1985, Pub. L. No. 99-47, 99 Stat. 82, 83. *See also* Peters, *supra* note 10, at 503.

60. The committee's resolutions are non-binding. Israel FTA, *supra* note 11, art. 19 at 664.

61. 19 U.S.C. §§ 1303, 1671-72, 1675-77 (1982).

62. 19 U.S.C. § 1673 (1982).

U.S. section 201,⁶³ which addresses "fair" foreign trade practices that adversely impact U.S. trade. These areas were addressed by the Canada FTA.

B. *The United States-Canada Free Trade Agreement*⁶⁴

The free trade negotiations between Canada and the U.S. were based on economic conditions both different and similar to those present during the Israel FTA negotiations. The conditions were different in that Canada is a much larger trading partner with the U.S. than is Israel.⁶⁵ The conditions were similar because, like Israel, Canada was growing increasingly dependent on the U.S. market for its exports and saw an FTA as a means of avoiding the possibility of increased U.S. protectionism.⁶⁶

The Canada FTA "regulates economic barriers . . . including tariffs, economic and investment irritants, and non-tariff barriers" between the parties.⁶⁷ Under the agreement, both countries are prohibited from increasing any existing customs duty except where the agreement allows for it.⁶⁸ The Canada FTA progressively eliminates, beginning January 1, 1988, customs duties on all goods originating in the other's territory.⁶⁹ The rules of origin provide the foundation for many of the Canada FTA provisions and are designed to ensure that the benefits of the Canada FTA are conferred only on goods originating in either Canada or the United

63. 19 U.S.C. § 2251 (1988).

64. The Canada FTA helped formalize the economic integration that had already began to emerge in North America. Stewart A. Baker & Shelly P. Battram, *The Canada-United States Free Trade Agreement*, 23 INT'L LAW. 37, 38 (1989).

65. The United States carries a trade deficit with Canada and nearly twenty percent of total U.S. imports are from Canada. Moreover, in 1987 the Canada-United States trading exchange was the largest in the world, totaling \$131.3 billion in merchandise and \$30.1 billion in services. Baker & Battram, *supra* note 63, at 38. Compare imports from Israel which are only .05 percent of U.S. totals. Jock A. Finlayson & J. Christopher Thomas, *The Elements of a Canada-U.S. Comprehensive Trade Agreement*, 20 INT'L LAW. 1307, 1309 (1986).

66. Leonard Waverman, *A Canadian Vision of North American Economic Integration*, in CONTINENTAL ACCORD: NORTH AMERICAN ECONOMIC INTEGRATION 31, 34 (Steven Globerman ed., 1991).

67. Baker & Battram, *supra* note 64, at 38.

68. Canada FTA, *supra* note 4, art. 401.

69. *Id.* art. 401.2. The customs duties are eliminated at three different rates depending on the type of goods involved. Duties on goods in Category A are completely eliminated by January 1, 1989. Category A includes Automatic Data Processing Equipment, Leather, Telephones, Motorcycles, Modems, Whiskey and Rum, Fur, Animal Feeds, and Unwrought Aluminum. Duties on Category B goods are removed in five annual stages commencing on January 1, 1989 and are completely eliminated by January 1, 1993. Category B goods includes Paper, Furniture, After-Market Automotive parts, Machines, Paints, Petroleum, Chemicals, Precious Jewelry, Explosives, and Subway Cars. Category C goods duties are eliminated in ten annual stages, eliminating duties by January 1, 1998. Category C goods includes Steel, Rubber, Agricultural Products, Tires, Textiles and Apparel, Instruments, Plastics, Wood Products, Appliances, Rail Cars, and Alcoholic Beverages. *Id.* annex 401.2.

States.⁷⁰ To allow a reasonable time to adjust to tariff changes and to mitigate the legislative opposition of interest groups, certain product sectors, including agriculture and automotive sectors, receive special consideration under the agreement.⁷¹ All bilateral tariffs will be completely eliminated by January 1, 1998.

Negotiators of the Canada FTA also made significant progress in the areas of technical standards,⁷² agriculture, energy,⁷³ automobiles,⁷⁴ government procurement, services, immigration,⁷⁵ investment issues,⁷⁶ cultural industries,⁷⁷ financial services,⁷⁸ and dispute settlements.

Although the Canada FTA could have achieved greater advances on government procurement issues, it establishes a precedent in the reform of government procurement practices for future FTAs. Under the agreement, Canada and the U.S. agree to eliminate their respective "buy national" restrictions on procurement of "eligible goods"⁷⁹ and to lower the GPC threshold.⁸⁰ These provisions allow for expanding markets open to U.S. and Canadian suppliers.⁸¹ In addition, the rights and obligations provided for by the GPC are incorporated, as modified by the Canada FTA, into the

70. Baker & Battram, *supra* note 64, at 38.

71. John A. Kazanjian & John W. Craig, *The Canada-United States Free Trade Agreement*, 16 INT'L BUS. LAW. 112, 113-14 (1988).

72. "The Canada FTA . . . prohibits the maintenance or introduction of federal technical standards for goods, processes, or production methods that would create 'unnecessary obstacles' to trade between the [two countries]." Baker & Battram, *supra* note 64, at 44; Canada FTA, *supra* note 4, art. 602, 603.

73. The Canada FTA reflects a significant commitment to grant the U.S. nondiscriminatory access to Canadian energy supplies and to grant Canada secure U.S. market access for Canadian energy exports. Baker & Battram, *supra* note 64, at 48.

74. "Automotive trade (completed vehicles and parts) is the cornerstone of the trade relation between the [U.S. and Canada]." Baker & Battram, *supra* note 64, at 50.

75. Under the Canada FTA, both countries "give reciprocal undertakings regarding temporary entry into each other's country by citizens of the other [country] . . . for business purposes." Baker & Battram, *supra* note 64, at 59; Canada FTA, *supra* note 4, art. 1501.

76. Both countries have agreed to accord "national treatment," with some exceptions, to each other's investors with respect to investment and to trade in goods and services. Canada FTA, *supra* note 4, art 105.

77. Cultural industries and foreign investment in Canada are not included in the Canada FTA. Baker & Battram, *supra* note 64, at 64; Canada FTA, *supra* note 4, art. 2005.1.

78. National treatment with respect to financial services was achieved only for insurance. Baker & Battram, *supra* note 64, at 66.

79. The Canada FTA defines "eligible goods" as unmanufactured materials mined or produced in the territory of either Canada or the United States, as well as materials manufactured in either country so long as the cost of the goods originating outside either country and used in the materials is less than fifty percent of the total cost of goods used. Canada FTA, *supra* note 4, art. 1309; *see also* Baker & Battram, *supra* note 64, at 55 n.122.

80. The threshold was lowered from \$171,000 to \$25,000. Kazanjian & Craig, *supra* note 71, at 114.

81. *Id.* at 114; *see also* Baker & Battram, *supra* note 64, at 54-55.

agreement.⁸² Unless otherwise specified, the agreement automatically incorporates any modifications to the GPC and, in the event of an inconsistency between the GPC and the agreement, the Canada FTA will govern.⁸³

The Canada FTA is the first comprehensive international agreement that adequately addresses trade in services between nations.⁸⁴ Moreover, it represents the first U.S. bilateral agreement to cover all current and future laws, regulations, and practices relating to financial institutions.⁸⁵ The limited services provisions are premised on the concept of national treatment.⁸⁶ By applying national treatment to services, both Canada and the U.S. agree not to discriminate between Canadian and U.S. providers of listed commercial services.⁸⁷ The scope of these provisions is limited to providers who are residents of Canada or the United States and allow for each country to continue to license and regulate covered services in relation to competence and ability.⁸⁸ Both countries are prohibited from introducing measures that require the commercial presence of a person from the other country as a condition of providing services, if such measures are a "means of arbitrary or unjustifiable discrimination" or are a "disguised restriction on bilateral trade in covered services."⁸⁹

Canada used the Canada FTA as a means of negotiating changes in dispute resolution methods in trade law. The negotiated

82. Canada FTA, *supra* note 4, arts. 1302, 1303; Baker & Battram, *supra* note 64, at 54.

83. Baker & Battram, *supra* note 64, at 54. For covered procurement, the Canada FTA requires that each country:

1. provide equal access to pre-solicitation information;
2. permit equal opportunity to compete in the pre-notification phase of the procurement cycle;
3. provide equal opportunity to potential suppliers and to be responsive to the procurement requirements in the tendering and bidding phase;
4. use decision criteria in all phases that best meet the requirements specified in the tender document and that are free from preferences;
5. give public notice of criteria in advance; and
6. promote competition by making information available on contract awards in the post-award phase.

Id. at 55; see also Canada FTA, *supra* note 4, arts. 1301-1309.

84. Baker & Battram, *supra*, note 64, at 57; Canada FTA, *supra* note 4, art. 1306.3. Services that are not included are transportation, basic telecommunications, legal services, doctors, dentists, child care, and services provided for by the government.

85. This allows U.S. financial institutions to acquire Canadian financial service firms and to compete on a more equal basis with their Canadian counterparts.

86. Baker & Battram, *supra* note 64, at 57; Canada FTA, *supra* note 4, arts. 105, 1402.1.

87. Canada FTA, *supra* note 4, annex 1408; see also Baker & Battram, *supra* note 64, at 57.

88. Canada FTA, *supra* note 4, art. 1403.1.

89. Baker & Battram, *supra* note 64, at 58 citing Canada FTA, *supra* note 4, art. 1402.8. If the U.S. lowers the barriers between the commercial banking and the securities industries, Canadian commercial banks will be given the same treatment and opportunities as U.S. commercial banks. Kazanjian & Craig, *supra* note 71, at 114.

agreement establishes a bilateral trade commission that will attempt to develop new rules and procedures for dealing with unfair pricing, government subsidies, and problems arising out of the implementation of the dispute settlement procedure.⁹⁰ In addition, unless both parties agree otherwise, the Canada FTA shifts the jurisdiction for judicial review of trade disputes from the U.S. and Canadian federal courts to a new binational panel.⁹¹

C. *What the Canada Free Trade Agreement Does Not Accomplish*

Canada and the U.S. are far from the comprehensive economic integration enjoyed by the European Community. In particular, there are a number of important issues not covered in the Canada FTA.

First, the Canada FTA is not an agreement liberalizing trade in all goods. Certain goods, such as agriculture, are only covered peripherally while trade in other goods is constrained⁹² or excluded.⁹³ Second, the Canada FTA is only the beginning of an agreement covering trade in services and certain services are explicitly excluded.⁹⁴ Third, in the investment area, services are excluded from: financial services, transportation, Crown corporations, and investment related to government procurement. Fourth, the Canada FTA does not liberalize trade in factors. In particular, labor movements are forbidden except for certain limited circumstances. Finally, the Canada FTA does not allow free movement of goods since each country can still impose contingent protection measures (countervail and anti-dump) against other's imports.⁹⁵

Because both the Israel FTA and the Canada FTA are enforced gradually over a period of several years, it is difficult to assess their effectiveness. Nevertheless, both FTAs may serve as models for negotiating an FTA involving all of North America.

90. Canada FTA, *supra* note 4, art. 1907; Baker & Battram, *supra*, note 64, at 72. The Commission will establish its rules of procedure, unless both countries agreed otherwise. Canada FTA, *supra* note 4, art. 1903.2.

91. Kazanjian & Craig, *supra* note 71, at 115. See also Baker & Battram, *supra* note 64, at 75-77. The constitutionality of this provision has been the subject of much debate in the United States. See Gilad Y. Ohana, *The Constitutionality of Chapter Nineteen of the U.S.-Canada Free Trade Agreement: Article III and the Minimum Scope of Judicial Review*, 89 COLUM. L. REV. 897 (1989); see also Baker & Battram, *supra* note 64, at 77-80.

92. One example is textiles. For an overview of the areas excluded from the Canada FTA, see Waverman, *supra* note 66, at 35-36.

93. One example is beer. *Id.* at 35.

94. These include basic telecommunications, transportation, culture, media, doctors, dentists, lawyers, and child care. Also, trade in other services is constrained since existing discrimination is grandfathered, i.e., financial services. *Id.* at 35-36.

95. *Id.*

III. NEGOTIATING A NORTH AMERICAN FREE TRADE AGREEMENT

A. *The Fast-Track Process*

The Trade & Tariff Act of 1984 authorizes the negotiation of tariff concessions with any other country that requests such negotiations.⁹⁶ Under the United States Constitution, the legislature has jurisdiction over tariffs.⁹⁷ Therefore, Congress must grant authority to the executive branch to begin free trade negotiations. After granting this authority, the legislature reserves the right to approve or reject the final FTA agreement, and to impose conditions ensuring that its opinions will be taken into account during the negotiations.

To facilitate an orderly framework for legislative involvement, a "fast-track" procedure has been developed.⁹⁸ The fast-track procedure gives Congress ninety legislative days⁹⁹ to approve or reject the entire text of the agreement once the countries have concluded negotiations.¹⁰⁰ At this point, no amendments, additions, or removals from the text of the agreement are permitted, thus preventing the agreement from being gutted and effectively killed. However, for the fast-track procedure to be used, the administration must allow sixty legislative days, prior to the beginning of negotiations, for the House Ways and Means Committee and the Senate Finance Committee to determine that they are not opposed to the beginning of negotiations.¹⁰¹

Statutory fast-track authority was set to expire June 1, 1993.¹⁰² The initial strategy adopted by U.S. opponents of a new North American free trade agreement was to oppose the extension of fast-track authority.¹⁰³ If extension of fast-track authority had been denied, the new treaty would have probably become bottled up in Congress for months as special interests mounted intensive efforts to amend or block specific provisions of the FTA. The Bush administration had expressed fears that such a process would effectively

96. 19 U.S.C.A. § 2112(b)(4)(A) (West Supp. 1991).

97. U.S. CONST. art. I, § 8, cl. 1.

98. The "fast-track" procedures are set forth at 19 U.S.C.A. §§ 2902-2903 (West 1991).

99. Legislative days are defined as days when both the Senate and House are in session. 19 U.S.C.A. § 2112(b)(4)(C)(i)-(ii) (West 1991).

100. 19 U.S.C.A. § 2903(a)(1)(A) (West 1991).

101. 19 U.S.C.A. § 2902(c)(3)(C) (West 1991).

102. 19 U.S.C.A. § 2903(b)(A) (West 1991).

103. Section 2903(b)(1)(B) provides for extension of fast-track authority as follows:

(B) . . . fast track procedures shall be extended to implementing bills submitted with respect to trade agreements entered into under section 2902 of this title after May 31, 1991, and before June 1, 1993, if (and only if) -

(i) the President requests such extension . . . and

(ii) neither House of Congress [disapproves of such extension]. 19 U.S.C.A. § 2903(b)(1)(B) (West 1991).

kill prospects for a free trade pact.¹⁰⁴ Moreover, Mexico indicated that it would have to reconsider whether to proceed with FTA negotiations if fast-track authorization was not extended. However, on May 23 and May 24, 1991, the House and Senate both agreed to extend fast-track authority to President Bush.¹⁰⁵

B. *Steps Required to Negotiate a Free Trade Agreement*

Including the fast-track procedure, the following steps are required to negotiate an FTA.¹⁰⁶ The U.S. must announce its intention of entering into an FTA.¹⁰⁷ Next, the U.S. administration must receive a formal letter from the foreign country that announces its intention to enter into an FTA with the United States.¹⁰⁸ The U.S. President must then notify the Committee on Finance of the Senate and the Committee on Ways and Means of the House of Representatives of the beginning of negotiations.¹⁰⁹ This starts a period of sixty legislative days of consultations with both Committees. Consultations must include: (1) the nature of the agreement, (2) how and to what extent the agreement will achieve the applicable purposes, policies, and objectives, and (3) implementation matters.¹¹⁰ After these initial formalities, the negotiations formally begin. Negotiations may take as long as necessary. When the parties to the FTA finalize negotiations, and at least ninety calendar days prior to signing, the U.S. President must notify Congress of intention to sign.¹¹¹ The final text of the accord must then be signed by the Presidents of each country as a final step to negotiations. The final agreement is then submitted to Congress and the fast-track process begins.¹¹² At the end of the ninety legislative days, Congress must produce a final vote rejecting or approving the FTA. The FTA enters into force following congressional approval, on the previously agreed date.

104. See generally *Ways and Means Trade Subcommittee 30-1, Hills-02/20/91*, Federal News Service, Feb. 20, 1991, available in LEXIS, Nexis Library, Omni File.

105. See H.R. Res. 146, 102nd Cong., 1st Sess. (1991).

106. See generally *International Reports, Mexico Service, Issue of the year: Free Trade Agreement*, January 2, 1991.

107. On June 11, 1990, the U.S. announced its intention to expand commercial relations with Mexico. Peter Jennings, *World News Tonight With Peter Jennings* (June 11, 1990) (transcript available in LEXIS, Nexis Library, Omni File).

108. This occurred August 21, 1990. See Ingrid Mohn, *U.S.-Mexico Free Trade Agreement Means Greater Mutual Prosperity*, BUS. AM., Oct. 8, 1990, at 4.

109. The President notified both committees on September 25, 1990. On February 5, 1990, the President sent the committees notice that Canada would participate in the negotiations. *White House Briefing Ways and Means Trade Subcommittee*, Federal News Service, Feb. 20, 1991, available in LEXIS, Nexis Library, Omni File.

110. 19 U.S.C.A. §§ 2902(d)(2)(A)-(C) (West 1991).

111. 19 U.S.C.A. § 2903(a)(1)(A) (West 1991).

112. *Id.* § 2903(a)(1)(B).

IV. LIKELY IMPACT OF A NORTH AMERICAN FREE TRADE AGREEMENT

Presidents Bush and Salinas have endorsed negotiations of an FTA that involves "the gradual and comprehensive elimination of trade barriers between the two countries, including: (1) the full, phased elimination of import tariffs; (2) the elimination or fullest possible reduction of non-tariff trade barriers, such as import quotas, licenses, and technical barriers to trade; (3) the establishment of clear, binding protection for intellectual property rights; (4) fair and expeditious dispute settlement procedures; and (5) means to improve and expand the flow of goods, services, and investment between the United States and Mexico."¹¹³

A. *Impact on Mexico*

1. *Mexico's fundamental goals*

Responding to the economic crisis of 1982, which was caused by prior bad economic policies, Mexico has recently made significant economic reforms.¹¹⁴ Mexico's current goal is to put these reforms into the "framework of a new economic policy regime which, among other things, will prevent the same mistakes from being committed in the future and will link Mexico to the dynamics of industrialized economies."¹¹⁵ Mexico's desire to integrate its economy, through an FTA, with that of the U.S. is consistent with these goals.¹¹⁶

Jamie Serra, Minister of Trade and Industrial Development in the Salinas cabinet,¹¹⁷ has explicitly set out the Mexican government's rationale and expectations for free trade and described the terms the government would pursue. Serra stated that Mexico seeks seven basic desirable characteristics of an FTA:

1. It must include liberalization of trade in goods, services and flows of investment compatible with the Mexican Constitution,
2. It must be compatible with the GATT,
3. It must eliminate tariffs among signatories at a gradual pace that assures an adequate transition period and avoids unsettling any sector of the Mexican economy,

113. BUS. AM., June 18, 1990, at 24, quoting The White House, Office of the Press Secretary, *Joint Statements by Mexico and the United States on Negotiation of a Free Trade Agreement*, June 11, 1990.

114. Rodelio Ramirez, *A Mexican View of North American Economic Integration*, in CONTINENTAL ACCORD: NORTH AMERICAN ECONOMIC INTEGRATION 1, 26 (Steven Globerman ed., 1991).

115. *Id.*

116. Rodelio, *supra* note 114, at 26.

117. Serra addressed the Mexican Senate on March 1, 1991 to open a new round of hearings on free trade with the United States. *Free Trade Progress Second Thoughts on FTA*, International Reports: Mexico Service, Mar. 13, 1991, available in LEXIS, Nexis Library, Omni File.

4. It must eliminate non-tariff barriers applied to Mexican exports,
5. It must negotiate rules of origin to avoid triangulation in trade, which would nullify the purpose of the FTA,
6. It must contain precise rules for avoiding the use of "distorting subsidies" that affect conditions of competition, and
7. It must include a specific chapter about dispute resolution with the objective of eliminating the vulnerability of Mexican exporters in the face of unilateral measures.¹¹⁸

2. *Advantages of a Free Trade Agreement for Mexico*

a. *Access to U.S. Markets and Employment Benefits*

The major advantage of an FTA to Mexico is that it would provide greater security to U.S. markets and reduce the chances of being locked out by U.S. protectionism. An FTA would also provide Mexico with advantages of access to the U.S. markets currently protected by tariffs and quotas.¹¹⁹ Moreover, guaranteed access to U.S. markets will "protect Mexico from harmful economic policy shifts in the United States and allow more efficient economic planning."¹²⁰

The increased U.S. investment and the opening of the U.S. market will also result in the increase of jobs in Mexico. Because of Mexico's critical unemployment and underemployment problems,¹²¹ an FTA is needed to help create many of the one million new jobs needed each year to keep up with Mexico's population growth. Also, a vibrant, growing Mexican economy would help prevent the flight of highly motivated, but low-skilled Mexican labor to the United States.¹²² The FTA would also disperse employment opportunities offered by the maquiladora program,¹²³ now

118. *Id.*

119. These U.S. trade barriers have the greatest impact on the textiles and apparel, steel and agricultural industries. Phase II, *supra* note 7, at 1-17.

120. Phase II, *supra* note 7, at 1-17, *quoting* Written Statement from Rep. Jim Kolbe, Before the Subcommittee on Trade, House Committee on Ways and Means (June 14, 1990), at 4.

121. Mexico had an estimated unemployment rate of 20% in 1989. Central Intelligence Agency, *The World Fact Book*, 206 (1990).

122. As an FTA increases economic opportunities and jobs in Mexico, illegal immigration from Mexico to the U.S. would likely decrease. "Mexico's objective is to export goods and services, not workers . . . a strong and stable Mexican economy will greatly diminish the crossings of Mexican workers to the United States, consequently diminishing many of the problems experienced due to illegal migration." Phase II, *supra* note 7, at 1-16, *quoting* Raul Rangel Hinojosa, written submission to the USITC. For an extensive look into how U.S. and Mexican economic policies effect Mexican immigration into the U.S. see Gregory C. Shaffer, *An Alternative to Unilateral Immigration Controls: Toward a Coordinated U.S.-Mexico Binational Approach*, 41 STAN. L. REV. 187 (1988).

123. The Mexican maquiladora or in-bond industries import merchandise and raw materials and process them immediately for export. The finished products are not intended for sale in Mexico and the Mexican government does not assess customs duties on them. A typical Maquiladora program involves twin plants operating on both sides

located almost exclusively near the border, to other parts of Mexico.

b. *Productivity and Competitiveness*

On June 11, 1990, Mexican President Salinas stated in an address to U.S. businesses, "[Mexico] must stress the significance of an FTA in raising the international competitiveness and well-being of our countries within the context of world change and particularly with regard to the formation of the European bloc and the economic cooperation of the Pacific Basin countries."¹²⁴ Jamie Serra has also stressed this point by stating that competitiveness was key to modernization.¹²⁵ He argues that the free trade area will help Mexico enhance its competitiveness and along with the climate of certainty that will be established, will stimulate investments, especially in those sectors that require long terms for maturity.¹²⁶

By encouraging production sharing and joint ventures, an FTA would permit Mexican companies to gain access to U.S. technology. Joint ventures with U.S. companies will also allow Mexico to develop expertise in international marketing and industrial techniques. Also, the elimination of Mexican domestic content requirements would render their industries more competitive because they would then be able to buy strategic, high quality components from the U.S. and other foreign sources. "An FTA would result in the adoption by Mexican companies of U.S. industrial methods and work ethics, similar to the skills learned by Mexican managers in maquiladora operations."¹²⁷

c. *Capital and Investment*

In addition to an increase in economic activity, an FTA would create an economic climate in Mexico which is more attractive to both foreign and domestic investors. "[B]y cutting tariffs and non-tariff barriers, protecting intellectual property and promoting for-

of the U.S.-Mexico border. The labor intensive portions are located in Mexico and the capital intensive portions are located in the United States. Most Maquiladoras are U.S. owned and concentrate in the manufacture of electric goods, textiles and apparel, furniture, and transportation equipment. See Shaffer, *supra* note 122, at 202.

124. Phase II, *supra* note 7, at 1-12, quoting Mexican President Carlos Salinas de Gortari, Address at the Business Roundtable, Washington D.C. (June 11, 1990).

125. According to Serra, a central advantage in forming an FTA is that it would provide an "ideal route for [the countries involved] to utilize their relative advantages, gain broader access to markets and exploit economies of scale, all of which strengthens productivity and increase capacity for internal development." *Free Trade Progress Second Thoughts on FTA*, International Reports: Mexico Service, Mar. 13, 1991, available in LEXIS, Nexis Library, Omni File.

126. *Id.*

127. Mexico would not seek sustained export success through low wages; this would be a formula for permanent underdevelopment. What Mexico seeks is an increase in productivity because this is the only way to raise wages in a non-inflationary manner. Phase II, *supra* note 7, at 1-18, quoting Sidney Weintraub, Written Statement before the Subcommittee on Trade, House Committee on Ways and Means, (June 14, 1990), at 8.

eign investment, Mexico will attract new flows of capital . . . new technologies [and] modern enterprises . . . [which] will improve the access of Mexican enterprises . . . access to international capital and debt markets."¹²⁸ These new developments will help make Mexico more competitive internationally by producing additional export opportunities.¹²⁹

An FTA will also stimulate large amounts of direct U.S. investment into the Mexican infrastructure, manufacturing, agricultural, computer, automotive, and service areas. Direct investment, which will likely be in the form of joint ventures, will make it possible for the larger Mexican export-oriented firms to compete internationally.¹³⁰

Finally, an FTA will help address Mexico's capital flight problem. It is estimated that over \$50 billion has left the country.¹³¹ If an FTA is successfully implemented, it would encourage the repatriation of this capital back into Mexico.¹³² When combined together with the considerable new investment that would result from the FTA, this "would produce a valuable source of private finance for development of the Mexican economy."¹³³

3. *Relief of Foreign Debt and Inflation Problems*

An FTA will sufficiently increase Mexican economic activity to allow it to generate more foreign exchange and help Mexico reduce its substantial foreign debt. The FTA, to the extent that it works as a lever for the reflow of Mexican capital, will benefit the commercial banks. With the exception of the crisis in the early 1980's,¹³⁴ Mexico has always been willing to service its debts. With the repatriation of flight capital, there will be enough resources to finance imports required for growth and pay interest payments on the external debt.¹³⁵ U.S. labor, however, is highly skeptical of this claim.¹³⁶

128. Phase II, *supra* note 7, at 1-18, quoting R. Herzstein, Co-Chairman of the Trade Subcommittee, Submission to the Mexico-U.S. Business Committee, (1990) at 3.

129. *Id.*

130. Phase II, *supra* note 7, at 1-18.

131. Phase II, *supra* note 7, at 1-18, quoting Gerard J. Van Heuven, Executive Vice-President U.S.-Mexico Chamber of Commerce to the Subcommittee on Trade, Written Statement to the House Committee on Ways and Means, (June 28, 1990), at 5.

132. *Id.*

133. *Id.*

134. The "crisis" refers to Mexico's 1982 recession. On August 20, 1982, mainly due to a substantial drop in oil export revenues, Mexico announced that it was out of cash and could no longer make payments on its \$75 billion in foreign debts. By the end of 1986, Mexico owed \$101 billion in debt. Priya Alagiri, Comment, *Give us Sovereignty or Give us Debt: Debtor Countries' Perspective on Debt-For-Nature Swaps*, 41 Am. U.L. Rev. 485, 487 (1992).

135. Phase II, *supra* note 7, at 1-18, quoting Rudiger Dornbush, Written Statement to the Subcommittee on Trade, House Committee on Ways and Means, (June 14, 1990), at 13.

136. "That the total new dollars flowing into Mexico due to the incentives of a FTA

The FTA will also help lower inflation. The broad liberalization measures undertaken during the 1980's by the Madrid and Salinas administrations have resulted in lower prices for Mexicans. These measures have forced domestic producers of tradable goods to price their products at prices which are competitive internationally. This, along with the macroeconomic changes in Mexico, has helped Mexico reduce inflation from nearly 200 percent in 1987 to less than twenty percent in 1989.¹³⁷

B. *Impact on the United States*

1. *Advantages of a Free Trade Agreement for the U.S.*

a. *U.S. Competitiveness*

A major advantage of an FTA with Mexico is that, if it is combined with the Canadian FTA, it will greatly enhance U.S. competitiveness in world markets. With growing international competition in the manufacturing and supply industries, the trade and investment liberalization resulting from an FTA would be very beneficial to U.S. industries.¹³⁸ Moreover, "an FTA with Mexico will offer U.S. industries competitive advantages vis-a-vis the other major trading blocks developing in the Far East and Europe . . . [and] will allow U.S. manufacturers to more thoroughly globalize their operations, thus making the manufacture of their products more cost effective and hence, more competitive."¹³⁹

An FTA would also be advantageous because the economies of the U.S. and Mexico are complimentary. Mexico with its younger labor force¹⁴⁰ and low wages excels in labor intensive industries. The U.S. excels in capital intensive, complex, research-intensive production. An FTA would therefore tend to produce specialization in both countries. One could expect a substantial expansion of labor intensive manufacturing exports from Mexico to the United States. These products would include textiles, clothing, leather goods, and lumber products because Mexico has the advantage in

will come anywhere close to solving Mexico's debt problem . . . is completely unrealistic." Phase II, *supra* note 7, at 1-18, quoting Jack Sheinkman, President of Amalgamated Clothing and Trade Textile Workers Union, Written Statement to the Subcommittee on Trade, House Committee on Ways and Means, (June 28, 1990), at 2.

137. D. Asman, *President Salinas on Mexico's Economy*, WALL ST. J., Apr. 4, 1990, at 14. The inflation rate of 20% is based on consumer prices. Central Intelligence Agency, *The World Fact Book*, 206 (1990).

138. Michael Habig, President of the Maquiladora Association of Reynosa, Mexico, Testimony at the USITC Hearing in McAllen, Texas, (July 19, 1990), at 63.

139. Phase II, *supra* note 7, at 1-12, quoting P. A. Jacobs, Market Strategies International, Written Submission to the USITC, (July 9, 1990), at 5.

140. It has been suggested that in the near future, the U.S., because of its aging population, will require the younger Mexican labor force for services and manpower. *Royal Bank Official Sees Limited Opposition to Canada's Participation in Mexico FTA Talks*, INT'L TRADE REP. (BNA) FEB. 6, 1991, AT 203.

these areas. Because these labor intensive areas are already declining in the U.S., they would tend to continue to become smaller and at the same time shift to specialty products. Once the, perhaps painful, adjustment to the economy had occurred, the efficiency gain in the U.S. would be of considerable magnitude.

b. *Mexico's 88 Million*¹⁴¹ *Consumers*

The principle advantage to an FTA with Mexico would be elimination of tariff and non-tariff barriers to U.S. access to the Mexican consumer market. Because U.S. exports to Mexico have increased significantly since Mexico began reducing its tariffs and liberalizing its imports regime,¹⁴² U.S. sales should increase even more dramatically under an FTA. However, it should be noted that although Mexico has a population of 88 million, the number of people who have the resources to purchase significant quantities of U.S. goods is estimated at less than 8 million.¹⁴³ Therefore, it is likely that it will be many years before Mexican per capita income rises to a level where the majority of the population can purchase significant quantities of U.S. goods, services, and agricultural products.¹⁴⁴ Thus, "[the] advantages in an FTA with Mexico are dynamic, and long term. The big gains will come from a future, well-developed United States-Mexican economy, with high wage and productivity levels which will jointly constitute a large, powerful market."¹⁴⁵

c. *U.S. Industry and Agriculture*

Many U.S. service sectors and industries would benefit from a Mexico-U.S. FTA.¹⁴⁶

These include computers and software, certain steel products, automobiles, pharmaceuticals, alcoholic beverages, telecommunications, processed foods, furniture, household appliances, paper,

141. Based on Mexico's population of 88 million. Central Intelligence Agency, *The World Factbook*, 205 (1990).

142. For a extensive analysis of Mexico's liberalization measures and their effect on U.S.-Mexico trade, See Sidney Weintraub, *A Marriage of Convenience: Relations Between Mexico and the United States* (1990).

143. Phase II, *supra* note 7, at 1-13.

144. In 1988, Mexico's Per Capita income was \$1,820 as compared to \$19,780 in the United States. *The World Bank Atlas*, 1989.

145. Phase II, *supra* note 7, at 1-13. It is estimated that "Mexico will have 100 million consumers before the year 2000. As Mexico's economy develops, its citizens will prosper, resulting in ever-increasing demand for consumer goods . . . as Mexico's industries develop, they will require materials, components, and inputs." *Id.* at 1-14, quoting The Business Roundtable, *Building a Comprehensive U.S.-Mexico Economic Relationship: Looking Towards the Future*, (June 1990), at 4.

146. Phase II, *supra* note 7, at 1-14, quoting Ambassador Carla Hills, United States Trade Representative, Testimony before the Subcommittee on Trade, Committee on Ways and Means, U.S. House of Representatives, (June 14, 1990), at 9.

transportation services and metalworking equipment.¹⁴⁷

Agricultural areas which are currently hampered by Mexican non-tariff barriers, and would significantly improve under an FTA are U.S. producers of dairy, livestock and poultry, deciduous tree fruits, oilseeds, grain and feed, and forest products.¹⁴⁸ If investment in areas currently restricted by the Mexican Constitution are also made part of the FTA, the U.S. financial services and petroleum/petrochemical sectors may also benefit.¹⁴⁹

d. *Development of the Border Areas*

An FTA with Mexico would benefit the economically depressed U.S. border areas currently faced with high unemployment levels. Along the Mexico-U.S. border, "an FTA could provide opportunities for both countries to expand commerce, create jobs, reduce unemployment, and increase income and retail trade."¹⁵⁰ A new FTA would likely bring a variety of new industries to the Mexico-U.S. border region. This will produce an area with rapid and progressive growth which will in turn attract many of Mexico's best and brightest young workers who must currently look elsewhere for suitable employment.¹⁵¹ Ideally, those who would come would include educators and those involved in service industries.¹⁵² "It should also make the region more attractive for travel and tourism and could well attract the attention of many national companies."¹⁵³

An FTA would also encourage the further development of an

147. *Id.*

148. Phase II, *supra* note 7, at 1-14.

149. Phase II, *supra* note 7, at 1-2, quoting Gary D. Nicholson, LTV Energy Products Company, Garland Texas, on behalf of Petroleum Equipment Suppliers Association Testimony at USITC McAllen, Texas Hearing Transcript, (1990), at 69-70.

150. Phase II, *supra* note 7, at 1-14, quoting Michael J. Blum, President, First City Bancorporation of Texas, Written Submission to the USITC, (1990), at 5.

151. Environmentalist foes of the FTA stress pollution concerns with the development of the Mexican side of the border area which offers less stringent environmental regulations. However, President Salinas has pointed out that Mexican government environmental spending has risen eight fold over the last three years and that his administration has shut down a "slew" of polluting factories and opened 44 parks in the area. Matt Moffett, *Salinas Goes on Tour to Push Free Trade: Mexican Leader Woos North American Support for Pact*, WALL ST. J., Apr. 15, 1991 at A10. However, the new action plan on environmental and labor issues in free trade negotiations with Mexico indicates that the U.S. and Mexico would pursue, parallel to the FTA negotiations, an ambitious program of cooperation on a wide range of environmental matters including the design and implementation of an integrated border environmental plan to address air and water pollution, hazardous wastes, chemical spills, pesticides and enforcement. *Action Plan on FTA Includes Plans for Worker Adjustment Program*, Daily Rep. Exec., May 2, 1991, available in LEXIS, Nexis Library, OMNI File. Bush promised environmentalists a voice in trade policy by appointing their representatives to a number of advisory committees. Karen Tumulty, *Bush Proposes Concessions on Free-Trade Plan*, L.A. TIMES, May 2, 1991, at A1.

152. Moffett, *supra* note 151.

153. Blum, *supra* note 150.

overburdened and outdated infrastructure along the Mexico-U.S. border. Problem areas include customs facilities, highways, and bridges. An FTA would help eliminate administrative paperwork and transportation delays which create bottlenecks on both sides of the border. Changes in these areas would expedite the movement of U.S. trucks into Mexico by eliminating the need to change drivers and cabs at the border.

e. *The U.S. Labor Market*

An FTA has the potential to create more U.S. jobs.¹⁵⁴ Although an FTA will probably encourage many U.S. manufacturers to move the labor intensive portions of their production process to Mexico as a competitive alternative to the Far East or other areas of low cost labor, it is likely that most of the equipment and components they use will be from the United States because of its proximity. Therefore, as the productivity of Mexico increases, so will the need for more U.S. supplied parts and equipment. This will in turn create more U.S. jobs. In addition, an FTA between the U.S. and Mexico will likely prompt Asian companies to increase their manufacturing processes in Mexico in an attempt to gain access to the U.S. market and again, because of proximity, they will also likely buy parts and components from the United States.¹⁵⁵

An FTA will also enable U.S. products to be marketed throughout Latin America. The Latin American market will create additional U.S. jobs as U.S. industry gains increased access to the large developing market in Mexico and also a "jumping off" point into the rest of Latin America. "The market in Latin America holds over 300 million people. While there is substantial disparity both in the various countries and between these countries and the United States, it is a young and growing market that the United States cannot afford to ignore."¹⁵⁶

154. Phase II, *supra* note 7, at 1-15, quoting Kenneth O. Lilley, President Association of Maquiladoras of Sonora, Written Submission to the USITC, 1 (1990); see also FTA Impact, *supra* note 19, at 2-6.

155. Phase II, *supra* note 7, at 1-15, quoting testimony of James Ebersole, Chairman, Border Trade Alliance, Commission Hearing in Las Cruces (1990).

156. Phase II, *supra* note 7, at 1-15 quoting Written Submission of P. A. Jacobs, Market Strategies International, to the Commission, (1990), at 5-6. "For instance, . . . the Association Latin Americana De Integracion, provides favorable trade conditions for Mexican-origin exports. This means that intermediate exports from the U.S. to Mexico, that are subject to processing or manufacture in Mexico may be eligible for preferential treatment in other South American markets. Consequently, Mexico has the potential to provide access to markets much greater than its own. Because Mexican-origin goods will be entitled to preferential treatment in these markets, the combined effect of a FTA with the U.S. will be an incentive for value added operations in Mexico, a significant benefit for U.S. companies." Phase II, *supra* note 7, at 1-15, quoting Gerald J. Van Heuven, Executive Vice-President U.S.-Mexico Chamber of Commerce to the Subcommittee on Trade, Address Before the House Committee on Ways and Means, (June 28, 1990), at 6.

U.S. labor strongly opposes an FTA with Mexico and contends that it requires a "quantum leap of faith" to conclude that a U.S.-Mexico FTA, as proposed by the Bush administration, would work to the benefit of workers in both countries.¹⁵⁷ Labor unions stress that an FTA will result in U.S. job losses as companies move their production to lower cost Mexico and accelerate the process of eliminating low-paying jobs in the United States. Members of the American Federation of Labor and Congress of Industrial Organizations (AFL-CIO) have argued that the potential of an FTA to create new jobs in the U.S. is vastly overrated and that the net effect will be a net loss in jobs. Thomas Donahue, AFL-CIO Secretary-Treasurer, has stated that the FTA, as proposed by the administration, "would be an economic and social disaster for U.S. workers."¹⁵⁸

U.S. labor also argues that an FTA will ultimately cause U.S. wages to fall. One expert has opined that although free trade between the U.S. and Mexico would increase total incomes in the United States, "it would also redistribute income away from unskilled and semi-skilled labor and toward professional and technical labor and capital. Because the 'winners' would be people whose incomes are already above average, while the 'losers' would start with below average incomes, this arrangement would make the distribution of U.S. incomes more unequal."¹⁵⁹

Government officials counter labor arguments by pointing out that labor cost is only one factor of production. Other factors such as industrial infrastructure, availability of services, raw materials, and supplier markets are very important in the investment decision and will mitigate any potential mass exodus of U.S. industry to Mexico.¹⁶⁰

f. *Permanent and Predictable Investment Environment in Mexico*

An important advantage of an FTA is that it would make the recent economic liberalization taken by Mexico permanent. If U.S. businesses had some assurances that the new Mexican regulations, which were put into effect through Presidential decree, were permanent and could not be easily changed by the next Mexican administration, U.S. investment in Mexico would likely increase.¹⁶¹ "International commitments such as an FTA, as well as the pro-

157. *Labor Leaders See Scant Benefit in Free Trade Pact With Mexico*, DAILY REP. EXEC., February 11, 1991, at A12.

158. *AFL-CIO Official Blasts Proposed FTA in Testimony Before Senate Finance Committee*, INT'L TRADE REP., Feb. 13, 1991, at 232.

159. Robert M. Dunn Jr., *Low-paid Workers Would Lose Even More in a Free-Trade Pact with Mexico*, WASH. POST, Aug. 1, 1990, at F3.

160. Phase II, *supra* note 7, at 1-21.

161. An FTA would codify and ensure the permanency of the Mexican reforms. According to Article 133 of the Constitution of the United States of Mexico, an international treaty, executed by the President of Mexico, ratified by the Mexican Senate, and

spective GATT accords, would help lock in domestic reforms instituted over the past five years that have substantially reduced Mexican trade barriers and liberalized regulations regarding foreign investment . . ."¹⁶² An increase in investment in Mexico would help raise wage incomes and employment in Mexico, increase GDP growth, increase foreign exchange earnings, and facilitate the transfer of technology. This would increase Mexico's demand for imports and, to the extent they are purchased from the United States, benefit the U.S. as well.

An FTA will also benefit U.S. investors if it establishes Mexican statutes and procedures which protect U.S. intellectual property rights. Although Mexico has recently made progress in this area,¹⁶³ many U.S. patent and trademark rights are not recognized or protected in Mexico.¹⁶⁴ If U.S. computer, software, and pharmaceutical sectors gained patent and copyright protection through an FTA, U.S. investment in Mexico would likely increase. Moreover, if an FTA further provided trade secret protection in Mexico, it would increase the opportunity of U.S. companies to invest in joint ventures with Mexicans.¹⁶⁵

C. *Canada's Role in the Mexico-U.S. Free Trade Agreement Negotiations*

On February 5, 1991, Canada announced that it would become a party in the negotiations toward a North American FTA.¹⁶⁶ The announcement sparked critical debate in Canada, not unlike that which accompanied consideration of the earlier Canada FTA. Although Canada may be sincere in its desire to expand its economic ties with Mexico, this goal is secondary to its desire to participate in any North American dialogue on trade and to preserve its rights under the Canada FTA.¹⁶⁷

not contrary to the Mexican Constitution, becomes supreme law of Mexico, having the same force and effect as all Mexican federal laws.

162. Phase II, *supra* note 7, at 1-16, quoting Jeffery J. Schott, *The Mexican Free-Trade Illusion*, INT'L ECON., June 1990, at 33.

163. See USITC Pub. No. 2275, Invest. No. 332-282, *Review of Trade and Investment Liberalization Measures by Mexico and Prospects for Future United States-Mexican Relations, Phase I: Recent Trade and Investment Reforms Undertaken by Mexico and Implications for the United States*, April 1990, at 6-1-6-15.

164. *Id.* at 6-10.

165. *Id.* at 6-16.

166. Mishra, *supra* note 6; Jennings, *supra* note 6.

167. Canada may wish to participate in the negotiations for the following reasons:

1. Mexico could develop into a competitor for Canada's share of exports to certain U.S. markets;
2. substantial trade and investment diversion would occur if Canada remained outside the agreement and the U.S. became the sole North American location with duty-free access to all three markets; and
3. the U.S.-Mexico agreement will likely expand into Central and South America and Canada needs to be part of the process.

1. *Areas of Interest to Canada*

A number of issues would be important to Canada in any attempt to broaden free trade in North America. These include:

- (1) Tariffs - any attempt to further lower duties would be of major importance,
- (2) Rules of origin - any North American agreement would require complex rules of origin governing the production of goods within the free trade area to ensure that goods or parts of goods produced outside the area are not accorded the same special tariff status as those produced within the area,
- (3) Energy - a very sensitive area for Mexico, and one in which Canada would want to be included,
- (4) Auto and auto parts - the U.S. and Canada auto industries are already very closely integrated and any change in the balance in this sector would be of considerable interest to Canada,
- (5) Textiles, clothing and footwear - this is an area where Mexico is likely to seek major concessions and where Canadian interests and concerns are similar to that of the United States,
- (6) Intellectual property rights - the area of Mexico's compulsory licensing for pharmaceuticals is deemed particularly important,
- (7) Standards - an area where progress under the Canada FTA is still pending,
- (8) Dispute settlement - a very important topic where concerns remain from the Canada FTA, and one which is anticipated to grow more complex because in the Canadian view the Mexican legal system is not synchronous with the more closely aligned Canadian and U.S. procedures for handling trade disputes.¹⁶⁸

V. BILATERAL OR TRILATERAL FREE TRADE AGREEMENT?

The new FTA could be negotiated either bilaterally, between Mexico and the U.S. alone, or trilaterally, involving all three countries.¹⁶⁹ The advantages and disadvantages of a bilateral or a trilateral agreement depends on each country's point of view. For each country, the advantages and disadvantages of the two types of agreements will be discussed below.

A. *Mexico's View*

Mexico can accomplish its goals through either a bilateral or trilateral agreement. If a bilateral agreement is negotiated with the U.S., Mexico will have tariff-free access to its largest market - the

For an excellent overview of Canada's position, see Waverman, *supra* note 66.

168. FTA Impact, *supra* note 19, at 3-2; see generally Waverman, *supra* note 66, at 56-62; Phase II, *supra* note 7, at 1-25-1-31.

169. A bilateral FTA would only include Mexico and the United States, a trilateral FTA would include all three countries; Mexico, Canada, and the United States. FTA Impact, *supra* note 19, at 3-1.

United States. If a trilateral agreement is negotiated among Mexico, Canada, and the U.S., Mexico gets the same access to the U.S. plus the additional benefit of access to the Canadian market. Moreover, a trilateral FTA will liberalize access for Canadian investment in Mexico. Therefore, although either type of agreement will be beneficial, there are greater advantages for Mexico if a trilateral agreement is negotiated.¹⁷⁰

Under a bilateral agreement, depending on the actual terms negotiated, Mexico would gain security of access to the U.S. markets in terms of limitations on the use of quotas and the national defense excuse for restricting trade. A bilateral agreement would also necessarily provide some type of dispute settlement mechanism. However, a trilateral agreement would not reduce security of access but probably increase access, because having three countries involved would enhance its importance. Secure access to the U.S. "market has been Canada's main objective in negotiating with the U.S., and it is the U.S. that is resisting any reduction of its powers under its trade and remedy laws and any weakening of its ability to act unilaterally to restrict access when *it* judges that the access results from 'unfair' practices."¹⁷¹

Bilateral negotiations between the U.S. and Mexico would probably be less complex than trilateral negotiations involving Canada. However, Mexico is inexperienced with international trade negotiations and observing Canada's tactics and techniques may provide Mexico with some helpful pointers concerning the negotiations. An additional benefit in having Canada involved is Canada's experience in specific negotiations with the U.S. administration and Congress. Canada's extensive expertise and institutional organization can assist Mexico at critical times in trilateral negotiations.

As mentioned above, if Canada is not included in the new FTA, Mexico forfeits the additional benefits of free trade with Canada. However, if involving Canada causes the trilateral negotiations to fail or delays completion of a Mexico-U.S. bilateral agreement, Mexico would lose the benefits of free trade entirely. Therefore, Mexico is more concerned with reaching an agreement with the U.S. than it is with adding Canada as a third member.¹⁷²

B. *Canada's View*

The Canada FTA gave Canada a preferred position in the U.S. market over any other country. Any similar bilateral FTA between

170. Richard Lipsey, *The Case for Totalitarianism*, in CONTINENTAL ACCORD: NORTH AMERICAN ECONOMIC INTEGRATION 89, 107 (Steven Globerman ed., 1991).

171. *Id.* at 108.

172. E. Andere, *Strategic Consideration is the Free Trade Agreement Given the Involvement of Canada*, THE MEXICAN ECON. MONTHLY REP., Sept. 1990, at 21.

the U.S. and any other country, whether or not it includes Canada, will remove Canada's advantage over that new country in the U.S. market. If the U.S. and Mexico sign a bilateral agreement, Canada will lose the preferred access it gained to the U.S. market through the Canada FTA and any advantages Canada has obtained over Mexico in the U.S. market will be removed.¹⁷³ However, a trilateral agreement that grants Mexico free trade in the U.S., would have the same results in Canada.

A bilateral FTA between the U.S. and Mexico will disadvantage Canada as a location for investment because Canada will be unable to offer Mexico tariff-free access to its markets as is offered by the United States. By adopting a trilateral agreement, Mexico, Canada, and the U.S. would share equal footing in attracting investors who desire to gain access to the entire North American Market.¹⁷⁴

C. *The U.S. View*

"With a [Mexico-U.S.] bilateral agreement, the U.S. gains the advantages of specialization according to comparative advantage in respect to the large part of its total international trade . . . with Mexico."¹⁷⁵ The U.S. also benefits from trade diversion vis-a-vis Canadian competition in the Mexican market.¹⁷⁶ However, the U.S. can also achieve these gains through a trilateral agreement and, therefore, the U.S. views either type of agreement as advantageous. A bilateral agreement, however, does give the U.S. one major advantage over that of a trilateral agreement. If the U.S. and Mexico sign an FTA, the U.S. would become the favored location for investment in the North American market because, when considered together with the Canada FTA, it would be the only country with tariff-free access to all three markets.¹⁷⁷ With a trilateral agreement, the U.S. would remain as an attractive location for investment to serve all three countries, however, it would not have the preferred status offered by two separate bilateral agreements.

If large free markets are preferred over small free markets, a

173. Lipsey, *supra* note 170, at 110.

174. *Id.*

175. "Comparative advantage is defined as the international advantage a country has in one industry relative to a second industry. Comparative advantage should not be confused . . . with absolute advantage [which occurs when] one country may have lower costs of production than another country in a specific industry." Waverman, *supra* note 66, at 41 n.7.

176. *Id.* at 109.

177. A bilateral agreement between the U.S. and Mexico would allow the U.S. to become the "hub" of the so called "hub and spoke" model. Under this theory, "only the U.S. has tariff-free access to [both Mexico and Canada]. The more spokes are added to the wheel, the more the preferred position of the U.S. is strengthened." As a result, the smaller spoke countries are limited in their ability "to combine to put collective pressure on the U.S. where that is appropriate." Lipsey, *supra* note 170, at 110.

trilateral agreement would serve these objectives better than a bilateral agreement. Adding Canada's economy to any agreement would promote faster growth in Mexico. Moreover, by not excluding Canada, the U.S. can avoid potential and likely backlash from the Canadian people.¹⁷⁸ "Initiating a movement towards a larger group of co-operating, equal partners is more likely to lead to favorable political reactions in the long run than making the U.S. the senior partner in a number of bilateral agreements negotiated on what others may come to see as a divide-and-conquer principle."¹⁷⁹

D. *The Proposed Trilateral Free Trade Agreement*¹⁸⁰

Although Mexico, Canada, and the U.S. have all agreed to participate in FTA negotiations, the countries have not yet decided whether a new bilateral FTA between Mexico and the U.S. will be negotiated or whether a trilateral FTA involving all three countries will be accomplished. If the United States has political and economic goals of creating conditions that will promote and maintain economic health, peace, and stability in North America, an organization of equals is required. With this in mind, a trilateral agreement is the better of the two choices. However, because the Canada FTA has too many delicately crafted compromises of give and take, it is unlikely that it could be amended in such a way that would avoid reopening debate in the U.S. and Canada, and Mexico would agree to become a signatory to it.

North American free trade requires a new agreement among Mexico, Canada, and the U.S. that will simultaneously: (1) preserve the existing Canada FTA intact, (2) provide for a trilateral FTA that will give the three countries the access to each other's markets, (3) settle potential issues between the U.S. and Mexico, and (4) provide a core agreement to which other countries could accede in the future.¹⁸¹

A "core" agreement, which would rely heavily upon the existing Canada FTA and which would provide for separate "temporary" trade agreements, can achieve the above goals. To be successful, the core agreement would need to be based on the principles of full free trade in both goods and services. These principles would be the end to which the actual free trade area would evolve when all sunset provisions or any temporary trade agreements had expired. The core agreement would need to cover free trade in goods and would most likely cover the liberalization of services and

178. For an analysis of Canadian political repercussions of a new FTA, see Waverman, *supra* note 66, at 54-60.

179. Lipsey, *supra* note 170, at 109.

180. This section relies heavily upon Lipsey, *supra* note 170, at 113-17.

181. *Id.* at 112.

investment. Any other country could then join the free trade area by acceding to the core agreement. Each new signatory would also have the opportunity to bargain for separate temporary trade agreements relating to special concerns with each or all of the existing members. The separate temporary trade agreements could be worked out country by country or with all the member countries as a whole. The temporary trade agreements could contain exceptions, phase-in allowances, adjustment provisions, and special cases. In virtually every case, these temporary agreements would be sunsetted rather than being permanent and would be kept to a minimum.

1. *The Core Agreement*

The core agreement should come from Chapters 1 through 6, 11, 14, 15, 17 through 19, and parts of 20 of the existing Canada FTA. However, limiting a core agreement only to these sections would probably cause considerable problems of both inclusion and exclusion.

Chapters 1 through 6 of the Canada FTA cover the introduction of objectives, definitions, rules of origin, border measures, national treatment, and technical standards. These six chapters provide the cornerstone of the Canada FTA for free trade in goods. These chapters have issues that would need to be worked out, however, and the complex rules of origin provisions would probably be the most difficult to resolve.

Chapter 11 on emergency actions is an important limitation to trade restricting measures. Because of Mexico's current economic condition, it will probably want to enlarge the scope of this chapter. However, any such measures would need to be clear sunset provisions and placed in a "temporary trade" agreement with the fundamentals of Chapter 11 being the ultimate goal after any negotiated transition period has expired.

Chapter 14 covers services. Although its coverage is limited, it provides an important step towards actual free trade and is nonetheless an important chapter. Moreover, one can argue that over time, the distinction between goods and services becomes blurred and "free trade in goods" should routinely come to be called "free trade in goods and services." As with Chapter 11, Mexico may initially resist including this chapter in the core agreement because of its current economic problems, but if sunset provisions were clearly drawn and the transition period was extended over many years, it would be possible to include it.

Chapter 15 provides for temporary entry for business persons. United States labor unions and those concerned about illegal Mexican immigration into the U.S. will probably make an issue out of

this provision if it is included in an FTA involving Mexico. However, this chapter of the Canada FTA was specifically drafted to establish clear criteria and procedures for facilitating temporary entry while, at the same time, ensuring security and protection of permanent employment for each other's labor forces.¹⁸² Therefore, the Chapter 15 provisions should provide a model framework for details to be worked out.

Chapter 17 on financial services involves sensitive issues that are not easily and willingly extended or accepted by others. Because both the U.S. and Mexico have greater restrictions over their financial sectors than does Canada, all that will likely be accomplished in this area is to obtain national treatment for any domestic deregulation that occurs in the financial services sector.

Chapter 18 covers dispute settlement procedures. Any new FTA should include similar provisions in the core agreement. It will be necessary for the provisions to cover disputes that arise out of the core agreement itself and also changes in national laws which affect the agreement. A difficult issue here is the special concessions made by the U.S. concerning the review of proposed U.S. legislation. The U.S. may be reluctant to extend this concession to countries other than Canada. However, in order to save the gains achieved under the Canada FTA, it may be necessary for the U.S. to extend Chapter 18 coverage to Mexico as well as future members of the FTA. If the U.S. does not agree, a core agreement will likely fail.

Chapter 19 covers binational panel dispute settlement in anti-dumping and countervailing duty cases. The U.S. and Canada decided on this procedure instead of agreeing to use the inept multilateral mechanisms provided by the GATT. This chapter was intended to be temporary while bilateral negotiations on a subsidy code take place. However, if these negotiations are not successful, Chapter 19 will likely become permanent. It will be difficult to extend Chapter 19 mechanisms to Mexico because, unlike the U.S. and Canada, Mexico does not have the procedure for determination by quasi-judicial bodies combined with appeals to higher courts.

Exclusions from the core agreement will cause their own special problems. Chapters in the Canada FTA which should be excluded from the core agreement and negotiated under a temporary trade agreement include: Chapter 7 on agriculture, Chapter 9 on energy, Chapter 13 on government procurement, Chapter 16 on investment, and Chapter 20 on cultural industries. These chapters in the Canada FTA have sensitive and painstakingly crafted provisions to which Mexico will not want to accede without significant revisions.

182. Canada FTA, *supra* note 4, art. 1501.

2. The "Temporary" Trade Agreements

The temporary trade agreements are where special interest groups in Mexico, Canada, and the U.S. will have their say about the new North American FTA. These temporary agreements will provide special concessions that will temporarily be made to each country. However, before this type of agreement is negotiated, the parties would first be required to decide whether the special concessions should be embodied in a single trilateral or separate bilateral temporary agreement. These problems will become more complex as more countries and the number of special concession increase.

CONCLUSION

Positive experience with the Israel and Canada FTAs together with current and probable future economic conditions, make it possible to predict that a trilateral North American FTA would be beneficial for Mexico, Canada, and the U.S. The United States would benefit from the new FTA through "trade creation resulting from reduced trade barriers, increased economies of scale for both U.S. and Mexican producers, lower prices for U.S. consumers, and greater competition in certain U.S. markets."¹⁸³ However, the net gain for the U.S. would probably be relatively small for two reasons. First, although Mexico has a population of 88 million, its economy is very small compared to the U.S. economy.¹⁸⁴ Second, because existing U.S. tariffs and non-tariff barriers are currently very low,¹⁸⁵ total elimination of them under a new FTA would have little effect on the bulk of U.S. imports.¹⁸⁶ The new FTA will affect individual industries and regions of the U.S. more than the economy as a whole. Industries currently protected by large tariff or non-tariff barriers will be the most adversely affected.¹⁸⁷ U.S. regions most affected are those which contain a high concentration of FTA impacted industries or those in which trade with Mexico represents an unusually large portion of its economic base.

The benefits of a new FTA for Mexico will be much greater than those for either the U.S. or Canada. This is because Mexico will be integrated into economies several times as large as its

183. FTA Impact, *supra* note 19, at 2-2. "The only loss to the national economy would be trade diversion resulting from part of the displacement of trade with third countries. *Id.*

184. In 1989, Mexico's GDP of \$187 billion was only 3.6 percent of the U.S. GDP. CIA, *The World Fact Book*, 206 (1990); see also FTA Impact, *supra* note 19, at 2-3.

185. "In all but a few sectors, both countries have relatively low tariff and non-tariff barriers to trade with each other, this limits the amount of trade liberalization possible." FTA Impact, *supra* note 19, at 2.

186. FTA Impact, *supra* note 19, at 2-3, quoting Sidney Weintraub, Statement to the USITC, (Nov. 21, 1990).

187. *Id.*

own.¹⁸⁸ The benefits will be both direct and indirect. Direct benefits include an increase in Mexican exports, imports, and investments, along with a concurrent rapid increase in economic growth. The indirect benefits will be a change in business and public attitudes towards Mexico and its changing world status.

Canada will benefit simply by retaining the gains it achieved with the Canada FTA and by developing closer economic integration in North American and ultimately within the hemisphere.

PHILLIP E. KOEHNKE*

188. Mexico's integration with the U.S. has been compared to Spain and Portugal's joining the EEC in 1986. FTA Impact, *supra* note 19, at 2-3, quoting Rudiger Dornbusch, Testimony before the Subcommittee on Trade, Committee on Ways and Means, U.S. House of Representatives, (June 14, 1990), at 7. Since that time Spain's GDP has grown annually near or above 5 percent. *Id.*

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