

A FRAMEWORK FOR RETHINKING NAFTA FOR THE 21ST CENTURY: POLICIES, INSTITUTIONS, AND REGIONALISM^a

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^a Paper authored by “Fresh Voices” selected by the Academic Committee of the Geneva-Georgetown 2017 Annual Conference on WTO Law, following a call for papers open to all scholars..

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Abstract

The 2016 U.S. presidential campaign made the North American Free Trade Agreement (NAFTA) a prime target in a heated and divisive debate that questioned the United States' participation in the international trading system. Though campaign rhetoric typically softens as a candidate takes office, this time may be different. President Donald Trump has called NAFTA “the worst trade deal ever negotiated,” and in May 2017 indicated his administration’s intent to renegotiate NAFTA.

NAFTA is certainly not perfect, as all international agreements are the product of various political compromises, but it is also not the disaster its opponents claim. NAFTA was a good deal when it was made, but it has become antiquated due to rapid changes in information technology and global supply chain integration. In addition, some of its provisions were innovative at the time, but experience has shown us where improvements are needed. As a result, a renegotiation should not be feared, but rather seen as an opportunity to reinvigorate and revitalize North American integration for a 21st century global economy.

In this paper, we highlight the new policy objectives the agreement can incorporate; discuss the institutional upgrades that can improve its functioning and reduce political friction; and consider how NAFTA could serve as a framework for thinking about trade agreements that come after it, much as it did when it made its debut. We argue that while there is no need to start a revolution in trade agreements through this renegotiation process, there is a real opportunity to upgrade those aspects of NAFTA that either do not work, are out of date, or could not have been imagined at the time the deal was originally negotiated. In doing so, we draw from recent innovations found in contemporary trade agreements, such as the Trans-Pacific Partnership (TPP), and the Comprehensive Economic and Trade Agreement (CETA), where appropriate. Overall, we conclude that while the challenges may be significant, and the context of the renegotiation a bit worrying, the opportunity to upgrade the NAFTA architecture should be welcomed.

I. Introduction

The North American Free Trade Agreement (NAFTA) came into force on January 1, 1994. At the time, it was the most cutting edge and comprehensive trade deal in the world. Building on the Canada-U.S. Free Trade Agreement (CUSFTA), NAFTA was the first trade agreement to include extensive disciplines on intellectual property rights, a dispute settlement mechanism specifically for trade remedies, as well as provisions on environment and labor. Beyond these legal and policy innovations, NAFTA lay the groundwork for a highly integrated regional economy, as it brought nearly all tariffs between Canada, Mexico and the United States to zero, either immediately or with phase-out periods. U.S. total trade in goods with Canada and Mexico was \$291 billion in 1993, and grew over 250% to \$1.1 trillion in 2016. As a destination for U.S. exports, Canada and Mexico rank first and second, respectively, buying 34% of total U.S. exports in 2016, and are also a major source of U.S. imports (24% of the total), ranking as the second and third largest import partners.⁴

Despite the economic expansion NAFTA set in motion, it has not been without criticism. NAFTA has been particularly controversial because it was the first trade agreement between two highly industrialized countries and one developing country member. This was one of the reasons why a labor side agreement was included by the Clinton administration, to allay fears over competition with cheap labor. The impact on workers has been a major sticking point, with some opponents claiming that NAFTA has led to substantial job losses in the United States.⁵ However, the consensus among economists has been that the impact of NAFTA on real wages has been close to zero, with concentrated effects on a few industries that were highly protected prior to NAFTA.⁶ Beyond the impact on workers, there have been a wide range of criticisms from groups across the political spectrum. Critics have raised concerns over the inclusion of investor-state dispute settlement, the lack of enforceability of the environment and labor side agreements, a race to the bottom on health and safety standards, and restrictions on discrimination in government procurement and services. The laundry list of complaints is long, and it has made NAFTA “a piñata for pandering pundits and politicians” during many election seasons in the United States.⁷

The 2016 U.S. presidential campaign was no exception, and it brought renewed focus to NAFTA, with candidate Donald J. Trump calling it “the worst trade deal ever negotiated.” He repeatedly blamed NAFTA for the loss of manufacturing jobs in the U.S. and promised to

⁴ M. Angeles Villarreal and Ian F. Fergusson, “The North American Free Trade Agreement (NAFTA),” Congressional Research Service (22 February 2017), p. 11, <https://fas.org/sgp/crs/row/R42965.pdf> (visited 13 April 2017).

⁵ See Robert E. Scott, “Heading South: U.S.-Mexico Trade and Job Displacement under NAFTA,” Economic Policy Institute (3 May 2011), and Dean Baker, “NAFTA Lowered Wages, as It Was Supposed to Do,” *The New York Times*, Room for Debate (5 December 2013) <http://www.nytimes.com/roomfordebate/2013/11/24/what-weve-learned-from-nafta/nafta-lowered-wages-as-it-was-supposed-to-do> (visited 17 May 2017).

⁶ One notable exception is a paper by Scott, Salas, Scott and Campbell (2006) which argue that NAFTA brought about significant job displacement, to the figure of 1 million U.S. jobs. However, the USITC noted that this study’s methodology departs from more commonly used estimations, because their calculations are based on changes to the bilateral trade balance since NAFTA was implemented, not on the size of the tariff reductions. Since a trade imbalance can be impacted by a number of other factors, the estimates may be overstated. See, De La Cruz et al. “The Impact of NAFTA on U.S. Labor Markets,” U.S. International Trade Commission (June 2014) <https://www.usitc.gov/publications/332/ec201406a.pdf> (visited 13 April 2017).

⁷ Robert Pastor, *The North American Idea* (New York: Oxford University Press, 2011) p.3.

renegotiate the treaty, or even withdraw completely if the terms of the new deal were not to his liking. Since he assumed the Presidency, however, his general complaints about NAFTA have not given way to a coherent vision of what to do about it. President Trump's advisors have not been entirely clear as to how they intend to fix NAFTA, or what they think the specific problems may be. The limited details that have been provided, thus far, point to a focus on developing more stringent rules of origin, new provisions on e-commerce, strengthening labor protections, changes to dispute settlement as it relates to trade remedies, changing government procurement rules to allow Buy America provisions, and, more generally, improving the trade balance.⁸ However, the specific negotiating objectives on each of these items remains uncertain. Both Canada and Mexico have indicated that they are open to renegotiation, but have also been clear that they view raising tariffs as extremely harmful, and that walking away from NAFTA entirely would do great damage to existing supply chains, particularly in autos.⁹ Commerce Secretary Wilbur Ross has indicated that the earliest start for negotiations is likely to be in the fall of 2017, and that the goal is to wrap up talks quickly. However, given the recent history of trade negotiations, that seems like a rather ambitious and unlikely goal.

Against this backdrop of uncertainty, the time is ripe to put forth ideas to reenvision NAFTA for the 21st century. At this stage, the Trump administration has not finalized its negotiating objectives, and may be open to considering its options (it has solicited public comments and has held a three day hearing). No trade agreement is perfect, and one as old as NAFTA could benefit from an update. So where do we begin? The most useful starting point may be the fundamentals of NAFTA. For many people, it is just a soundbite, a political term that signifies broader concerns, rather than an actual trade agreement. It stimulates emotion without offering much in the way of understanding what it does. Thus, in addressing a NAFTA renegotiation, we must unpack its core elements.

In this regard, as a framework to guide the renegotiation process, it may be helpful to emphasize several different aspects of NAFTA which could be revisited during a new negotiation. First, NAFTA is a set of shared policy objectives. For example, through NAFTA, Canada, Mexico, and the United States have, among other things, promoted free trade by reducing almost all tariffs to zero; committed to environmental cooperation; and decided on a high level of intellectual property protection. Second, NAFTA is a set of institutions. NAFTA has executive and legislative functions, through which new NAFTA law can be made and existing law implemented; and a judicial branch that interprets existing NAFTA law to resolve disputes. And third, NAFTA is a framework through which the parties carry out international economic relations. NAFTA creates a North American economic bloc that has both commercial and diplomatic functions, and this high level of integration requires regular cooperation in many issue areas. This regional approach to economic governance can be

⁸ Sarah Babbage, "BGOV OnPoint: What's at Stake in a Nafta Renegotiation (1)," Bloomberg Government (22 March 2017) <https://www.bgov.com/core/news/#!/articles/ON6M3U6JTSE8> (visited 17 April 2017). Andrew Mayeda, "Nafta Talks Likely Won't Begin Until Later This Year, Ross Says," Bloomberg (8 March 2017) <https://www.bloomberg.com/politics/articles/2017-03-08/nafta-talks-likely-won-t-begin-until-later-this-year-ross-says> (visited 5 May 2017).

⁹ Gary Gereffi, "NAFTA and Global Value Chains," Brookings Institution (28 April 2017) <https://www.brookings.edu/blog/future-development/2017/04/28/understanding-trade-relations-in-a-value-chain-linked-world/> (visited 5 May 2017).

contrasted with the multilateral WTO system, or with the more haphazard spaghetti bowl of proliferating bilateral agreements.

In this paper, we address each of these aspects of NAFTA, and argue that while there is no need to start a revolution in the content of trade agreements through this renegotiation process, there is a real opportunity to upgrade those aspects of NAFTA that either do not work, are out of date, or could not have been imagined at the time the deal was originally negotiated. To this end, we highlight the new policy objectives the agreement can incorporate; discuss the institutional upgrades that can improve its functioning and reduce political friction; and argue for maintaining NAFTA's regional character. In doing so, we draw from recent innovations found in recent trade agreements, mainly the Trans-Pacific Partnership (TPP), and the Comprehensive Economic and Trade Agreement (CETA), where appropriate. These agreements, it can be argued, reflect contemporary consensus on a way forward for international trade, and attempt to address several long-standing complaints about the regime that would benefit NAFTA if incorporated.¹⁰ We conclude with an acknowledgement of the challenges each of the parties will face during the negotiations, and support a pragmatic approach to negotiations, while cautioning against any radical transformations, or the inclusion of additional measures more akin to global governance that lay outside the purview of what trade agreements can realistically accomplish. With this in mind, we believe that renegotiating NAFTA presents a unique opportunity to update the agreement and revitalize North American integration for a 21st century global economy.

II. NAFTA's Policy Goals: Free Trade, and Somewhat Beyond

When it was originally designed, NAFTA was an innovative attempt to set policy in a number of areas. Some of these were core trade issues; some of these went further. Most notably, it brought almost all tariffs between the three countries to zero. It also took on several kinds of non-tariff barriers, including some services and procurement liberalization. Beyond removing protectionist barriers to trade, it also included provisions to protect intellectual property rights, and pushed for cooperation in labor and environmental matters. Opening up NAFTA will mean taking a fresh look at these policies, as well as considering whether additional policies should be included.

During a NAFTA renegotiation, one crucial aspect must remain unchanged: Zero tariffs. Tariff-free trade on most products between the three nations has led to an integrated North American production network. Undermining this economic structure would harm all three countries tremendously. Beyond tariffs, there are a number of key policy issues that could be discussed in the renegotiation, such as state-owned enterprises (SOEs), the technical barriers to trade (TBT) and sanitary and phytosanitary (SPS) chapters, services, and government procurement, to name a few. In this section, we highlight a few key issues that capture three major criticisms of NAFTA: the things it could not anticipate at

¹⁰ For instance, the TPP is considered a major step forward on environment and labor provisions, as well as on innovation in e-commerce and rules of origin, to name a few. The CETA is the first agreement to incorporate a regulatory cooperation chapter, and also to have provisions on sustainable development. It is also the first to "rethink" ISDS. It has been widely noted that all three countries intend to borrow heavily from these agreements, which is why we focus our attention on them instead of other initiatives.

the time, such as e-commerce; the chapters that need an update to better reflect the reality of trade today, such as regulatory issues and rules of origin; and lastly, areas with weak or non-existent enforcement, such as the labor and environment provisions. We address each in turn.

What NAFTA Could Not Anticipate: E-commerce

With the drafting of NAFTA taking place mainly in the 1990s, there are no rules that effectively address modern e-commerce and digital trade issues. At that time, these technologies were in their infancy, and thus the rules did not account for the special characteristics of this trade. In the ensuing decades, new business models based around online sales and other activities have proliferated. Amazon led the way in selling traditional goods over the internet, and later moved into the sale of digital books, music, television shows and movies. Google offered search engines, email, and online videos. And Facebook made social networking ubiquitous.

In the process of transforming old industries and creating new ones, these companies developed practices that affect, among other things, the privacy and speech rights of their users. In response, governments have created new regulations, some of which became impediments to trade and data flows. Because the leading companies in this field are often American ones, many of the regulations were imposed by other governments, with U.S. officials pushing for trade agreement rules that would constrain these regulations.

As an example, Facebook gathers data on its users and sells it to advertisers in order to offer more targeted advertising. In Europe, however, these practices have led to concerns about the U.S. government having access to the information of European Union (EU) nationals, and the United States and the EU have clashed over regulations that force companies to store this data in the EU, where it is more difficult for the U.S. government to access.

In recent years, a number of U.S. trade agreements have tried to push forward on this issue. The Trans Pacific Partnership (TPP) was the latest and most extensive effort. The TPP e-commerce chapter is sometimes portrayed as a broad effort to promote the “free flow of data.”¹¹ However, the reality is probably somewhat narrower in some ways, although broader in others. The chapter includes a mix of negative obligations that prohibit TPP parties from imposing trade barriers, and positive obligations that require the parties to undertake specific measures. It includes prohibitions of customs duties on electronic transmissions; prohibitions of restrictions on “the cross-border transfer of information by electronic means, including personal information, when this activity is for the conduct of the business of the covered person”; prohibitions of requirements that local computing facilities be used as a condition of doing business in the territory; and prohibitions against requiring the “transfer of, or access to, source code of software owned by a person of another Party, as a condition for the import, distribution, sale or use of such software, or of products containing such software, in its territory.”¹²

¹¹ Office of the United States Trade Representative, “TPP Chapter Summary: Electronic Commerce,” <https://ustr.gov/sites/default/files/TPP-Chapter-Summary-Electronic-Commerce.pdf> (visited 17 May 2017).

¹² TPP Articles 14.3, 14.11, 14.13, and 14.17.

With respect to the positive obligations imposed on governments, this chapter covers a number of regulatory areas. It requires parties to have "consumer protection laws to proscribe fraudulent and deceptive commercial activities that cause harm or potential harm to consumers engaged in online commercial activities." It requires that parties have a "legal framework that provides for the protection of the personal information of users of electronic commerce." And it addresses the issue of spam e-mails, requiring measures that limit the ability of companies to use spam.¹³

The enforceability and effectiveness of these provisions is open to question, as the scope of the obligations is uncertain and a variety of exceptions apply. Thus, the full impact of these e-commerce provisions will have to await application. Nevertheless, given the importance of e-commerce in the modern economy, some provisions along these lines are needed in a renegotiated NAFTA. A NAFTA renegotiation offers an opportunity to develop international e-commerce policies that can promote a freer flow of trade and data.¹⁴ It will take time for these rules to become effective, and their scope will continue to be fought over, but NAFTA, by incorporating the TPP chapter, can be a first step down this road.

Time for an Update: Non-Tariff Barriers and Rules of Origin

There are several aspects of NAFTA that could benefit from an update, but here we focus on two key issues that deal directly with current challenges to liberalization: non-tariff barriers (NTBs) and rules of origin (RoO). Though lowering tariffs in the global economy is still an important goal overall, for Canada, Mexico and the United States, this is not a significant issue (because of NAFTA). Instead, so-called "behind the border" measures -- statutes, regulations and other requirements -- that cumulate into a tyranny of small differences are where most of the remaining obstacles to trade lie.¹⁵ This is why "regulatory cooperation" chapters are becoming an increasingly common feature of new generation trade agreements. Rules of origin have also become a hot topic, not least because the proliferation of FTAs has led to the creation of overlapping and complex rules to determine whether or not products qualify for preferential duty rates. Furthermore, the fact that global production networks have ushered in a new reality in global commerce, which is that products are not just "made in" a particular country. Rather, parts and components or production processes can span several countries. Thus, a restrictive RoO regime impedes the full benefits of a truly global economy. Below we offer suggestions for how to deal with each of these issues.

¹³ TPP Articles 14.7, 14.8, 14.14.

¹⁴ Canada and Mexico can also take measures domestically to raise their *de minimis* thresholds for duty free shipments, something the U.S. did in 2016. Given the growth of online shopping, such reforms make practical sense to provide more choices of where to shop for consumers. Currently, the three countries have the following thresholds for international shipments: Canada (\$20), Mexico (\$300), and the United States (\$800). A low *de minimis* threshold increases the costs of purchases, by adding on additional taxes and duties that are usually not known until a package goes through customs; there can also be additional customs brokerage fees. It has been noted that the Canadian government spends more money on collecting these duties than the value of the duties themselves. For an overview of this topic, see McDaniel et al. "Rights of Passage: The Economic Effects of Raising the *de minimis* threshold in Canada," C.D. Howe Institute (23 June 2016) https://www.cdhowe.org/sites/default/files/attachments/research_papers/mixed/E-brief_Rights%20of%20Passage_June16.pdf (visited 17 May 2017).]

¹⁵ For instance, see: Thomas Cottier, "International Economic Law in Transition from Trade Liberalization to Trade Regulation," *Journal of International Economic Law* (2014) 17, 671–677.

Regulatory (In)coherence

Recent trade agreements have made regulatory cooperation a key focus of talks, and progress in this area has been noted as possibly contributing to the largest economic gains of modern trade deals. For instance, a 2009 study on the Transatlantic Trade and Investment Partnership (TTIP) found that a total elimination of non-tariff barriers could lead to a 2.5-3.0% increase in GDP.¹⁶ Though it is fair to say that many non-tariff measures are not actionable through cooperative efforts, the benefit of convergence is still substantial. As we have noted elsewhere, cooperation can take many forms, such as harmonization, mutual recognition, or equivalence, with each approach facing its own unique challenges.¹⁷

The NAFTA includes disciplines on Standards-Related Measures (Chapter 9) as well as Sanitary and Phytosanitary Measures (Chapter 7), and established working groups that “made modest progress,” with many of these groups halting meetings altogether because of a lack of domestic political support for regulatory reform efforts.¹⁸ A subsequent innovation by the NAFTA parties was the creation of two Regulatory Cooperation Councils in 2011, between the United States and Canada and between the United States and Mexico, which expanded on the existing working groups and created a forum for information exchange and cooperation on regulatory divergence.¹⁹ Though the U.S.-Mexico High Level Regulatory Cooperation Council has not made substantial progress on its outcomes, the Canada-U.S. RCC has had notable success.²⁰ Though regulatory cooperation has garnered much attention in the new generation of “comprehensive” trade agreements,²¹ nothing has yet come close

¹⁶ Koen G. Berden et al., ‘Non-Tariff Measures in EU-US Trade and Investment—An Economic Analysis’, European Commission, Directorate-General for Trade OJ 2007/S 180-219493 (11 December 2009), p. xviii http://trade.ec.europa.eu/doclib/docs/2009/december/tradoc_145613.pdf (visited 15 November 2013).

¹⁷ Lester, Simon, and Inu Barbee. “The challenge of cooperation: Regulatory trade barriers in the Transatlantic Trade and Investment Partnership.” *Journal of International Economic Law* 16, no. 4 (2013): 847-867.

¹⁸ Christopher Sands, “The case for a ‘mutual recognition’ deal with the US,” *Policy Options* (12 May 2017) <http://policyoptions.irpp.org/magazines/may-2017/the-case-for-a-mutual-recognition-deal-with-the-us/> (visited 12 May 2017).

¹⁹ Through annual work plans that initially covered 36 initiatives such as agriculture and food safety, transportation, environment, and cross-sectoral issues, the councils developed a forum for regular stakeholder input and collaboration across agencies. The Canada-U.S. RCC launched with 29 separate initiatives, while the U.S.-Mexico High Level Regulatory Cooperation Council began with 7 separate initiatives. See, Treasury Board Secretariat of Canada, “Joint Action Plan for the Canada-United States Regulatory Cooperation Council,” (15 April 2016) <https://www.canada.ca/en/treasury-board-secretariat/corporate/transparency/acts-regulations/canada-us-regulatory-cooperation-council/joint-action-plan.html> (visited 17 May 2017) and International Trade Administration, “U.S.-Mexico High-Level Regulatory Cooperation Council,” <http://trade.gov/hlrcc/> (visited 17 May 2017).

²⁰ For example, Health Canada and the Federal Drug Administration created a common electronic submission process that allows for a single application to both agencies for pharmaceutical and biological products; progress was also made in establishing mutual recognition of foreign animal disease zoning, as well as a joint review process for crop protection products. See, Treasury Board Secretariat of Canada, “Canada-United States Regulatory Cooperation Council Joint Forward Plan August 2014,” (15 April 2016) <https://www.canada.ca/en/treasury-board-secretariat/corporate/transparency/acts-regulations/canada-us-regulatory-cooperation-council/joint-forward-plan-august-2014.html> (visited 17 May 2017).

²¹ For an overview of challenges on regulatory cooperation in the TTIP, see: Alberto Alemanno, “The Regulatory Cooperation Chapter of the Transatlantic Trade and Investment Partnership: Institutional Structures and Democratic Consequences,” *Journal of International Economic Law* (2015) 18, 625–640 (2015), and Simon Lester and Inu Barbee. “The challenge of cooperation: Regulatory trade barriers in the Transatlantic Trade and Investment Partnership.” *Journal of International Economic Law* 16, no. 4 (2013): 847-867.

to the level of cooperation that has been achieved by the Canada-U.S. RCC. However, it is important to note that the structure of the RCC has generally remained ad hoc, as its mandate does not come from a specific provision in NAFTA, though it has benefitted greatly from high-level support.²² In fact, the 2014 Joint Forward Action Plan argues that high-level commitment is a necessary component of the success of these initiatives and also “provides needed strategic direction to advance regulatory cooperation.”²³

To date, there are only two trade agreements that include provisions resembling the work of the RCC: the EU-Canada Comprehensive Economic and Trade Agreement (CETA), and the TPP. Looking at the content of these agreements is a useful exercise for understanding the different forms a regulatory cooperation chapter can take. In the TPP, this is referred to as “Regulatory Coherence” (Chapter 25) and differs markedly from the aims of the RCC. In fact, the TPP provisions on regulatory coherence place a significant amount of emphasis on the harmonization of regulatory processes, not just substance, which can be termed “procedural-plus”²⁴ provisions.²⁵ Overall, the TPP regulatory coherence chapter is limited in scope, but ambitious for its developing country parties with regard to clarifying regulatory procedures and transparency. However, it is insufficient as a model for any NAFTA renegotiation on regulatory issues because Canada, Mexico and the United States have similar regulatory bodies and procedures, and each country is generally able to navigate the others regulatory process. In addition, the TPP regulatory coherence chapter does not make reference to the TBT, SPS, GATT 1994, and GATS agreements, which may indicate it is not building on the existing framework of regulatory cooperation, but rather creating something entirely different. Furthermore, its proposed Committee on Regulatory Coherence would only be obligated to meet every 5 years, which would certainly prevent regular progress and coordination at the level the Canada-U.S. RCC has witnessed, which meets every year.

The CETA is very different from the TPP, as it acknowledges that the scope of its regulatory cooperation chapter is also covered by the WTO TBT and SPS Agreements, the

²² The RCC owes much of its success to being elevated as a top priority during the 2011 North American Leaders’ Summit. It also did not hurt that the Obama administration made international regulatory cooperation one of its signature issues, as noted in a 2012 Executive Order, as well as its insistence on the inclusion of regulatory cooperation in both the TTIP and TPP. See: The White House, Executive Order Promoting International Regulatory Cooperation (1 May 2012) <http://www.whitehouse.gov/the-press-office/2012/05/01/executive-order-promoting-international-regulatory-cooperation> (visited April 12 2017), Simon Lester and Inu Barbee, “Will Regulations Sink EU-U.S. Free Trade?” *The National Interest* (15 October 2013) <http://nationalinterest.org/commentary/will-regulations-sink-eu-us-free-trade-9229> (visited 17 May 2017).

²³ Treasury Board Secretariat of Canada, “Canada-United States Regulatory Cooperation Council Joint Forward Plan August 2014,” (15 April 2016).

²⁴ Marc Busch and Krzysztof Pelc, “Yes, the TPP agreement is over 5,000 pages long. Here’s why that’s a good thing,” Monkey Cage, *Washington Post* (2 August 2016) https://www.washingtonpost.com/news/monkey-cage/wp/2016/08/02/yes-the-tpa-agreement-is-over-5000-pages-long-heres-why-thats-a-good-thing/?utm_term=.f68e17857127 (visited April 12, 2017).

²⁵ For example, Article 25.4.1 states that “regulatory coherence can be facilitated through domestic mechanisms that increase interagency consultation and coordination associated with processes for developing regulatory measures” and Article 25.4.2 recognizes that though the parties may have “differences in levels of development and political and institutional structures” their regulatory process should share “overarching characteristics.” These include regulatory review, consultations, public reporting, and good regulatory practices, such as regulatory impact assessment, notice and comment, and stakeholder input.

GATT 1994, the GATS, and the CETA chapters on TBT and SPS chapters of the CETA as well as four additional chapters.²⁶ The CETA regulatory cooperation chapter also focuses on future regulatory activity, and has a regulatory cooperation forum that is supposed to meet once a year. In addition, the CETA also includes sector-specific annexes for priority sectors, which is the only area for work on existing regulations. Information sharing and transparency are an important component of the CETA regulatory cooperation chapter, as they are in the TPP, but Article 21.4 provides a more specific list of regulatory cooperation activities the parties can engage in other than general good regulatory practice.²⁷ CETA is particularly innovative in its involvement of third parties in the regulatory cooperation forum, noting openness to business, industry and civil society groups, but also allowing for the participation of “other international trading partners” upon mutual consent of the parties.²⁸ In addition to addressing issues of transparency, this provision is an acknowledgement of the complexity of trade that requires the possible inclusion of other countries, which is an important step to avoid the creation of competing regional regulatory blocs.

Generally, CETA provides a fairly good template for regulatory cooperation, one that could work well for the three NAFTA countries.²⁹ In many ways, a chapter on regulatory cooperation could allow for the institutionalization of processes that have already been underway through the RCC so that past efforts retain their momentum and there is a clearer framework for future cooperation and engagement. This is particularly important because of the history of North American initiatives falling by the wayside shortly after much excited announcements at the North American Leaders’ Summits. It is worth emphasizing that regulatory cooperation should remain a voluntary exercise so as to preserve the right of countries to take regulatory measures they see fit. The CETA stipulates this clearly, and a similar provision should be included in any NAFTA regulatory cooperation chapter.³⁰

Another important consideration is to avoid duplication of processes that already exist at the multilateral level, such as the WTO Technical Barriers to Trade (TBT) Committee.³¹ This committee oversees the implementation of the TBT Agreement and provides a forum to discuss ongoing trade friction, as well as serving as a hub for notification of trade related technical barriers. Though it makes sense for the NAFTA partners to cooperate on their own where their interests align and such cooperation promotes the integration of the North American market, they must be cautious in ensuring that such

²⁶ Article 21.1 also makes reference to CETA chapter Nine (Cross-Border Trade in Services), Twenty-Two (Trade and Sustainable Development), Twenty-Three (Trade and Labour) and Twenty-Four (Trade and Environment).

²⁷ For instance, it notes bilateral discussions on regulatory governance, consulting/information exchange, sharing of non-public information, notice and comment, and providing sufficient standstill periods for responses from interested parties.

²⁸ See CETA Article 21.6.3.

²⁹ It could also be argued that the CETA regulatory cooperation chapter does not go far enough to address regulatory divergence in North America, and that an approach similar to the EU regulatory regime should be pursued instead. For instance, see: Inu Barbee, “Regulatory Convergence and North American Integration: Lessons from the European Single Market,” *Journal of International Service* (2012).

³⁰ See CETA Article 21.2.6.

³¹ On the potential role of the WTO to take a more prominent role in international regulatory cooperation efforts see: Thomas J. Bollyky and Petros C. Mavroidis, “Trade, Social Preferences and Regulatory Cooperation: The New WTO-Think,” *Journal of International Economic Law* (2017), 20, 1–30.

efforts do not simply create additional barriers to trade, by creating a separate North American regulatory framework. To the extent possible, the inclusion of third parties would be beneficial, and issues that could possibly be elevated to a multilateral setting should be proposed as such. A motto of regional where necessary, and multilateral where possible, could provide a guiding logic for these efforts.

Rules of Origin

Rules of origin requirements are set out in Chapter 4 of the NAFTA, with additional details on product-specific rules in Annex 401. NAFTA applies rules of origin based on three different calculation methods: a tariff shift, where a product undergoes a change in tariff classification; or regional value content, which calculates regional value by subtracting all non-originating inputs (which also requires a minimum percentage of local value-added for certain products); or a combination of both.

The Harmonized Commodity Description and Coding System (HS) is used to determine the changes in tariff classification of a given product. HS codes are broken up into 96 chapters (the 2-digit level), then into headings (4-digit level), and subheadings (6-digit level). For a product to be considered originating, it usually needs to undergo some form of *substantial transformation* in the country it is coming from. NAFTA RoO are particularly restrictive because they often require a change of heading and a change in chapter to qualify as originating. In fact, 54% of NAFTA tariff lines require a change in chapter to qualify for NAFTA preferences.³² For instance:

orange marmalade is classified under heading 20.07 while fresh oranges are 08.05. The specific NAFTA ROO for orange marmalade requires a chapter change. If fresh oranges from Brazil are transformed into orange marmalade in the United States, the orange marmalade is an originating good since a change from chapter 08 to chapter 20 has occurred.³³

Determining origin with regional value content utilizes two methodologies-- the transaction value method (requiring 60% NAFTA value added) or the net cost method (requiring 50% NAFTA value added).³⁴ Both are considered to be relatively strict methodologies to qualify for originating status. In fact, a study by Estevadeordal found that NAFTA has some of the strictest RoO requirements of any trade agreement.³⁵ The requirements are so stringent that in many cases companies will choose not to even bother

³² Estevadeordal, Antoni, and Kati Suominen. "Rules of origin in the world trading system," in *seminar on regional trade agreements and the WTO* (2003).

³³ Robert Kunimoto and Gary Sawchuk, "NAFTA Rules of Origin," Policy Research Initiative (June 2005), p. 4, <http://publications.gc.ca/collections/Collection/PH4-22-2005E.pdf> (visited 17 April 2017).

³⁴ Regional value content calculated using the transaction value method is: $RVC = \frac{TV - VNM}{TV} \times 100$ and the net-cost method is calculated as: $RVC = \frac{NC - VNM}{NC} \times 100$. Whereas TV is the transaction value of the good (adjusted to F.O.B. basis), VNM the value of non-originating materials used in production, and NC the net cost of the good. The percentage requirement for RVC using the transaction method is higher because a producer is able to count both costs and profits as originating.

³⁵ Antoni Estevadeordal, "Negotiating Preferential Market Access: The Case of the North American Free Trade Agreement," *Journal of World Trade*, 34 (2000).

figuring out how to qualify for NAFTA preferences and will opt to pay the MFN duty instead. For example, from 2009-2011 just a little over 50% of U.S. imports from Canada and Mexico claimed NAFTA origin preferences, which means that the rest simply resorted to MFN rates.³⁶

In addition to transformation and regional value content rules there are often *de minimis* requirements for specific products as well.³⁷ NAFTA includes yarn forward and fibre forward provisions that require use of North American yarns and fibres in the textile industry.³⁸ In addition, automobiles require at least 62.5% NAFTA originating components. Then there are the often seemingly arbitrary requirements, such as on tomato ketchup, which states:

that a change to ketchup (HS 210320) from imported inputs of any chapter except subheading 200290 (tomato paste) will confer origin. In other words, any ketchup made from imported fresh tomatoes will confer origin, but ketchup made from tomato paste imported from outside the area will not qualify for preferential treatment, even though the basic change of tariff classification requirement has been satisfied.³⁹

And all this just to shield Mexican tomato producers from their Chilean competition in tomato paste.⁴⁰

It should be clear at this point that RoO are complicated, and NAFTA's reliance on product-specific rules makes taking advantage of the preference scheme not only complex, but out of date with the reality of global supply chains. Though the Trump administration has signaled a preference for strengthening rules of origin, research suggests that stricter rules tend to raise production costs⁴¹ and may actually decrease regional value added.⁴² This is because a strict regional content threshold may not be tenable for many firms, and some will

³⁶ Maria Donner Abreu, "Preferential Rules of Origin in Regional Trade Agreements," World Trade Organization, Economic Research and Statistics Division (22 March 2013), p. 22, https://www.wto.org/english/res_e/reser_e/ersd201305_e.pdf (visited 13 April 2017).

³⁷ NAFTA Article 405 sets out a seven percent maximum of non-originating material on the transaction value of the good for it to be considered as "originating." Some products have higher thresholds. This is generally considered a strict *de minimis* threshold. In comparison, the TPP has a ten percent *de minimis* threshold.

³⁸ The basic rule in NAFTA is yarn forward, with specific fiber forward requirements for particular items, such as cotton and man-made fibers.

³⁹ Paul Brenton, "Preferential Rules of Origin," in *Preferential Trade Agreement Policies for Development: A Handbook*, pp.161-177 (June 2011), p. 163, <http://siteresources.worldbank.org/INTRANETTRADE/Resources/C8.pdf> (visited April 28, 2017).

⁴⁰ See, D. Palmetier (1997), "Rules of Origin in Regional Trade Agreements," in Demaret, P., J.F. Bellis and G. Garcia Jimenez (eds), "Regionalism and Multilateralism after the Uruguay Round: Convergence, Divergence, and Interaction, European Interuniversity Press, Brussels.

⁴¹ Portugal-Perez, Alberto, "Assessing the Impact of Political Economy Factors on Rules of Origin Under NAFTA," World Bank Policy Research Working Paper Series (February 1, 2009). Available at SSRN: <https://ssrn.com/abstract=1350683> (visited 13 April 2017).

⁴² Dan Ciuriak and Derk Bienen, "Overcoming low preference utilization in PTAs: Presumption of origin for small shipments," BKP Development Research & Consulting Trade & Development Discussion Paper No. 02/2014 (30 June 2014). Available at SSRN: https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2460648 (visited 13 April 2017).

find it more efficient to use non-originating materials and simply pay the MFN duties, if they are low; in contrast, high MFN rates increase regional preference utilization.⁴³

So what should be done with RoO in the NAFTA renegotiation? One of the most important things to fix is to move away from too many product-specific RoO and move towards a general regional value content method on the majority of tariff lines. To complement this, improved rules on cumulation are necessary to ensure that the entire region benefits from RoO preferences. Currently, though NAFTA provides for full cumulation in the calculation of regional value content, exporters still need to satisfy other origin criteria, such as a change in tariff classification (which differs by product).⁴⁴ As a result, NAFTA cumulation rules are quite restrictive. The CETA includes a provision on cross-cumulation which allows for components from countries with which the parties both have an FTA to count as originating.⁴⁵ This would also be a good way to begin untangling the “spaghetti bowl” of overlapping rules that have been created with the proliferation of bilateral FTAs.

The TPP also incorporates a newer methodology for calculating origin, based on the focused value method, which subtracts the value of non-originating materials that are outlined in product-specific rules. This is similar to the build-down method, but differs in that it does not take into account *all* non-originating materials used in production. This maximum content threshold method departs from current NAFTA practice of *de minimis* thresholds, and may be one way to reform RoO. Broadly speaking, utilizing a regional value content methodology that can be applied across a wide range of products, without having to satisfy additional requirements on substantial transformation, could significantly reduce the burden faced by SMEs in complying with preference criteria. The important thing to keep in mind in thinking about recrafting the RoO chapter is to find a way to make these rules as simple as possible, so as to facilitate, and not restrict, the use of NAFTA preferences. RoO are complicated and challenging to navigate, particularly for small businesses without the resources to make sense of how to qualify for preferential tariffs, who end up paying the higher MFN duties on their shipments. Currently, shipments that do not exceed \$1,000 are exempt from providing certificates of origin, but this value is quite low, and potentially limiting the growth of small business exports.⁴⁶ For this, and many other reasons, simplifying rules of origin should be a priority of the negotiators.

⁴³ For an overview of NAFTA RoO costs for firms see: Caroline Freund, “Streamlining Rules of Origin in NAFTA,” PIIIE Policy Brief (June 2017) <https://piie.com/system/files/documents/pb17-25.pdf> (visited 22 June 2017).

⁴⁴ Two notable conditions of accumulation in NAFTA: the net cost method must be used for conferring origin; and all non-originating materials must undergo a change in tariff classification, as listed in Annex 401 on product specific rules.

⁴⁵ See, Protocol on rules of origin and origin procedures, Section B, Article 3.

⁴⁶ This requirement is unchanged in the TPP (see Article 3.23). For an interesting reform proposal on adjusting the *de minimis* threshold on exemption from certificates of origin based on tariff revenues, see Dan Ciuriak, “Making Free Trade Deals Work for Small Business: A Proposal for Reform of Rules of Origin,” C.D. Howe Institute E-Brief (6 August 2015) https://www.cdhowe.org/sites/default/files/attachments/research_papers/mixed/E-Brief_212.pdf (visited 22 June 2017).

Strengthening Enforcement: Labor & Environment

The labor and environment side agreements were added to NAFTA by President Clinton, in order to convince reluctant members of his party to support the deal. Though they lack a strong enforcement mechanism, the North American Agreement on Labor Cooperation (NAALC) and the North American Agreement on Environmental Cooperation (NAAEC) were the first labor and environment provisions to be included in a trade agreement, and ushered in a new era in which “progressive” elements in trade agreements have grown in importance.⁴⁷

The NAALC outlines 11 principles on worker rights,⁴⁸ and was considered an important achievement as part of the first trade agreement between two highly industrialized states and one developing country. The fear of low-wage competition from Mexico was a major concern in pushing for the inclusion of the labor agreement. In addition, the NAALC did not create any new obligations or require the three governments to adopt any new laws to meet the 11 principles it set out. Instead, the governments committed to cooperative activities to improve labor conditions, while continuing to enforce their current labor laws. Theoretically, three of the 11 principles (child labor, minimum wage, and occupational health and safety), are enforceable through sanction; however, it is not clear how well this dispute process would function in practice, and no disputes have been heard thus far.⁴⁹

The NAALC has had mixed results. Many U.S. commentators have argued that Mexico still lags behind in worker rights,⁵⁰ which is one reason why enforceable labor provisions in TPP became a contentious issue between the U.S. and Mexico. In the end, Mexico was

⁴⁷ Some have argued that the “soft law” created by the inclusion of labor and environment provisions in trade agreements has not been sufficient, and that these disciplines should instead be incorporated into the WTO. For instance, Thomas argues that labor and environment obligations have just as much connection to trade as intellectual property rights do. see: Chantal Thomas, “Trade-Related Labor and Environment Agreements?” *Journal of International Economic Law* (2015) 18, 827–860.

⁴⁸ These include: freedom of association and protection of the right to organize; the right to bargain collectively; the right to strike; prohibition of forced labor; labor protections for children and young persons; minimum employment standards, such as minimum wages and overtime pay, covering wage earners, including those not covered by collective agreements; elimination of employment discrimination on the basis of race, religion, age, sex, or other grounds as determined by each country's domestic laws; equal pay for men and women; prevention of occupational injuries and illnesses; compensation in cases of occupational injuries and illnesses; and protection of migrant workers.

⁴⁹ Mary Jane Bolle, “NAFTA Labor Side Agreement: Lessons for the Worker Rights and Fast-Track Debate,” Congressional Research Service (October 2001), p. 5-7, http://digitalcommons.ilr.cornell.edu/cgi/viewcontent.cgi?article=1042&context=key_workplace (visited 8 May 2017). Vogt (2015) has noted that though countries have leverage to induce legislative reforms of labor laws before a trade agreement is ratified, the lack of enforceable labor provisions in many U.S. and EU trade agreements has led to little post-ratification reforms, with firms willing to take higher risks due to a lack of consequences for violations. See: Jeffrey S. Vogt, “The Evolution of Labor Rights and Trade—A Transatlantic Comparison and Lessons for the Transatlantic Trade and Investment Partnership,” *Journal of International Economic Law* (2015) 18, 827–860.

⁵⁰ See Barry LaSala, “NAFTA and Worker Rights: An Analysis of the Labor Side Accord after Five Years of Operation and Suggested Improvements,” *The Labor Lawyer*, Vol. 16, No. 3 (Winter/Spring 2001), pp. 319-348; Buchanan, Ruth, and Rusby Mariela Chaparro. “International institutions and transnational advocacy: The case of the North American Agreement on Labour Cooperation,” Available on SSRN (2008); Hufbauer, Gary Clyde and Jeffrey J. Schott, *NAFTA revisited: Achievements and challenges* (Washington DC: Peterson Institute, 2005).

supportive of the inclusion of enforceable labor provisions in the TPP,⁵¹ but insisted that “it would not make any of its labor reforms contingent on TPP, but instead would undertake reforms through its domestic process.”⁵² Others have noted that the NAALC has had the positive effect of generating increased information sharing among the three countries, so that they can better understand each other’s labor laws and labor market indicators, which is an important basis for any communication on these issues.⁵³

If turning this side agreement into an enforceable chapter within NAFTA is a priority for all three countries, then they could draw from their efforts in the TPP, which, building on other FTAs, filled the gaps left by the NAALC. In fact, the TPP chapter summary provided by the U.S. Trade Representative notes that “applying these standards to Mexico and Canada delivers on the President’s promise to renegotiate NAFTA.”⁵⁴ The TPP has the strongest worker protections of any trade agreement negotiated to date, and requires its parties to adopt the fundamental labor rights identified by the International Labor Organization (ILO) as part of their domestic law.⁵⁵ However, since the TPP is not in force, it is difficult to tell how this chapter will work in practice. On paper, though, it is certainly the most comprehensive chapter on labor rights in any trade agreement.

The NAFTA environmental side agreement, the NAAEC, was the first time environmental provisions had been included in a trade agreement. Though the objectives outlined in Article 1 of the agreement are quite broad and ambitious, the actual commitments are more limited in scope, and respect each country’s right to implement and enforce its own environmental laws on its territory, though it does encourage consideration of recommendations proposed by the Council of the Commission on Economic Cooperation (CEC), which meets once a year.⁵⁶ Two additional bilateral agreements were made between Mexico and the United States as well, the Border Environmental Cooperation Commission (BECC) to deal with specific environmental issues on the southern border, and the North American Development Bank (NADBank) which finances environmental and sustainable development projects.⁵⁷

The TPP environment chapter could provide an upgrade to the NAFTA environmental agreement, though it differs in its focus in some respects. The parties will need to decide whether to retain the current institutional structure of the CEC, and a hybrid approach might be needed, which includes a council, secretariat, and a joint public advisory committee. The TPP only provides for an Environment Committee “composed of senior government representatives, or their designees, of the relevant trade and environment national

⁵¹ M. Angeles Villarreal and Ian F. Fergusson, p. 29.

⁵² *Inside U.S. Trade*, “U.S., Mexico Continue Discussing Labor Reforms After TPP Conclusion,” (8 October 2015) <https://insidetrade.com/inside-us-trade/us-mexico-continue-discussing-labor-reforms-after-tpp-conclusion> (visited 23 May 2017).

⁵³ Mary Jane Bolle, p.11.

⁵⁴ Office of the United States Trade Representative, “TPP Chapter Summary: Labor,” p.8, <https://ustr.gov/sites/default/files/TPP-Chapter-Summary-Labour-1.pdf> (visited 17 May 2017).

⁵⁵ These include: (1) freedom of association; (2) the right to bargain collectively; (3) freedom from forced labor; (4) freedom from child labor; and (5) freedom from discrimination in employment.

⁵⁶ See, for instance, NAAEC Article 2. The council is made up of “cabinet-level or equivalent representatives” and is the governing body of the commission (NAAEC Articles 9.1, 10).

⁵⁷ These two organizations were supposed to merge following an agreement by their two Boards, but this had not yet happened. Canada declined to join the NADBank.

authorities” that is scheduled to meet every two years.⁵⁸ In contrast, the CEC Council meets once a year (which functions like a “Board”), and the Secretariat (which supports the Council) has an Executive Director that rotates every three years, with a permanent staff at the headquarters in Montreal.

Due to the shared environmental challenges of the NAFTA partners, particularly as a result of sharing two of the world’s largest borders, it is hard to see why the current governance structure of the CEC should be substantially changed. One of the innovations of the NAAEC is that it established a forum on cooperation across all environmental issues of shared concern, not just specifically trade related. In fact, this enabled the 2014 initiative announced at the North American Leaders Summit to preserve the monarch butterfly, which migrates across all three countries.⁵⁹ Despite its achievements, the CEC has faced numerous challenges, and there is certainly much room for improvement. A 10-year independent assessment of the body noted that there is much to be done on clarifying its mandate, increasing public participation, improving transparency, and developing clear and deliverable work plans.⁶⁰

It is not entirely clear that the TPP model would be fully adequate or specifically address North American concerns, so it is probably prudent to incorporate only those provisions that all parties agree are necessary to advance their environmental interests. For instance, it may be worthwhile to include provisions for cooperation on trans-national environmental threats, trade in endangered species, illegal fishing practices, and increased transparency in rulemaking.⁶¹ All but the first are included in the TPP (20.17, 20.16, 20.7). In addition, it is not clear that dispute settlement is required under a new environmental chapter. The 2004 CEC assessment noted that:

Relatively few trade and environmental concerns have arisen...none of which have threatened to take the form of a government-to-government NAFTA trade dispute as referenced in Article 10(6). In the case of NAFTA bilateral trade disputes with a secondary environmental dimension (United States-Canada softwood lumber, United States-Mexico trucking), the environmental aspect has not been integral to the legal arguments in the trade dispute....⁶²

However, it is likely that some form of dispute settlement will find its way into the agreement. Canada’s Ambassador to the United States, David MacNaughton, stated that Canada would borrow from the CETA trade and environment chapter in NAFTA renegotiations,⁶³ which hints towards a desire for stronger enforcement. The report does go

⁵⁸ See TPP Article 20.19.

⁵⁹ Tim Johnson, “NAFTA leaders agree to protect monarch butterfly,” *The Star* (20 February 2014), https://www.thestar.com/news/world/2014/02/20/nafta_leaders_agree_to_protect_monarch_butterfly.html (visited 12 April 2017).

⁶⁰ Pierre Marc Johnson et al., “Ten Years of North American Environmental Cooperation,” Ten Year Review and Assessment Committee to the Council of the Commission for Environmental Cooperation (5 June 2004), p. 5, http://www.cec.org/sites/default/files/documents/reviews/7287_TRAC-Report2004_en.pdf (visited 12 April 2017).

⁶¹ M. Angeles Villarreal and Ian F. Fergusson.

⁶² Pierre Marc Johnson et al., p. 24.

⁶³ He also noted that Canada would likely borrow from the labor provisions in CETA as well. See, Josh Wingrove, “Trump Warms to North America Trade ‘Fortress,’ Canada Envoy Says,” *Bloomberg* (15 June 2017)

on to note that a clearer obligation of the NAFTA Free Trade Commission to consult with the CEC on environmental matters would be useful. Without clear guidance on policy objectives and priorities, however, the CEC will continue to struggle in producing major results, though it can achieve smaller goals at present. Regardless, it is apparent that more consultation between the bodies would be useful, but more for utilizing the environmental network facilitated by the CEC to assist in providing information should a dispute arise in which environmental concerns are part. It is entirely possible that the work of the CEC could foreseeably be subsumed within the NAFTA Secretariat (discussed in more detail below), and that this could potentially alleviate any communication concerns. This latter option may be ultimately preferable, as the U.S. Environmental Protection Agency is responsible for not only the U.S. financial contribution to the CEC funding pool, but also for coordinating efforts with its Canadian and Mexican counterparts. With potential cuts to funding of the U.S. EPA,⁶⁴ consideration must be given to how the work of the CEC could continue.

III. Institutional Upgrades

NAFTA, along with its predecessor CUSFTA and later offshoots like the US-Canada and US-Mexico regulatory cooperation councils, has been a source of wide ranging institutional innovation in trade governance. New bodies, both permanent and ad hoc, have been established to oversee the functioning of North American trade and investment, and related issues. These consist of institutions related to dispute settlement, as well as institutions created for the overall governance of the agreement. To this end, NAFTA has three separate dispute settlement processes (Chapter 11, Chapter 19, and Chapter 20) with panels or tribunals to hear claims; it has special commissions to examine labor and environmental concerns; it has a Secretariat that is housed within national government agencies; it has a Free Trade Commission to monitor the overall functioning of the agreement; and it has special bodies for addressing regulatory issues. There are also institutions outside of NAFTA, but related to the concerns of the three countries, such as inter-parliamentary groups and the North American Development Bank, that could also play an important role in a revised NAFTA. Any renegotiation of NAFTA must evaluate the effectiveness of these institutions and mechanisms, to see how they have stood the test of time and whether they need updating.

Dispute Settlement

Dispute settlement in international trade agreements typically involves ad hoc panels of experts who hear claims from either governments or private actors. These panels act as the judicial arm of the international trading system. The degree of enforceability in a dispute process varies depending on the design of the system. There are three main types of dispute settlement in NAFTA, all of which have experienced problems or come under criticism: The core dispute procedures for state to state complaints in Chapter 20; the special trade

<https://www.bloomberg.com/news/articles/2017-06-15/trump-warms-to-north-america-trade-fortress-canada-envoy-says> (visited 22 June 2017).

⁶⁴ Coral Davenport, "Trump Budget Would Cut E.P.A. Science Programs and Slash Cleanups," *The New York Times* (19 May 2017) https://www.nytimes.com/2017/05/19/climate/trump-epa-budget-superfund.html?_r=0 (visited 26 May 2017).

remedy review procedures in Chapter 19; and the investor-state dispute procedures in Chapter 11. We address each in turn.

Chapter 20 (State-state dispute settlement)

The core NAFTA dispute settlement procedure was carried over from the CUSFTA. At the time these provisions were drafted, GATT dispute settlement was the state of the art for trade disputes, and CUSFTA/NAFTA dispute provisions were written with the GATT as the main source of experience. GATT dispute settlement was updated during the Uruguay Round, with the creation of the WTO and its DSU. However, the various refinements included there, such as an appeals mechanism and an interim report, were not part of NAFTA (final drafting of the dispute section of NAFTA was completed a couple years before the WTO).

In the early years of NAFTA, there were three disputes that proceeded all the way through the process, from initial complaint to panel report to implementation.⁶⁵ Implementation of the last one, related to trucking services, has been a challenge, but some progress has been made. However, in the late 1990s, Mexico brought a complaint against U.S. barriers to trade in sugar, and flaws were exposed in the panel composition process, as the United States blocked the panel from being set up.⁶⁶ At the WTO, if the parties cannot agree on panelists, the Director-General can step in and appoint a panel. In NAFTA, by contrast, there is no such possibility.

More recent trade agreements have set out a detailed process that helps ensure that parties cannot block panels in this way. The TPP's approach to the problem is very thorough in this regard.⁶⁷ CETA also makes important innovations in this area.⁶⁸ These provisions may indicate that countries are aware of these issues, and have attempted to address them. The TPP and CETA provisions could be a good source of inspiration for improved NAFTA dispute rules.

⁶⁵ Scholars have identified up to 11 complaints in total. See, David A. Gantz, "Dispute Settlement under the NAFTA and the WTO: Choice of Forum Opportunities and Risks for the NAFTA Parties." *American University Int'l L. Rev.* 14 (1998): 1025; Gary Clyde and Jeffrey J. Schott, Hufbauer, *NAFTA revisited*.

⁶⁶ This problem was described by Mexico in its submissions in a related WTO dispute (Panel Report, *Mexico – Tax Measures on Soft Drinks and Other Beverages*, WT/DS308/R, adopted 24 March 2006, as modified by Appellate Body Report WT/DS308/AB/R, DSR 2006:I, p. 43). Mexico argued: "The uncontradicted evidence is that it has been almost five years since Mexico requested the formation of an arbitral panel under NAFTA Chapter Twenty and that the United States refused to cooperate in naming arbitrators. The United States even gave instructions to its NAFTA Secretariat Section to abstain from appointing them," and "The US has provoked an unfair interaction between the NAFTA and the WTO Agreement, resulting from the automatic operation of the WTO's DSU and Chapter Eleven of the NAFTA, and the corresponding lack of automaticity in the operation of NAFTA's Chapter Twenty, due to the US refusal to appoint panelists in a proceeding that presently requires the good faith and cooperation of both disputing Parties." (paras. 4.398 and 4.475). See also: Joost Pauwelyn, "Adding Sweeteners to Softwood Lumber: The WTO–NAFTA "Spaghetti Bowl" is Cooking" (2006)." *Journal of International Economic Law* 9: 197.

⁶⁷ TPP Article 28.9. See Simon Lester, "Can TPP Dispute Panels Be Blocked?", *International Economic Law and Policy Blog*, 12 June 2017.

<http://worldtradelaw.typepad.com/ielpblog/2017/06/can-tpp-dispute-panels-be-blocked.html>

⁶⁸ CETA Article 29.7.

Chapter 19 (Binational panels for AD/CVD)

During the Canada - U.S. trade negotiations in the 1980s, one of the big concerns for Canada was effective oversight by U.S. courts of certain trade remedy decisions by U.S. trade agencies. U.S. courts were seen as biased in favor of positions favorable to domestic industries. To address this issue, Canada and the United States agreed in the CUSFTA to a special review process, through which parties to trade remedy proceedings could appeal agency decisions to a special bi-national panel, made up of experts from both countries, rather than to a domestic court. When the CUSFTA was brought into NAFTA, the bi-national panel process was extended to that agreement, and is found in Chapter 19.

Over the years, U.S. industry groups have objected to this process, and have filed several claims in U.S. court arguing that the U.S. Constitution does not allow international panels to interpret and apply U.S. law in this way. None of those challenges were fully resolved by the courts on their merits, however, and the question of constitutionality remains uncertain.⁶⁹ Early indications are that one of the major U.S. demands for renegotiating NAFTA will be to remove or scale back Chapter 19. Canada and Mexico are likely to resist such a proposal, either because they see value in the procedure, or in order to ask for something else in exchange.

In terms of the usefulness of Chapter 19, it is worth noting that it is invoked much less frequently now than it was in its early years,⁷⁰ and that there is a somewhat effective alternative to challenge trade remedies at the WTO (more effective than the GATT was in the 1980s, when Chapter 19 was developed).⁷¹

Chapter 19 remains an anomaly, never having been duplicated in other trade agreements. Removing it might be the kind of "tweak" that could be marketed by the Trump administration as a significant change, while not fundamentally altering the economic integration established by the NAFTA. At the same time, Canadian business groups strongly support the mechanism,⁷² as they view it as crucial to address important cases such as softwood lumber, and they will not part with it lightly.

1. ⁶⁹ Jeanne J. Grimmatt, NAFTA Binational Panel System: Second Constitutional Suit Dismissed, 10 February 1998.

⁷⁰ "List of all NAFTA/CUSFTA Chapter 19 and ECC Decisions," WorldTradeLaw.net, <http://worldtradelaw.net/databases/naftastats.php> (visited 17 May 2017).

⁷¹ In terms of its actual impact on domestic trade remedy decisions, one scholar has suggested that through 2005, Chapter 19 panels were more likely to favor foreign interests than U.S. courts would be. Juscelino F. Colares, "Alternative Methods of Appellate Review in Trade Remedy Cases: Examining Results of U.S. Judicial and NAFTA Binational Review of U.S. Agency Decisions from 1989 to 2005," 5 *Journal of Empirical Legal Studies* 171 (March 2008). However, those who have been involved in the system present a more nuanced picture, with some evolution of the results over time. While early Chapter 19 panel decisions may have been more likely to go against the United States than similar decisions from the U.S. Court of International Trade were, it is not clear how different the results are today. *Authors' conversations with practitioners and NAFTA Chapter 19 panelists.*

⁷² Andrew Sulzenko, "What the U.S. NAFTA demands mean for Canada," *The Globe and Mail* (30 March 2017) <https://www.theglobeandmail.com/report-on-business/what-the-us-nafta-demands-mean-for-canada/article34492745/> (visited 5 May 2017).

Chapter 11 (Investor-state dispute settlement)

One of NAFTA's most lasting achievements was to initiate the partial merger of the investment regime and the trade regime. Previously, investment treaties had been separate from trade agreements, with different dispute procedures and often with separate government departments responsible. By incorporating the investment treaty model as a chapter in a trade agreement, NAFTA brought the two regimes together. This innovation caught on, and has become standard practice in trade agreements around the world. While it might not have been anticipated at the time, as there had been very few investor state complaints yet, the inclusion of investment led to increased criticism of trade agreements. Investor state dispute settlement (ISDS) is controversial generally, but it was a handful of NAFTA cases that generated early criticism in the United States and Canada.⁷³

The NAFTA investment rules were drafted many years ago, before the modifications that have been adopted in recent trade agreements to rebalance the rights and obligations. One version of these that was agreed to by the United States, Canada and Mexico is in the TPP. In any reconsideration of ISDS, the TPP investment text may be a good model to start with, as this is the most recent attempt at balancing out the demands of business groups and civil society.⁷⁴ It is worth noting that Canada has been involved, with the European Union, in creating a new investment court as part of CETA, but there are no indications that the United States would support such a change to ISDS.⁷⁵ At the same time, there are strong objections to ISDS more generally these days, and it will be more difficult to finalize a new version of NAFTA that includes ISDS than it was to complete the original NAFTA, when ISDS was relatively unknown.

Institutional Governance

Beyond dispute settlement, there are other important institutions than can help administer a trade agreement more broadly. One of these is a Secretariat, a permanent staff that works on various functions related to the agreement. Another is a forum, often called a commission or a committee, for the governments to act jointly on these same issues. In addition, there may be some issues that require regular technical cooperation through the establishment of working groups. The possibilities for how to structure such institutions vary widely. As NAFTA already established a number of institutions, it is worthwhile to take a

⁷³ See, e.g., Guillermo Aguilar Alvarez William W. Park, "The New Face of Investment Arbitration: NAFTA Chapter 11," 28 *Yale J. Int'l L.* 365 (2003).

⁷⁴ For example, in its summary of the investment chapter, USTR noted that "TPP explicitly clarifies that an investor cannot win a claim for breach of the MST obligation merely by showing that a government measure frustrated its expectations (for example, its expectations of earning certain profits)." <https://ustr.gov/sites/default/files/TPP-Chapter-Summary-Investment.pdf> One important caveat is that the "tobacco carveout" was the subject of strong criticism from many Republicans, including Senate Majority leader Mitch McConnell, and therefore might not make it into a new NAFTA. See, Bernie Becker and Vicki Needham, "McConnell warns Obama against tobacco carve-out in trade deal," *The Hill* (31 July 2015) <http://thehill.com/policy/finance/249913-mcconnell-warns-obama-against-tobacco-carveout-in-trade-deal> (visited 5 May 2017).

⁷⁵ See, e.g., Inside U.S. Trade, "Commission Official Defends EU Investment Court Appeals Mechanism," 16 June 2016. <https://insidetradetrade.com/inside-us-trade/commission-official-defends-eu-investment-court-appeals-mechanism>

moment to discuss how the governance of NAFTA can be updated to account for both old and new challenges the three countries will face going forward.

Secretariat

At the time of the creation of CUSFTA and NAFTA, the GATT Secretariat was already well established as a permanently staffed trade institution, assisting with dispute panels, negotiations, and general oversight of the trading system. However, while CUSFTA and NAFTA also establish a Secretariat, it is of a different, and much more limited, nature.

At the GATT, the Secretariat was an independent organization, headed by a Director General, and with several legal, economic, and other experts. The GATT Secretariat staff served all the GATT Contracting Parties, but were not directly employed by the governments. By contrast, CUSFTA established a Secretariat that was housed within national government agencies. Each party to the agreement was to designate someone within its own government as the secretary responsible for various tasks associated with administering the agreement. Interestingly, CUSFTA provides for this Secretariat in Chapter 19, related to binational panels reviewing anti-dumping and countervailing duty orders. However, language was included that allowed the Secretariat to provide support to the Free Trade Commission as well.

NAFTA mostly carries over the CUSFTA vision for the Secretariat, although it moves the relevant provisions to Chapter 20, in the context of a section on institutional arrangements. It also makes explicit that, in addition to binational panels, the Secretariat should provide administrative assistance to state-state dispute panels, something which had occurred on an informal basis under the CUSFTA. Unlike at the GATT/WTO, where a permanent secretariat provides legal support to dispute panels, CUSFTA/NAFTA panels do not rely on the Secretariat for legal advice. Instead, the panelists hire assistants on an ad hoc basis.

With a NAFTA renegotiation on the table, the parties should consider what this agreement needs in terms of a permanent support staff. The answer depends in part on how the parties see NAFTA's role and function. Do they expect there to be many enforcement actions? Will the meetings of the Free Trade Commission or other administering body be substantive and require implementation? Will the accession provision be utilized? If the answer to some or all of these questions is yes, a permanent, somewhat independent, secretariat staff would be useful.⁷⁶

After NAFTA, U.S. FTAs did not include a secretariat of any sort. Perhaps as a result, these other FTAs have been somewhat frozen in time. They resulted in a number of commitments, but there were only minor subsequent developments. To avoid this fate for NAFTA, the parties should consider establishing a secretariat like that of the WTO, although on a much

⁷⁶ There may be fears that a secretariat could become too powerful, and undermine the sovereignty of the state parties, but the role of the secretariat can be narrowly defined by the negotiators to ensure that states retain ultimate authority. For more on this see: Jan Wouters and Jed Odermatt, "Comparing the 'Four Pillars' of Global Economic Governance: A Critical Analysis of the Institutional Design of the FSB, IMF, World Bank, and WTO," *Journal of International Economic Law* (2014) 17, 49–76.

smaller scale. Though there may be no present inclination on the part of the Trump administration to strengthen these institutions, doing so would facilitate updating the agreement to address future issues, as they arise.

Free Trade Commission

To supervise the implementation of U.S. free trade agreements, the parties create an oversight body made up of the government parties, either called a Joint Committee or a Commission. These bodies have a wide range of tasks, such as considering proposals to amend or modify the agreement, issuing interpretations of the provisions, and supervising the work of other committees, working groups and any other subsidiary bodies. Article 2001 of NAFTA establishes a Free Trade Commission made up of cabinet-level representatives. Typically, these ministerial-level meetings take place between the USTR, the Mexican Secretary of Economy, and the Canadian Minister of International Trade. Though on paper, the role of the Commission is quite broad, in practice, irregular meetings and the lack of a fully functioning, independent secretariat have limited its effectiveness.

In the TPP context, the idea of including a Free Trade Commission became controversial, although only because of misunderstandings on the nature of the Commission created there.⁷⁷ Governments simply act together through these bodies. They are not, as critics fear, supra-national entities that have power over governments. Nevertheless, the criticism should give rise to caution in how these bodies are named and what powers they are given. It should be made very clear that governments are acting through these bodies (and that each government has veto power), and the responsibilities of these bodies should be articulated carefully and narrowly.

Regulatory Cooperation Council

Given the prominence of non-tariff barriers to trade, a Regulatory Cooperation Council would be an important feature of any regulatory chapter of the NAFTA. Rather than starting from scratch on how to build this, however, the three countries can simply institutionalize the current structure of the Canada-U.S. RCC.⁷⁸ The administrative work of the RCC is primarily conducted within the Treasury Board Secretariat in Ottawa, with some staff managing its functions in the Office of Information and Regulatory Affairs (OIRA), in Washington.⁷⁹ Ottawa has generally taken the lead on these efforts, a fact that has been noted as a particular challenge for the ongoing work of the RCC, with a heavier burden falling on Canada, though interest from the White House and support from OIRA are

⁷⁷ See, Simon Lester, "Sessions' TPP Misconceptions," *Cato at Liberty* (12 December 2016) <https://www.cato.org/blog/sessions-tpp-misconceptions> (visited 5 May 2017), and Simon Lester, "Don't Overstate the TPP's Infringement on American Sovereignty," *National Review* (30 January 2017) <http://www.nationalreview.com/article/444398/tpp-american-sovereignty-trading-power-economic-benefits> (visited 5 May 2017).

⁷⁸ Article 21.6.4 (c) of the CETA similarly sets up a Regulatory Cooperation Forum, which appears to be largely modeled off this approach, but also requires the RCF to "report to the CETA Joint Committee on the implementation of this Chapter, as appropriate."

⁷⁹ The Privy Council Office (PCO) used to have this role in Canada prior to April 2016.

essential to its functioning.⁸⁰ In addition, as there has been less progress on the U.S.-Mexico High Level Regulatory Cooperation Council, it could be absorbed into a trilateral RCC, where each party is given the flexibility to decide which activities it wants to participate in.

The RCC could then have rotating leadership assignments between the three countries, on an annual basis as they draft new work plans, but also potentially maintain a presence in a NAFTA Secretariat so that there could be regular support for the three governments in helping agencies and stakeholders connect to the right people across the border. Part of the challenge of regulatory cooperation is transparency and information sharing, so having a single point of contact to help field questions and provide contacts for both governments and stakeholders could help ensure that this process is as open and encouraging of participation as possible.

Inter-Parliamentary Group

A little known aspect of the U.S. - Canada and U.S. - Mexico relationships are two Inter-Parliamentary Committees, established in 1959 and 1961, respectively, that allow for information exchange and collaboration at the legislative level on common concerns. Delegates meet once a year in the capitals to discuss both bilateral and multilateral options for cooperation. Some have suggested that the efforts of the two bilateral committees could be merged, or at the very least, that they could meet every other year to discuss trilateral and NAFTA-wide issues.⁸¹ This could be valuable for a number of reasons. First, it would regularly engage Congress and the legislative branches of Canada and Mexico in ongoing NAFTA concerns, particularly if the agreement is to transform into a living agreement. Ensuring that the legislative branches are routinely part of the conversation is imperative to concerns regarding sovereignty erosion, but also provides a vehicle for constituent considerations to be taken into account. Second, making these committees more visible, and directly part of the NAFTA framework would elevate the importance of inter-parliamentary collaboration. Finally, meeting on a trilateral basis would eliminate any duplicative work on NAFTA-wide issues, such as border infrastructure and security, a single electronic window for customs clearance, and other such topics. Regular trilateral meetings could help establish a pragmatic agenda for truly North American issues, while still remaining sensitive to the fact that the United States has different concerns in some areas with each of its two neighbors. At any rate, a public and open dialogue on these topics is important for alleviating concerns over transparency and ensuring participation of effected groups.

IV. A New Framework for North American Economic Relations

Until recently, it seemed as though the North American idea might be lost, with NAFTA subsumed into the TPP. Now, though, with the TPP itself having been abandoned (at least by the United States), North America might be making a comeback. The Trump administration's focus on NAFTA could actually reinvigorate North American economic

⁸⁰ The Canadian Chamber of Commerce, "Canada's Next Top Trade Barrier: Taking International Regulatory Cooperation Seriously," (April 2016), p. 21.

⁸¹ See Pastor, *The North American Idea*, and Council on Foreign Relations Independent Task Force No. 71, "North America: Time for a New Focus," (1 October 2014).

integration. But the precise nature of the North American economic relationship that follows a NAFTA renegotiation remains to be seen.

To what extent will the renegotiation strengthen North America as an economic region? There are several aspects to this issue: Whether NAFTA is trilateral or bilateral; the extent to which benefits of low tariffs are restricted to the NAFTA parties; and whether NAFTA is open to other parties for accession. The answer to each of these questions will be determined largely by political factors, and the objectives set by each country as they get ready to come back to the negotiating table. Below we address what changes to NAFTA mean for the future of North American economic integration.

Bilateral versus Regional

On a number of occasions, President Trump and his trade advisers have insisted that trade negotiations should be done bilaterally, rather than with multiple countries. In their view, the United States gets better deals this way. There is no evidence that this is actually the case, but nevertheless, the Trump trade team has been insisting that this is the way they will approach trade negotiations.

If they follow through on this promise, it could mean the United States will negotiate separately with Canada and Mexico, unraveling NAFTA into separate U.S.-Canada and U.S.-Mexico trade agreements.⁸² Commerce Secretary Wilbur Ross has stated that the administration “[has] not yet decided whether to go the trilateral route or whether to pursue two matching bilaterals” for NAFTA renegotiations.⁸³ The United States Trade Representative (USTR), Robert Lighthizer, on the other hand, has suggested a preference for a trilateral deal.⁸⁴ If the administration takes the two bilaterals approach, the North American economy is likely to experience a de-integration, at least to some extent. The full scope of such a change is unclear, and depends on the actual terms of the bilateral agreements, but it would certainly undermine North American integration, which has built up a sophisticated network of global value chains for production. Even in a multilateral negotiation, however, some issues are discussed bilaterally, so it may be that this change would be more formal than substantive.

Over the past several decades, North America has emerged as a regional economic entity, and perhaps even a political one to some extent. There are benefits to all three countries from this development, and disrupting the existing system would have harmful effects on a wide range of actors. In our view, NAFTA should remain a trilateral economic agreement.

⁸² It is worth noting, however, that NAFTA would remain in effect between Canada and Mexico, even if the U.S. withdraws from the agreement.

⁸³ Adrian Morrow, “U.S. withdrawal from NAFTA is back on table: Wilbur Ross,” (10 May 2017) <http://www.theglobeandmail.com/news/world/us-withdrawl-from-nafta-is-back-on-table-wilbur-ross/article34934318/> (visited 11 May 2017).

⁸⁴ Inside U.S. Trade, “Following Lighthizer meeting, senators say administration favors a trilateral NAFTA approach,” (16 May 2017) <https://insidetrade.com/daily-news/following-lighthizer-meeting-senators-say-administration-favors-trilateral-nafta-approach> (visited 16 May 2017).

Regionalism in a Globalized World: What is North American?

As discussed above, for a product to benefit from the zero tariffs under NAFTA, it must have a certain amount of North American content, which varies by products. The Trump administration has talked about tightening up these rules to ensure that “the Agreement supports production and jobs in the United States” and address attempts at circumvention of preferential duties.⁸⁵ In essence, the issue is how restrictive or permissive the standard will be for determining when a product is North American. The narrower the standard, the more the agreement favors North Americans over others. By contrast, a broader standard pushes more towards freer trade, by applying the tariffs to more products. If the Trump administration pursues tighter rules of origin to restrict the amount of trade eligible for zero tariffs, this would reduce the benefits of NAFTA.

The problem with strict rules can easily be explained by briefly discussing the importance of global supply chains, and where North America fits in this picture. Lower transportation and communication costs allowed for the development of regional and global production networks that has fundamentally transformed how countries compete; globalization has not only generated sectoral competition, but also competition at different stages of production and by occupation—from trade in products to trade in tasks.⁸⁶ The automotive supply chain, for example, is so complex, that a typical car is composed of roughly 30,000 separate parts.⁸⁷ In addition to this, the assembly of these various parts can take place in a number of different countries, making it even harder to disentangle just how much of any given input was made anywhere. Thus, sourcing some parts and labor from Asia, and others in North America, makes it difficult to sort out the 62.5% NAFTA origin cut-off. The TPP relaxed this rule to roughly 45% under the net-cost method.⁸⁸

Generally speaking, Canada, Mexico and the United States have a large amount of trade in intermediate inputs. In fact, one important feature of North American trade is the high degree of value added in products that cross both the northern and southern borders. A study by Koopman et al. (2010) found that 40% of imports from Mexico and 25% of imports from Canada contain U.S. value added. The three countries don’t just trade together, they make things together. However, the increased fragmentation of production processes means that the region does not exist in a vacuum either. For instance, foreign value added accounts for roughly 15% of U.S. gross exports, and that figure is 23.4% for Canada, and 31.7% for Mexico.⁸⁹ Top providers of foreign inputs for the U.S. are Canada (14.5%), China

⁸⁵ Draft letter from Acting USTR to Congress on NAFTA renegotiation, p. 3. See, U.S. Chamber of Commerce (30 March 2017) <http://www.usmexicobusiness.com/files/2017/03/20170329150447161.pdf> (visited 30 March 2017).

⁸⁶ Richard Baldwin, *The Great Convergence* (Cambridge: The Belknap Press of Harvard University Press, 2016).

⁸⁷ David Francis, “Cat’s Cradle: Scrapping NAFTA will Wreak Havoc on Auto Industry Supply Chains,” *Foreign Policy* (28 February 2016) <http://foreignpolicy.com/2017/02/28/cats-cradle-scrapping-nafta-will-wreak-havoc-on-auto-industry-supply-chains/> (visited 6 May 2017).

⁸⁸ *Inside U.S Trade* “TPP Auto ROO Most Likely To Hurt Makers Of Less Complex Parts: Experts,” (21 January 2016) <https://insidetrade.com/share/152178> (visited 6 May 2017).

⁸⁹ World Trade Organization, “United States Trade in Value Added and Global Supply Chains,” (2011) https://www.wto.org/english/res_e/statis_e/miwi_e/US_e.pdf (visited 17 April 2017), World Trade Organization, “Canada Trade in Value Added and Global Supply Chains,” (2011)

(10.9%), and Mexico (8.6%), while Mexico receives most of its inputs from the U.S. (36.8%), China (13.2%), and Japan (7.4%), and Canada's highest source of inputs comes from the U.S. (39.8%), China (6.7%), and Japan (4.6%).⁹⁰ North America trades and makes things with the entire world, so any policy that forces firms to choose one location over another will naturally lead to higher costs of production.

NAFTA 2.0 and Beyond: NAFTA for the Rest of the World?

While the CUSFTA did not anticipate other countries joining, NAFTA had a brief provision on accession, which stated: "Any country or group of countries may accede to this Agreement subject to such terms and conditions as may be agreed between such country or countries and the Commission and following approval in accordance with the applicable legal procedures of each country."⁹¹ At the time, it was considered a possibility that other countries in the Americas might join the arrangement. However, no accession to NAFTA ever went forward (and further economic integration of the Americas through the Free Trade Area of the Americas (FTAA) was abandoned).

In renegotiating NAFTA, the parties need to consider their vision for the future of NAFTA, in particular its character as a regional arrangement. Is there any expectation of broadening the agreement beyond the three current parties? With over 20 years of experience, and in the context of the proliferating spaghetti bowl of trade agreements, how do the parties currently see NAFTA fitting into the international trade regime? If there is a chance that NAFTA will serve as a foundation upon which the trade regime can be modernized, some detailed provisions might be helpful, to guide the process a bit. The best source of experience with accessions to trade agreements is at the WTO, where they have handled many of these over the years. But in terms of a few basic provisions in a situation where accession may not be all that likely, the TPP provisions on accession might offer a good starting point.⁹²

V. Political Challenges

In the previous sections, we laid out a general framework for thinking about a NAFTA renegotiation. However, we cannot ignore the fact that debates about NAFTA do not occur in a vacuum, and that the impetus for these talks is President Trump and his challenge to the existing trade regime. While there will be many policy challenges to achieving a new deal, the largest sticking point in NAFTA re-negotiations will be politics, both domestic and international. What are the key political challenges? In many ways, this depends on the Trump administration's approach, which as of writing is largely unknown. In the absence of a clearly articulated trade policy, it may be hard to know how the NAFTA renegotiation will

https://www.wto.org/english/res_e/statis_e/miwi_e/CA_e.pdf (visited 17 April 2017), World Trade Organization, "Mexico Trade in Value Added and Global Supply Chains," (2011)

https://www.wto.org/english/res_e/statis_e/miwi_e/MX_e.pdf visited 17 April 2017).

⁹⁰ Ibid.

⁹¹ NAFTA Article 2204, para. 1.

⁹² TPP Article 30.4.

unfold, but there are some hints as to what some of the key political challenges may be. We address these below.

Though there have been various statements from administrations officials on what NAFTA renegotiations will address from Commerce Secretary Wilbur Ross, National Trade Council Director Peter Navarro, and the President himself, details have been generally lacking. This may primarily be due to the fact that the USTR, who is responsible for conducting negotiations, was only confirmed to his position in May 2017. An earlier document that outlines some policy objectives for NAFTA is a memo from Acting U.S. Trade Representative Stephen Vaughn to Congress.⁹³ The memo reiterates many of the known concerns the administration has consistently repeated: the trade deficit; market access; export subsidies on agricultural products; tightening rules of origin; customs enforcement; intellectual property; investor-state dispute settlement; eliminating Chapter 19; trade remedies; and enforceable environment and labor protections. The overall theme appears to be strengthening enforcement and increasing market access for the United States.

The May 18 notice to renegotiate NAFTA sent to Congress by USTR Robert Lighthizer, at less than 2 pages, sets a more muted tone than the administration had offered previously. Though it reiterates many of the items included in the previous memo from Acting USTR Vaughn, it does not elaborate on the issues. It states that “objectives for this negotiation will comply with the specific objectives set forth by Congress in section 102 of the Trade Priorities and Accountability Act.”⁹⁴ Further clarity will be provided in the 30 days prior to negotiations, when Lighthizer must set out detailed negotiating objectives, taking into account his consultations with Congress.

Regarding the specific issues we highlight as strong candidates for inclusion in a NAFTA update, there are several tacks the administration may take. On e-commerce, the administration is likely to draw heavily on the TPP chapter on this topic. Regarding regulatory issues, there is a possibility that the momentum built during the Obama administration will continue. For instance, the Draft Notice from Acting USTR Vaughn noted that negotiations will seek to “improve regulatory practice and promote increased regulatory coherence,” which perhaps hints at the continuation of current efforts by the RCC, although it could just mean adopting the TPP regulatory coherence chapter.⁹⁵ As NAFTA lacks a regulatory coherence chapter, this also signals the possibility that the administration may be open to the idea, particularly due to the elevated importance given to these issues in recent trade agreements. On rules of origin, however, the potential for greater challenges is a possibility, as noted earlier, because it appears the administration wants to create more

⁹³See, U.S. Chamber of Commerce, Draft letter from Acting USTR to Congress on NAFTA renegotiation, (30 March 2017) <http://www.usmexicobusiness.com/files/2017/03/20170329150447161.pdf> (visited 30 March 2017).

⁹⁴Inside U.S. Trade, Notice from USTR Lighthizer to Sen. Charles Schumer on NAFTA Renegotiation (18 May 2017) https://insidetrade.com/sites/insidetrade.com/files/documents/may2017/wto2017_0156a.pdf (visited 18 May 2017).

⁹⁵Inside U.S. Trade, Notice from USTR Lighthizer to Sen. Charles Schumer on NAFTA Renegotiation (18 May 2017) p.6.

restrictive RoO requirements.⁹⁶ This would be a negative development for all three parties to the agreement.

What may come of the labor and environment chapters is anyone's guess. The administration will most likely face pressure to include an enforceable labor chapter in a new NAFTA. Trump made labor issues a key theme of his campaign, often lambasting trade agreements for the loss of U.S. manufacturing jobs to low-wage countries. It would be difficult to imagine how he could renegotiate NAFTA without including strong labor provisions to fulfil one of his major campaign promises, regardless of whether such action can bring back any jobs to the United States. Here, we can likely expect a duplication of what already exists in the TPP. Environmental issues are another matter, however. Even though the Draft Notice from the Acting USTR cited enforceable environmental obligations as an objective of the talks, the administration's general attitude towards environmental issues does not seem to give it priority.⁹⁷ For example, it is a distinct possibility that the CEC could lose its contribution from the U.S. and thus be unable to function if the administration withdraws funding from the USEPA.⁹⁸

On institutional upgrades to NAFTA, it is even less clear what the administration intends to do, if anything. Trump has consistently noted his objections to international organizations and most forms of global governance, but has yet to take any substantive policy actions based on these pronouncements. If the administration brings this skepticism into NAFTA negotiations, however, we can expect little in the way of institutional upgrades. We caution against such skepticism because many of the criticisms that have been launched at NAFTA and other trade agreements seems to suggest a need for dynamic agreements that can adapt to the challenges of the day. Establishing a fully functioning, independent Secretariat, and reinvigorating the Free Trade Commission would be useful steps in this regard. In addition, creating a link between the inter-parliamentary groups in Congress will also be a positive step forward in addressing issues regarding a lack of transparency and democratic accountability in trade agreements. A regulatory cooperation council may be the least controversial institutional upgrade, and one that the administration should be able to get behind if it is able to frame it within its broader efforts at regulatory reform and reducing such barriers to trade.

As for dispute procedures, on NAFTA Chapter 11, it is possible that ISDS is a part of NAFTA the Trump administration would be willing to sacrifice to assuage trade critics, although perhaps more likely is simply amending it to look more like the TPP investment chapter.⁹⁹ On Chapter 19, the administration will probably push to eliminate it, and its fate

⁹⁶ If the U.S. administration sticks to a tight deadline for talks, however, it is hard to see how an overhaul of the RoO regime is possible, as it will require going through hundreds of pages of product-specific requirements in the annexes. It therefore may be possible that a few sectors, such as autos, may receive attention to politically show something was substantively changed, though the rest could be left as-is.

⁹⁷ Steve Mufson and Brady Dennis, "Trump victory reverses U.S. energy and environmental priorities," *The Washington Post* (9 November 2016) https://www.washingtonpost.com/news/energy-environment/wp/2016/11/09/trump-victory-reverses-u-s-energy-and-environmental-priorities/?utm_term=.c05580f35670 (visited 8 May 2017).

⁹⁸ The U.S. financial contribution to the CEC comes directly from the USEPA, specifically, from the Office of International and Tribal Affairs budget.

⁹⁹ With regard to the CETA "investment court" that has received a lot of attention, there does not appear to be support for this among U.S. business groups or government officials.

may depend on how attached the Canadians are to it. Some members of Congress certainly seem to be eager to drop it entirely.¹⁰⁰ And on Chapter 20, hopefully all parties will agree that a functioning dispute system is needed, and the TPP could serve as a basis. In fact, it would seem rather odd for an administration so heavily focused on enforcement not to include a revised Chapter 20 that could be properly utilized.

In addition to what the U.S. wants, it is important to keep in mind that Canada and Mexico will have their own priorities and needs. It is unclear how willing Canada will be to budge on sensitive issues such as opening its dairy market, and the U.S. may have to settle for limited gains in the face of strong domestic opposition the Trudeau government will face. The TPP, for instance, only granted duty-free access to 3.25% of Canada's dairy market, and in CETA, Canada increased its tariff-rate quota for cheese, granting the EU duty free access to 4% of the cheese market.¹⁰¹ Mexico is eager to begin negotiations as soon as possible, as President Enrique Peña Nieto's support falls to single digits, and he faces a populist challenger in the upcoming elections who would be far more willing to walk away from a deal.¹⁰² It is clear that the administration is aware of this, which is one reason why it appears they may be pushing for a quick renegotiation. Lighthizer suggested the goal is to wrap up negotiations by the end of 2017.¹⁰³ Given that negotiations cannot begin until mid-August, that leaves little over 4 months to negotiate.¹⁰⁴

Finally, there is also a more fundamental challenge of the NAFTA renegotiation process, and quite possibly, all future trade agreements the U.S. enters in to. Opposition to liberalization has undoubtedly been on the increase, and Trump has been quick to rally to this cause. How does this impact NAFTA? A recent Pew Research survey found that 51% of Americans, 60% of Mexicans, and 76% of Canadians say NAFTA has been good for their country.¹⁰⁵ Overall, it seems that majorities in all three countries support liberalization among them. However, this same survey also reveals something very surprising: in the United States, support for NAFTA is sharply divided by partisan lines, with just 30% of

¹⁰⁰ Inside U.S. Trade, "Wyden: Administration 'committed' to doing away with NAFTA's Chapter 19," (17 May 2017) https://insidetrade.com/trade/wyden-administration-'committed'-doing-away-nafta's-chapter-19?utm_source=dlvr.it&utm_medium=twitter (visited 17 May 2017).

¹⁰¹ See, Bill Curry, "The ABCs of TPP," *The Globe and Mail* (5 January 2017) <https://www.theglobeandmail.com/report-on-business/international-business/what-is-tpp-understanding-the-new-pacific-tradecdeal/article26648948/> (visited 19 May 2017) and European Commission, "CETA—Summary of the final negotiating results," (December 2014) https://trade.ec.europa.eu/doclib/docs/2014/december/tradoc_152982.pdf (visited 19 May 2017).

¹⁰² Azam Ahmed, "Renegotiate Nafta? Mexicans Say Get On With It," *The New York Times* (25 March 2017) <https://mobile.nytimes.com/2017/03/25/world/americas/nafta-renegotiation-mexico.html?referer=> (visited 17 April 2017).

¹⁰³ Inside U.S. Trade, "USTR notifies Congress of its intent to renegotiate NAFTA; U.S. hopes for a trilateral deal," (18 May 2017) <https://insidetrade.com/daily-news/ustr-notifies-congress-its-intent-renegotiate-nafta-us-hopes-trilateral-deal> (visited 18 May 2017).

¹⁰⁴ The only time the U.S. has concluded negotiations that quickly was in its FTA with Jordan, and on average, negotiations have taken approximately 1.5 years. Caroline Freund, "How Long Does it Take to Conclude a Trade Agreement with the US?" (21 July 2016) <https://piie.com/blogs/trade-investment-policy-watch/how-long-does-it-take-conclude-trade-agreement-us> (visited 19 May 2017). However, it is worth noting that more complicated deals can take much longer—the TPP took over 8.5 years from negotiation to signing.

¹⁰⁵ Bruce Stokes, "Views of NAFTA less positive – and more partisan – in U.S. than in Canada and Mexico," Pew Research Center (9 May 2017) <http://www.pewresearch.org/fact-tank/2017/05/09/views-of-nafta-less-positive-and-more-partisan-in-u-s-than-in-canada-and-mexico/> (visited 9 May 2017).

Republicans saying NAFTA has been good for the country—that figure for Democrats is 68%. This is a major shift for a party that has been traditionally pro-liberalization. To put this in context, in Canada, the most left-leaning federal party, the New Democrat Party (NDP) shows 73% favorability towards NAFTA, while the Conservatives record 82% support, and with 83% of Trudeau’s Liberal Party saying NAFTA was good for the country. In Mexico, these figures are 68% for the PAN, and 59% for the PRI (the party that was in power when NAFTA was negotiated).

The political challenge for the U.S. is clear. How will it be able to modernize NAFTA, or negotiate any trade agreements, if the President, and a significant portion of the constituents of the majority party in Congress, appear to be increasingly skeptical of these agreements? It is important to remember that the Trump administration will be engaging in a difficult balancing act, trying to satisfy business groups who want new and updated trade agreements, but also U.S. trade critics who have supported his anti-trade message. How this domestic battle plays out may largely determine just how modern the new NAFTA will be.

VI. Conclusion

The TPP was supposed to be the cutting edge of U.S. trade policy and agreements, but has now been formally abandoned by the United States. NAFTA will be the first trade negotiation undertaken by the Trump administration, which means it will be the agreement that sets the new U.S. trade agenda, taking the place of the TPP (and to some extent copying its terms). If this negotiation succeeds, NAFTA will likely be a model for the various bilateral trade agreements that the administration tells us will be negotiated in the coming years.

There is a risk, however, that this renegotiation will fall apart under the weight of its own ambitions. The administration may want to use the NAFTA renegotiation to solve the “problem” of trade deficits, or tackle currency manipulation, or address border tax adjustments. Similarly, some on the left argue for using trade agreements to take on inequality or climate change.¹⁰⁶ If this is how we approach trade negotiations, however, we may not see positive results. Unrealistic goals can lead to negotiations getting bogged down.

Despite any problems that exist with the existing trade regime, there is no need for a revolution in thinking about trade agreements. Rather, what is needed is a refinement of existing policies and institutions, based on the experience of the last 25 years. Some may argue that an evolutionary approach to NAFTA is not enough to address the many critiques of the agreement, coming from both the left and the right. However, the benefits of trade liberalization should not be abandoned in response to current political whims. A cautious and careful approach has served the system well over the years. By contrast, a drastic shift to an untested approach could result in many unforeseen consequences. To this end, we have presented a framework for thinking about how NAFTA could be refined, by examining those aspects of NAFTA that either do not work, are out of date, or could not have been

¹⁰⁶ See for example, Timothy Meyer. "Saving the Political Consensus in Favor of Free Trade." *Vand. L. Rev.* 70 (2017): 985, and Todd Tucker, "The Sustainable Equitable Trade Doctrine: Building Progressive International Cooperation to Counter Right-Wing Economic Authoritarianism," (13 March 2017) <http://rooseveltinstitute.org/wp-content/uploads/2017/03/The-Sustainable-Equitable-Trade-Doctrine.pdf>.

imagined at the time the deal was originally negotiated. In doing so, we conclude that there is scope for change in the agreement that would be beneficial to all three parties, and that a modernized NAFTA is possible if each side approaches the task in good faith.