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NORTH AMERICAN FREE TRADE AGREEMENT NEGOTIATIONS - AN ALBERTA PERSPECTIVE

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1. INTRODUCTION

Mexico, Canada and the United States are presently negotiating the development of an agreement which would substantially reduce barriers to trade in goods, services and investment among the three countries. If successful, it will result in a geographic area containing over 350,000,000 people and a gross domestic product of over \$6 trillion being relatively free of barriers to trade. There are

potential benefits to all three countries.

This Bulletin attempts to assess where the negotiations are in October of 1991, identify the key areas of negotiation and note some of the sensitivities which may complicate the negotiations prior to the final decision on whether there should be an agreement and what its content will be.

2. TIMING AND PROCESS

The **timing** of any North American Free Trade Agreement (NAFTA) will be dependent on if and when negotiations are complete. Nevertheless, there are some clear time limits. There appear to be two alternatives on when a successful conclusion of the NAFTA negotiations might occur.

If the negotiations can be completed in early 1992 prior to the beginning of the United States Primaries, President Bush could present the agreement to Congress at that time. This would give Congress the necessary time to review the agreement prior to United States elections in November 1992 and, if ratified,

would likely be implemented in January 1993.

If negotiations are not finished by early 1992, a more likely scenario would be to see negotiations continue on until the Fall and early Winter of 1992. Again, if a successful agreement can be negotiated, the new President could present the agreement to the next Congress in 1993 for ratification by mid year 1993 and implementation would likely occur in January 1994.

In both cases, the United States will use its "fast track" procedure which requires the Congress to approve or reject the agreement "as is" and within specified time limits. Because this "fast track" authority expires in June 1993, the United States Administration must present the agreement to Congress prior to March 1993, allowing the necessary time for Congress to consider its ratification.

3. MARKET ACCESS

Market access issues deal with tariff and non-tariff measures, Rules of Origin, duty drawbacks, the Maquiladora industries, customs facilitation, and border inspection among other issues.

Tariff cuts are likely to be set up in a similar way to those in the Canada/U.S. FTA. There will be three types of tariff cuts. An immediate set of cuts will eliminate tariffs on products with the implementation of the agreement. There will also be an intermediate and long-term phase-in of tariff cuts to other groups of products, but those time periods have yet to be agreed upon. The United States will likely pursue a fourth and even longer tariff cut phase-in for particularly sensitive horticultural products, but it is unclear whether this will be acceptable to Canada or Mexico.

There is unlikely to be any symmetrical reduction of tariffs required. Each country will have the opportunity to phase-in tariff cuts on a different product at the same speed as the country which requires the longest phase-in.

It is likely that a process for accelerated tariff reduction talks after the implementation of the agreement. This has been done in the Canada/U.S. FTA and has been widely supported by the private sector as a constructive process.

Non-tariff measure negotiations in the NAFTA have not progressed as far as the tariff talks. There is likely to be exchange of requests among the three countries early in the fall which will form the basis of offers by these countries shortly thereafter. This will initiate an iterative procedure involving three bilateral discussions and a trilateral agreement.

The **Rules of Origin** will be a major set of negotiations in itself. They will have to deal with duty drawbacks, the Maquiladora industries, customs facilitation, border inspection and the development of infrastructure in Mexico. It will also give Canada and the United States the opportunity to revisit the Rules of Origin outlined in the Canada/U.S. FTA and refine them. The key issue will be how "tight" the Rules of Origin need to be. Requiring a high percentage of North American content in order to qualify for coverage under a NAFTA would ensure broader benefits to North American producers, but would reduce competition in a wide variety of areas, something the three countries may not be willing to sacrifice.

In **textiles**, the United States has an extremely sensitive situation. The U.S. wants to ensure protection of their domestic market. This might require some type of long-term phase-in of tariff cuts, strict Rules of Origin for any product crossing the border and a safeguard mechanism which would allow the United States to "snapback" higher tariffs in case of import surges.

In **automobiles**, the key issue will revolve around the Rules of Origin. The United States has stated publicly it wishes to increase the North American content in the Canada/U.S. FTA from 50% to 60%. Canada has suggested that would be counterproductive. The United States has also identified the freedom to invest in the Mexican market as a high priority. Outside of those two issues, there are likely to be few problems between Canada and the United States in this sector.

4. ENERGY

The **energy sector** will be among the most sensitive areas discussed. Mexico has indicated that their Constitution requires them to retain the ownership and benefits of oil for the Mexican people. At the same time, one of the major reasons for Mexico initiating the request for a North American Free Trade Agreement was a wish for more investment.

The United States is clearly interested in ensuring they have an appropriate investment climate in Mexico to take advantage of

opportunities. Mexico will likely narrow its existing definition of energy and efforts will be made to find creative ways to provide access to Mexico's oil and gas reserves without challenging the Constitution. Key decisions will revolve around primary and secondary petrochemicals, distribution systems such as gasoline stations, and primary energy sources.

There is a degree of uncertainty as to whether there will be an energy chapter in the final NAFTA agreement.

5. AGRICULTURE

Four areas will be discussed in agriculture. Tariffs, non-tariff measures, subsidies and health and phyto-sanitary regulations.

Tariffs on agricultural products will be dealt with under the same rules as other products. As mentioned earlier, the United States appears to have the major problem in this area with their fruits and vegetables.

In **non-tariff measures in agriculture**, all countries have some difficulties. Mexico has its import licensing procedures. The United States has import quotas. Canada has supply managed products. Because all of these issues revolve around larger international problems, there will likely be limited movement in these areas unless progress is made in the Multilateral Trade Negotiations.

The issue of **agricultural subsidies** is quite similar to the non-tariff measures. Because Canada and the United States subsidize some agricultural goods as a result of a "subsidy war" with the European Community, it will be difficult for those countries to unilaterally refrain from using subsidies. Mexico does not have sufficient funds to subsidize extensively and uses an import licensing system to protect its producers. Again, it is unlikely that a NAFTA agreement can go much further than the Multilateral Trade Negotiations.

In **health and phyto-sanitary** discussions, the three countries will again use the Multilateral Trade Negotiations as a starting point and try to build on those.

6. GOVERNMENT PROCUREMENT

A **government procurement** chapter in the NAFTA is likely. The participants will probably use Chapter 13 of the Canada/U.S. FTA as a starting point. The issues will revolve around a threshold for open bidding, to whom it will be applied, and whether any exceptions will be made.

There is a particular problem here with Mexico as accurate information on government procurement may not be available and if it is, it may not be reliable.

There is likely to be an effort to include subnational governments: the states in Mexico and the United States and the provinces in Canada, as well as municipalities. If successful, it is likely that the states and provinces would,

on a voluntary basis, agree to the regulations associated with the procurement agreement chapter.

The major issue for negotiations will likely be the United States Small Business and Minority Set Aside, a key U.S. exception which has been challenged by both Canada and Mexico. The Small Business and Minority Set Aside allows the United States to set aside a certain portion of their government procurement for their Small Business. Unfortunately, Small Business in the United States, companies with up to 500 employees, are generally the most active in the those areas which Canadian and Mexican companies can best compete.

7. TRADE RULES

Trade rules involve dumping, subsidy and countervailing duties, and standards. This will be one of the more contentious areas in the negotiations.

In **dumping and subsidies/countervail**, the key issue will be dispute settlement. The Mexicans are disposed to want something similar to the Chapter 19 protection given to Canada in the FTA, while the U.S. may wish to resist that, holding out for something less binding such as a dispute settlement similar to that in the Multilateral Trade Negotiations.

Surprisingly, Mexico has dramatically cut its subsidies over the past five years and may not set as high a priority on the subsidy/countervail discussion as they will on the anti-dumping issue. However, the talks in this area are early and it is premature to suggest an outcome.

With respect to **standards**, the three countries will likely use the Uruguay Round as a point of departure. The technical barriers to trade text in the Multilateral Trade Negotiations was not one of the major stumbling blocks in the breakdown of the Ministerial in Brussels in December 1990. So one can conclude that much of that work has been successfully completed. The over arching issues will likely be national treatment, labelling requirements, consumer protection, and harmonization.

In negotiating standards, there will likely be three subgroups:

1. Animal and plant health;
2. Human health & the environment; and
3. Industrial and consumer standards.

The three countries do not appear to be focusing on the same issues in this area and that may make building on the Multilateral Trade Negotiation talks more difficult.

TRADE RELATED INTELLECTUAL PROPERTY RIGHTS (TRIPS)

TRIPs are like many other areas, in that the results of the Multilateral Trade Negotiations will likely have a significant impact on these issues in the NAFTA talks. The United States wants a strong agreement and has established this as a priority.

Mexico has recently completely rewritten its legislation with respect to copyright, counterfeiting, patent and trademark protection. This should make negotiations easier, as all three countries will be working from similar pieces of legislation.

There will likely be discussions related to minimum standards for intellectual property rights protection, where harmonization should or could occur, and enforcement. However, these are areas which have not been negotiated in detail to this point in time.

8. SERVICES

Services is one area where the NAFTA will likely be different than that negotiated in the Multilateral Trade Negotiations. With only three countries involved, not more than 100, the NAFTA can use the Canada/U.S. FTA as a building block. The FTA covers the key obligations which Canada and the United States were willing to undertake, and will likely be used to establish the parameters for Mexican rules and regulations.

The issues to be discussed will likely be:

1. The principles for services trade;
2. Financial/banking and securities;
3. Insurance;
4. Land transportation;
5. Telecommunications; and
6. Other services.

The key principles will likely be:

1. Transparency;
2. Advanced notice/publication of regulations;
3. Consultation and the opportunity to comment on changes to regulations;
4. National treatment;

5. Coverage; and
6. Licensing of professionals.

The financial services sector will likely have a different approach than the FTA. The FTA was essentially an exchange of concessions between Canada and the United States, and therefore cannot be logically extended effectively to Mexico.

In services, Mexico may be an interesting demandeur in a number of areas. They are more open than either the United States or Canada in certain areas of the service sector. They are likely to have an interest in both broadcast and cable, wishing to take advantage of the large and affluent hispanic population in the southern United States. However, this is an area where the United States currently has investment restrictions and it is sensitive in Canada because it is part of the cultural industries.

Temporary entry will probably be part of the services negotiations. The FTA will again provide the basis for an agreement with minor modifications likely.

9. INVESTMENT

This one of the areas which has not been focused on as extensively as it might be, given the importance of the chapter to the United States and Mexico in particular. If recent negotiations in the Multilateral Trade Negotiations and the Free Trade Agreement with Canada are an indication, issues should include:

1. National treatment (non-discrimination);
2. Performance requirements;

3. Transfer of funds;
4. Expropriation;
5. Temporary entry;
6. Transparency of rules and regulations;
7. Dispute settlement;
8. Sector coverage;
9. National security;
10. Extra-territoriality; and
11. State/provincial coverage.

10. SAFEGUARDS

The issue of how to deal with sudden surges in imports was critical on the Canada/U.S. FTA and will be important in the NAFTA. Unfortunately, Mexico does not have the legal infrastructure at present to deal with the process. In discussing the development of a safeguard system, eight areas need to be addressed.

1. The independence in composition of the body revealing the need for safeguards.
2. The standing of interested parties making representation to the institution.

3. The standard of proof required.
4. The notification process.
5. The requirement for public hearings.
6. The time periods required for making decision.
7. Public access to the decisions.
8. Alternative remedies available to the institution to address safeguards.

Until these are available in Mexico, it will be difficult to get an agreement on safeguard protection among the three countries.

11. LABOUR AND THE ENVIRONMENT

There have been a number of discussions regarding labour and environmental standards and whether they will be part of the negotiations.

It is unlikely that either labour or environmental issues will be negotiated within the context of the NAFTA.