The Heritage Foundation Backgrounder

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GUIDELINES FOR U.S. NEGOTIATORS AT THE TRADE TALKS WITH MEXICO

INTRODUCTION

The United States, Canada, and Mexico began negotiations in June on a North American Free Trade Agreement (known by the acronym NAFTA). This will allow the free trade of most goods and services from the Yukon in Alaska to the Yucatan in Mexico. Although no target date has been set for completion, it is expected that the U.S., Canadian, and Mexican delegations may finish their draft of the agreement by next spring. It then would be sent for approval to the U.S. Congress and the legislatures of the two other countries. The U.S. and Canada signed their own Free Trade Agreement in 1988.

A NAFTA will eliminate tariffs, trade quotas, import licensing, and other traditional barriers to trade. This freer trade will spur economic growth throughout North America. In addition, the NAFTA will help the U.S. compete against the European Community and the Pacific Rim nations in the production and export of goods and services, by creating a free trade zone of 360 million people with a combined annual economic product of over $6.2 trillion. This will be of particular importance to the U.S. in the 21st Century as it comes to rely more on world trade as a source of national wealth.

Free of Congressional Meddling. The Bush Administration won fast track authority for the NAFTA negotiations on May 31 when Congress failed to block an automatic two-year extension of that authority. This authority allows U.S. NAFTA negotiators to craft an agreement that will be free from congressional meddling once the NAFTA is signed. Under fast track authority the House and the Senate can vote only to approve or reject the agreement. Neither house can amend it. Now that negotiations have begun in earnest, U.S. negotiators must

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bring home the best NAFTA possible. Criteria thus are need to evaluate how well the negotiators do.

Because the U.S. already has a Free Trade Agreement with Canada, most major NAFTA negotiating issues involve Mexico and how it will be integrated into a North American Free Trade Area. To ensure the creation of an economically successful Free Trade Area with Mexico, U.S.negotiators should encourage the Mexicans to eliminate not only tariffs and quotas, but also such non-traditional trade barriers as domestic subsidies, as well as economic laws and regulations that restrict production and fail to protect private property. U.S. negotiators also should seek access to the Mexican market for U.S. goods and services and push for open investment in Mexico's energy, financial services, and transportation sectors.

In return, American negotiators should promise that the U.S. will reduce tariffs on Mexican exports to the U.S. and will strip import protections from U.S. industries, such as apparel, glassware, steel, and textiles, that have had an unfair advantage over Mexican imports because of tariffs and quotas. In addition, the U.S. should exempt Mexico from most anti-dumping legislation and create a trade dispute resolution process to settle trade conflicts arising between the two nations.

Boost for U.S. and Mexico. The U.S. economy would benefit greatly from freer trade with Mexico. Free trade and open markets would spur industrialization and economic growth in Mexico, producing greater demand there not only for American construction equipment, factory machinery and other capital goods, but also for American computers and financial services. As the Mexican economy grows, Mexican wages will increase, thus expanding the buying power of Mexicans.

Economic growth in Mexico will be slowed without a broad-based free trade agreement. For instance, U.S. computer and other advanced technology companies will be reluctant to invest in Mexico unless private property is fully protected by the Mexican legal system. So far, however, Mexican laws, regulations, and even constitutional provisions weaken the value of private property ownership. Mexican laws also prevent foreigners from owning the majority of stock in firms operating in Mexico. Until these obstacles to free trade are removed, many American firms will not invest the vast sums of money needed to rebuild the Mexican economy.

The time may be right for Mexico to make major reforms. Mexican President Carlos Salinas de Gortari wants not only an enormous infusion of investment capital from abroad, but greater access to U.S. markets. If the Salinas administration could be convinced that free market reforms would result in greater American capital investment in Mexico and more Mexican exports to the U.S., it may agree to far-reaching structural changes in the Mexican economy, such as allowing greater foreign investment.

To ensure the long-term benefits of free trade with Mexico, U.S. policy makers and trade negotiators should produce an agreement that will:

♦ **Rapidly eliminate tariffs, quotas, and licensing barriers between the two countries.** Eradicating U.S. tariffs rapidly will greatly benefit Mexican exporters who rely heavily on sales to the U.S. America already buys 70 percent of all Mexican exports. Yet a surge in Mexican exports to the U.S. is not expected to hurt American producers much. The reason: Mexican goods are only 6 percent of total U.S. imports. Because Mexico will benefit greatly if U.S. tariffs and quotas on Mexican goods are abolished, agreeing to do so will strengthen the hands of U.S. negotiators to push Mexico to eliminate Mexico's higher tariffs on U.S. exports.

♦ **Reduce or eliminate Mexican restrictions on foreign ownership.** Mexico's 1973 Foreign Investment Code prohibiting foreign majority ownership in all domestic businesses needs to be modified. Otherwise U.S. businesses will not invest in Mexico. In the NAFTA negotiations, U.S. negotiators should press Mexico to allow foreign majority ownership in Mexican industry including the so-called strategic sectors of the economy—energy, financial services, telecommunications, and transportation. Without private domestic or foreign investment in these vital areas, the Mexican economy will not grow to become the premier trading partner of the U.S.

♦ **Allow U.S. companies to compete against Mexican state-owned or heavily regulated industries.** The Mexican government still controls or heavily regulates several key sectors of the Mexican economy, like agriculture, banking, and energy. Although Salinas is moving toward opening these areas to private and foreign investment, reforms are far from complete. U.S. negotiators should seek concessions from the Mexican government that would allow U.S. firms to compete with Mexican government-owned or -regulated industries. U.S. companies should be allowed, for example, to sell and distribute petroleum and food products in Mexico although these areas are controlled heavily by the government. This access also should include the right of U.S. companies to bid on Mexican government projects.

♦ **Eliminate "production requirements" on goods produced in Mexico.** Mexican law must be changed to protect owners of private property if the Mexican economy is to prosper. To do this Mexico should rescind "production requirement" laws that restrict how manufacturers buy materials and sell their finished products, Mexico, too, should reduce its government's discretionary power to decide how much of a Mexican company foreigners can own.

♦ **Make laws on intellectual property rights enforcement uniform among NAFTA countries.** Mexico recently enacted laws governing the protection of intellectual property. This new legislation on copyrights, patents, and so forth actually protects intellectual property more than do Canada's laws. One problem with the new Mexican law, however, is that the power to decide who will be brought to court still rests with the government. This denies victimized parties recourse before the Mexican judicial system. Therefore, stronger, uniform enforcement procedures should be included in the agreement.

♦ **Establish workable "rules of origin" requirements.** As with the U.S.-Canada Free Trade Agreement, NAFTA probably will include rules of origin, which will give duty-free status to products made substantially in the U.S., Mexico, or Canada. These rules should be aimed at promoting free market reforms among countries outside the NAFTA, while not discouraging investment in North America.

♦ **Provide for effective dispute resolution mechanisms.** Complex environmental and labor safety regulations, as well as overlapping jurisdictions of power in the U.S. between state and federal agencies and federal and state judicial systems have created barriers to trade with Mexico. In October 1990, for example, a federal court in California banned all Mexican tuna imports due to concern over Mexico's use of tuna fishing techniques that allegedly contravened U.S. laws. The lengthy nature of the dispute has heightened tensions between the two countries. Such disputes almost certainly will increase in number as trade increases. The NAFTA should establish a more rapid dispute settlement mechanism so that neither country can use unfair trade, or environmental and labor safety laws, to indirectly create barriers to trade.

♦ **Seek to include Salinas's free-market decrees within the NAFTA.** Since taking office in December 1988, Salinas has issued numerous administrative decrees eliminating cumbersome economic regulations, privatizing state industries, and reinterpreting laws to allow for more foreign investment. These changes risk being overturned by subsequent presidents unless they are institutionalized. This could be accomplished by including the reforms to date within the NAFTA.

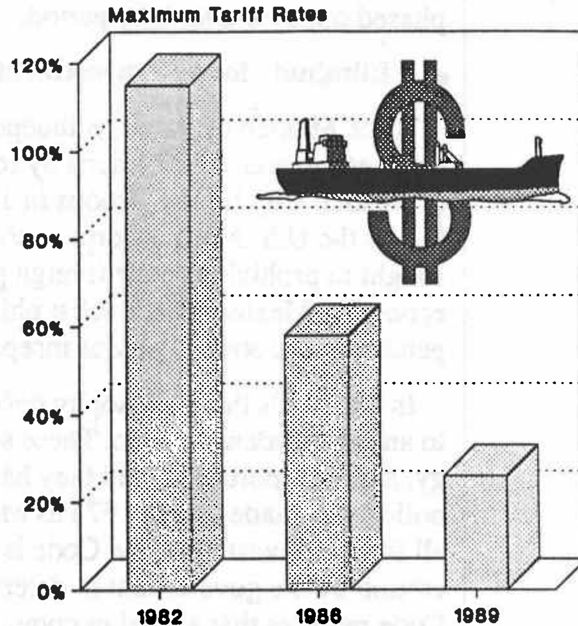
A CHECKLIST FOR A SUCCESSFUL NAFTA

Negotiations on a topic as sweeping as a free trade area will be tough and even, at times, brutal. There will be enormous give-and-take by the delegations. When they complete their work, the draft accord will be judged by U.S. lawmakers, policy makers, the press and, ultimately, the American public. When it comes time to assess how well the U.S. negotiators performed in crafting the North American Free Trade Area, they will deserve high marks if the accord will:

✔ **Rapidly eliminate quotas and tariffs.**

Tariffs between the U.S. and Mexico already are relatively low. Mexico imposes only an 11 percent average tariff on imported U.S. goods, while the U.S. imposes an even smaller 4 percent average tariff on imported Mexican goods. What are not so low are so-called non-tariff barriers such as import licensing and quotas in such key areas as apparel manufacturing, steel, textiles, and some agricultural goods. Mexico, for instance, requires that licenses be obtained, often through cumbersome procedures, for most farm goods that come into Mexico. Some grain imports also are hit with high tariffs. Mexican quotas and tariffs today boost the cost of U.S. grains sold in Mexico by 20 percent. These are high barriers to free trade. A barrier, too, is the import permit still required by the Mexican government on 60 agricultural products including dairy goods, grains, oilseeds

and some horticultural products.[1] Mexican corn is protected with a 70 percent tariff.[2]



U.S. Trade Barriers. For its part, the U.S. places restrictions on imports of products like apparel, cement, glassware, certain horticultural products, steel, and textiles. A reduction of U.S. tariffs on Mexican products would boost Mexican exports. Since the U.S. is a market for 70 percent of Mexican exports, even a small percentage increase in sales to the U.S. would have a significant impact on the Mexican economy. The U.S. moreover, easily can afford to be generous. The reason: The U.S. economy is thirty times larger than Mexico's. Thus concessions on tariffs and other barriers will have little negative impact on the U.S. economy, but will help U.S. negotiators gain greater concessions in areas of keen interest to the U.S., such as market access to sell U.S. products in Mexico and foreign investment in financial services.

The U.S. negotiating team on September 19 submitted its formal negotiating position to one of the NAFTA negotiating groups known as the Market Access Working Group. The U.S. is proposing a "long term" phase-down period of tariffs and quotas for products whose U.S. producers may be hurt by the NAFTA. These include citrus fruit, glasswares and textiles manufacturing. The "long term" envisioned by the U.S. is twelve to twenty years.

The U.S. proposal is unwise and would weaken the NAFTA greatly for two reasons. First, several large industries in the U.S. would seek to be included in the long-term tariff reduction category, thereby reducing the scope of the goods and services open to free trade between the two countries during the next decade. Second, Mexico has many more "import sensitive" industries than does the U.S.,

1 General Accounting Office, "U.S.-Mexico Trade: Trends and Impediments in Agricultural Trade," Appendix I, p. 11.

2 Damien Fraser, "Symbol of Mexican Revolution Threatened," *Financial Times*, July 3, 1991 p. 3.

due to its history of protectionism and the relatively small size of its economy. The Mexicans therefore would seek to include a large portion of their economy within this category, denying many U.S. companies an opportunity to compete fairly within Mexico. Quotas and tariffs therefore should be lifted rapidly, not phased out over a lengthy period.

✓ **Eliminate foreign investment restrictions in Mexico.**

Since Mexico declared its independence from Spain in 1821, the country has suffered several interventions by foreign countries. Among them: the occupation of Mexico City by U.S. troops in 1847, the French invasion in 1861, and the landing by the U.S. Marine Corps in Vera Cruz in 1914. In reaction, Mexico has sought to prohibit or limit foreign participation in its internal affairs, including the economy. Mexico's nationalist philosophy has held Mexican economic independence and sovereignty as inseparable.

In the 1970s this philosophy defined certain sectors of the economy as strategic to an independent Mexico. These strategic sectors are agriculture, banking, energy, and transportation, and they have been off limits to foreign ownership. This policy was made law in 1973 as Mexico's Foreign Investment Code. Regulating all foreign investment, the Code is highly ambiguous, allowing for enormous discretion by the government in determining the property rights of foreigners. The Code requires that a foreign company seeking to conduct business in Mexico must obtain a license from the Mexican government.

Criteria for granting the license include whether the foreign company's "social and cultural values" are suitable, whether the foreign company serves Mexico's "interest" and is connected to "foreign centers of economic decision," and whether the company "contributes to the achievement of [Mexico's] national development policy objectives." Even when foreign participation is deemed suitable, the law limits foreign ownership to 49 percent in almost all of Mexico's major industries, and prohibits foreign ownership in its "strategic sectors."

Creating Confidence. Transportation is one sector covered by the foreign investment law. Regarded as strategic, transportation has benefitted little from foreign investment. Yet Mexico will need tens of billions of dollars over the next decade to construct new airports, bridges, roads, and seaports. Much of this could come from the U.S. It will not, however, unless U.S. investors can control how their capital is used. Salinas, to be sure, already has decreed majority foreign ownership in several sectors of the economy, such as tourism. But this is based on reversible presidential decrees. To create an environment in Mexico that gives U.S. investors confidence, U.S. negotiators should press to permit foreign majority ownership in Mexico's transportation industry.

The oil industry is another sector of the economy where foreign investment is limited. If Mexico allowed greater foreign investment in this sector, U.S. oil companies probably would pump billions of dollars into oil exploration and refining and the production of petrochemicals. The state-run Mexican oil company, *Petroleos Mexicanos* (PEMEX), could permit U.S. companies to invest in oil exploration through concessions known as "built-lease transfer financing." This

financing technique allows the Mexican government to guarantee a foreign company a percentage of all revenues from the oil it extracts from the ground. It is uncertain whether this type of oil exploration by foreign companies would be allowed under the Mexican Constitution, which mandates exclusive state ownership of Mexico's oil reserves. However, subject to Mexico's Constitution, U.S. negotiators should seek to gain greater access for U.S. companies to invest in Mexican oil exploration and refining.

U.S. negotiators also can press the Mexican government to allow greater foreign ownership of Mexico's petrochemical industry. Foreigners should be allowed to own a majority share of a company manufacturing so-called secondary petrochemicals such as synthetic resins and certain plastics. Current law allows only 40 percent foreign ownership. And foreigners should be permitted to buy at least a minority share of PEMEX. Current law prohibits foreigners from possessing any PEMEX stock.

One of the most important areas of the economy where U.S. negotiators should seek permission for foreign majority ownership is the Mexican financial services industry. The movement of capital is one of the central elements of free trade. Free trade in capital benefits all participants enormously. A NAFTA allowing foreign ownership in Mexican financial services industries would see billions of dollars pouring into Mexico. Among other things, such capital would allow Mexico to fund its trade deficit, which was $5 billion last year and is estimated to climb to $6 billion this year.[3]

Lower Cost Loans. An infusion of foreign capital into Mexico's private commercial banks would spur economic growth by providing money to businesses at lower costs.[4] This not only will benefit U.S. banks, but will increase U.S. exports to Mexico as Mexican GNP increases. Foreigners currently can possess no more than 30 percent of a Mexican bank's equity. And individual investors, both Mexican and foreign, are limited to a 5 percent share. The penalties for exceeding these limits are draconian. Example: the government can force a violator to sell his bank shares back to the bank at half their value.

The Mexican government also limits foreign participation in a bank's board of directors. It prohibits, for example, foreign board members who have alliances with "foreign centers of economic decisions," which the government fails to define in the regulations. Laws that allow government intervention in the manage-

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3 Mexico's current account deficit is expected to increase to $30 billion within the next five years. The only way for Mexico to finance this deficit while keeping inflation under control will be to attract large amounts of foreign capital. Since international financial organizations such as the International Monetary Fund and World Bank are unwilling to fund Mexico's growth through large development projects, Mexico's only option is to seek capital through the private banking system. For more information on Mexico's bank privatization, see Robert Salinas, "Privatization in Mexico: Good But Not Enough," Heritage Foundation *Backgrounder* No. 797, November 18, 1990, p.13.

4 Real interest on commercial loans in Mexico is approximately 4 to 6 points higher than in the U.S.

ment decisions of banks should be eliminated under a NAFTA, especially when that intervention discriminates against foreign owners.

The U.S.-Canada Free Trade Agreement provides a good starting point for U.S. negotiators when seeking foreign investment concessions from Mexico. Under the FTA, Canada dramatically has reduced limitations on U.S.ownership of businesses in Canada. U.S. companies now can become complete owners of Canadian companies valued under $100 million. Next year this ceiling will be raised to $150 million. Salinas's decrees allow foreign investors to acquire 100 percent ownership of companies in some industries, such as tourism. These decrees and regulations should be included in a NAFTA so they will have the force of law. With greater foreign investment, key Mexican industries like banking, energy, and transportation will grow and spur growth in the rest of the economy.

✓ **Obtain access to Mexico's markets.**

Despite the progress Salinas has made in privatization, the government still owns or controls a large part of the Mexican economy. Mexican state-owned or -controlled industries are inefficient and burden the Mexican economy. They also send a strong message to Mexican and foreign investors that the government is still deeply involved in the market. This discourages private investment. A study released by the U.S. General Accounting Office this May 3, finds that many U.S. petrochemical firms would not invest in Mexico because of the Mexican government's monopoly ownership of the petrochemical industry.[5]

The pace of privatization and the sale of Mexican state-owned enterprises to the private sector are not part of the NAFTA negotiations. What U.S. negotiators can make part of the talks is the right of U.S. companies to compete with state-owned and heavily regulated Mexican firms. U.S. companies should be able to compete for Mexico's government procurement contracts and for servicing contracts for all of Mexico's state-owned companies such as PEMEX. The NAFTA also should allow U.S. companies to sell directly on the Mexican market products that compete with the output of state-owned and heavily regulated industries.

✓ **Eliminate restrictions on the production of goods and services.**

The Mexican government for years has imposed production requirements on foreign firms in Mexico. These laws and regulations limit the amount of profits that foreigners can take out of Mexico, mandate that products manufactured by these companies contain a certain share of domestically produced parts, and require that companies selling goods on the Mexican domestic market also must export goods.

Salinas has eliminated or reduced some of these requirements. Nevertheless, Mexican law still requires foreign companies to maintain a foreign currency

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5 Dolia Estevez, "U.S. Chemical Firms Want In," *El Financiero International*, July 8, 1991, p. 4.

budget surplus during the first three years of operation in Mexico.[6] This law is intended to pump hard currency into the economy and strengthen the weak *peso* by encouraging companies to buy Mexican products with *pesos*. In reality this law restricts Mexican-based subsidiaries of foreign companies from buying the best components for their products in the international market. It also prevents them from repatriating profits. Unable to make large enough profits, foreign companies are reluctant to invest in Mexico. A NAFTA should eliminate these kinds of restrictions.

Other Mexican laws restrict how businesses can use their property. The July 1990 Law of Credit Institutions, for example, authorized the privatization of the eighteen state-owned commercial banks. Yet the law also gives the government's National Banking Commission power to approve or disapprove "the naming of the bank President and his officers, and other officials directly below the President ...[in order to] avoid inconvenient or unsuitable actions for the [banking] system." This gives the government a strong say over the election of board members and top-level bank officials. This discourages foreigners from acquiring banks or investing large sums of money in the Mexican banking system. The lack of foreign investment will retard the growth of financial services in Mexico.

Another Mexican production law requires that various products produced in Mexico, even if produced by Mexican-owned firms, be made from components produced in Mexico. These laws discourage foreign investment and should be eliminated by NAFTA. As a model, negotiators could use the provisions in the U.S.-Canada Free Trade Agreement that prohibit production requirement laws in Canada and the U.S.[7]

✓ **Increase safeguards for intellectual property rights.**

Since so many U.S. companies rely on strong intellectual property protections when operating outside the U.S., U.S. negotiators should seek to strengthen intellectual property rights protections within a NAFTA. Like those of most developing countries, Mexico's intellectual property laws to protect a company's patents, trademarks and copyrights have been lax. This has improved dramatically by enactment this June of the Law on Development and Protection of Industrial Property. Still the law fails to protect intellectual property in several areas, among them biotechnology industries. The law also requires licensing of inventions. All this discourages investors. U.S. negotiators should seek to remedy these weaknesses in the law by changing them with the NAFTA.

There also has been some improvement on copyright protection in Mexico. On July 3 the Mexican Congress amended its copyright laws to prevent the illegal duplication of copyrighted material. But according to Eduardo Gaxiola, a lawyer

6 Regulations of the Law to Promote Mexican Investment and to Regulate Foreign Investment, *Official Gazette of the Federation*, May 16, 1989, Title 2, Art. 5, Par. IV.

7 U.S.-Canada Free Trade Agreement, Chapter 16, Art. 1603.

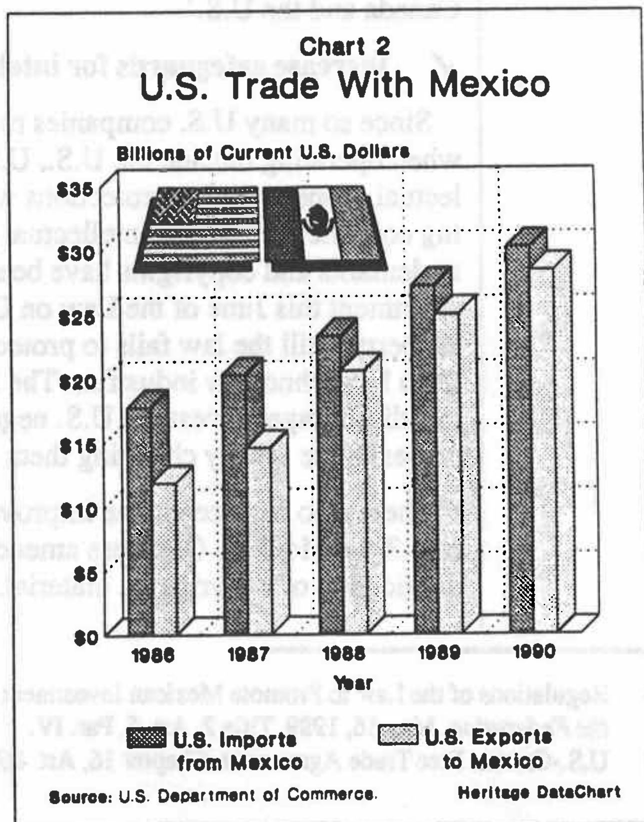
representing the Motion Picture Association of Amer. the new laws do not prohibit the unauthorized copying of films and recordings. Most important for U.S. companies, neither law allows private parties to sue (only the Mexican government can bring suit against potential violators) nor requires the government to stop the illegal activity while a case is being decided.

American computer companies invest large sums of money in research into new software programs, only to find them pirated by Mexican companies. U.S. companies lose an estimated $200 million to $250 million annually because Mexicans illegally copy their products. Of this amount, the American entertainment industry forfeits $32 million, the computer software industry $90 million, and the pharmaceutical industry an estimated $100 million per year. Because of these losses U.S. companies have a large stake in ensuring that any NAFTA has adequate provisions to protect their property. Therefore, U.S. negotiators should not only seek to improve intellectual property laws, but should establish more uniform methods of enforcement of intellectual property rights, such as the right for U.S. companies to bring suit on their own behalf.

✓ Include Salinas's free market decrees within the NAFTA.

Salinas's decrees that have liberalized the Mexican economy are not irreversible. Most of his liberalization reforms have been by fiat and by interpreting existing laws very liberally to allow a free market to take hold. Past Mexican administrations also used the strong powers that the Constitution gives the president to regulate the economy through decrees. But such executive decrees can be reversed at the whim of the next president, or even the current president. This creates uncertainty in the economy. Private investors, particularly foreigners, are unwilling to invest large amounts of money in industries that could once again be expropriated, or forced into bankruptcy through heavy regulation.

The Mexican petrochemical industry is one area where Salinas's decrees allow foreign participation once limited exclusively to the Mexican government and Mexican nationals. So far, understandably, the decrees are not enough to convince foreign investors that their



property rights are protected adequately. This July, the Washington, D.C.-based U.S. Chemical Manufacturers Association stated that it lacked confidence in free market reforms administered by presidential decrees because "a different Mexican admini-stration could interpret the law differently, and change the existing regulations."[8]

U.S. trade negotiators should seek to include Salinas's reform decrees within the NAFTA by creating provisions preventing any signatory country from reinterpreting existing laws in conflict with NAFTA rules. Since the NAFTA will be approved by the Mexican Congress, these decrees then would have the force of legislation and could not be overturned easily by subsequent Mexican governments.

THE U.S. CONTRIBUTION TO FREE TRADE

The U.S. needs to do its part in opening its market to Mexican goods. The U.S. levies tariffs on Mexican imports that average 4 percent of the total value of the imported goods. It also imposes quotas on several important Mexican exports, such as apparel, glassware, and certain horticultural goods. As a bargaining trade-off to convince the Mexicans to open their economy further, the U.S. should:

♦ **Quickly lower existing tariffs and reduce quotas on all Mexican goods entering the U.S.**

This could go a long way in prodding the Mexicans to remove their barriers to foreign investment, to protect property rights, and to take other measures to reform their economy. Most Mexican business leaders want free market reforms, but some fear competition with American companies if NAFTA is approved. By lowering U.S. tariffs on Mexican goods, and eliminating quotas, Washington could help persuade Mexican businessmen to support a NAFTA.

♦ **Establish workable "rules of origin".**

Rules of origin will mandate how much of a product can be made in a non-NAFTA country and still be given tariff-free status when sold in a NAFTA country. The U.S.-Canada Free Trade Agreement requires that 50 percent of the value of a product on some products sold in the U.S. or Canada must be made in either of the two countries. During the NAFTA talks, early agreement is expected on rules of origin in order to guarantee support of the agreement in the U.S. Congress, which has insisted on strict rules of origin.

A too strict rules of origin law, however, could hurt the competitiveness of U.S. companies wishing to sell products within the NAFTA and abroad. Such a law may require U.S. companies to make products from components made in a NAFTA country that are more expensive than components made elsewhere. U.S.

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8 Estevez, *op. cit.*

competitors may then underprice U.S. companies by finding cheaper components in non-NAFTA countries.

In addition, excessive rules of origin could persuade many companies to maintain their operations in non-NAFTA countries. This would happen if a company saved more money by facing the regular U.S. tariffs on imports than if it relocated within a NAFTA country and then had to find all its components for manufacturing its product within the NAFTA.

There is, however, a reason to have a rules of origin requirement. If there were no rules of origin, foreign companies could make their products in non-NAFTA countries and then reroute them through Mexico or Canada to take advantage of the duty-free status those products would enjoy as they entered the U.S. This would weaken the benefits to companies within the NAFTA as they sell their products to the U.S. tariff free.

♦ **Provide trade dispute resolution mechanisms.**

In October 1990 a federal district court in California issued an injunction banning the import of tuna from Mexico. The ruling was based on evidence that Mexico's fishing fleet was harvesting fish with techniques that killed too many dolphins and sea turtles. Federal law prohibits the import of certain foods harvested in a way that kills certain marine wildlife, including dolphins and turtles. This September 3 a General Agreement on Tariffs and Trade (GATT) panel recommended overturning the tuna ban, finding it was a violation of GATT's rules on non-tariff barriers to trade. The ban is still in place pending a final ruling by GATT. In the meantime, the Mexican fishing fleet continues to lose tens of millions of dollars in export revenues to the U.S.

Disputes like this, involving unfair trade practices, labor safety, and environmental violations, will increase as trade between the U.S. and Mexico increases. While some disputes are over genuine differences, many disputes are created by companies as a means of protecting themselves from fair competition. An effective free trade area requires a mechanism that sorts out the genuine from the contrived disputes. U.S. negotiators should point to Chapter 18 of the U.S.-Canada Free Trade Agreement as a model for a trilateral commission to resolve trade disputes between the three NAFTA countries. Under Chapter 18, trade disputes between the U.S. and Canada are brought before a commission composed of officials from each country. Disputes must be settled within nine months, and in several cases, the decision of the tribunal is binding on the parties.

♦ **Exclude Mexico from U.S. anti-dumping and countervailing duty laws.**

In 1897 the U.S. began using "anti-dumping" laws to prevent foreign companies from selling products on the U.S. market at prices below their production cost. These laws also prevent foreign governments from giving subsidies to companies to allow them to dump. Such laws aim at preventing companies from underpricing U.S. competitors and then raising prices once the American firms are forced out of business. These laws are not intended to regulate companies located within the U.S. that compete against other U.S. companies.

Since the NAFTA will seek to harmonize rules and regulations governing businesses, companies in Mexico by and large should be treated like those in the U.S. Mexican firms thus should not be subject to anti-dumping laws. A major reason for anti-dumping legislation was to counter a foreign government's use of export subsidies. Yet NAFTA itself should prohibit Mexico from subsidizing Mexican companies that export to the U.S. Exempting Mexico from most U.S. anti-dumping legislation also would support the broader outlines of the free trade accord with Mexico that seeks to accord equal treatment to U.S. and Mexican companies operating in the U.S.

- **Allow Mexico greater access to U.S. government contracts.**

During the past four decades, the economic power of the U.S., Canadian, and Mexican federal governments has grown dramatically. These governments limit or prohibit foreign companies from bidding on government contracts. Under the U.S.-Canada Free Trade Agreement, Washington agreed to allow Canadian companies to bid on up to 10 percent of all U.S. government contracts awarded to private companies. This 10 percent limit was a step in the right direction, but only a very small step. NAFTA now should go further and remove the ceiling. It dramatically limits the ability for foreign companies to compete. NAFTA should require equal treatment of Mexican and U.S. companies when bidding on U.S. government contracts. More open bidding would result in stronger competition and better services to the government.

CONCLUSION

Successful U.S., Canada, and Mexico negotiation of a North American Free Trade Agreement depends not just on how many tariffs are reduced or how many trade quotas are eliminated. It depends too on how well trade problems are resolved in areas like investment, services, and free competition in the domestic markets of the NAFTA countries. Unless Mexico reforms its foreign investment laws, improves protection of private property rights, and further privatizes its economy, its economy will not develop and create a larger market for U.S. goods.

Mexico's economic importance to America will rise only as the Mexican economy grows. Therefore, U.S. negotiators should press for Mexican economic reforms that will transform Mexico into a free market democracy. These reforms, included in the NAFTA should:

- Allow majority foreign ownership in many industries where the Mexican Constitution allows little or no foreign participation, such as oil, transportation and telecommunications.
- Allow foreign majority ownership in Mexico's financial services industries.
- Allow foreign access to Mexico's market to compete against *Petroleos Mexicanos* (PEMEX), for the refining and sale of oil and petrochemical products.

- ♦ Seek guarantees on private property rights — including patents, copyrights, and other intellectual property.
- ♦ Seek limits on the Mexican government's power to control businesses through laws such as production requirements.

In return, the U.S. should reduce the existing tariffs rapidly and eliminate quotas on Mexican exports. In addition, the U.S. should exclude Mexico from U.S. anti-dumping laws and should create a dispute resolution mechanism within the NAFTA that will enable NAFTA countries to quickly settle trade disputes.

If U.S. trade negotiators push these changes and produce a draft treaty that contains them, then the negotiators will have served all of North America well.

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