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A North American Community: A Proposal to Deepen NAFTA

What the highway builders of North American regionalism perhaps need most is a few good surveyors who can take the lay of the land and give the highway engineers, as well as the future drivers, a feeling for what lies ahead.[1]

—Charles F. Doran

Canada, Mexico, and the United States do not view themselves as parts of a region in the way that France and Germany view themselves as part of the European Union, but the idea of a European identity did not spring up fully formed in 1957. Indeed, even today, although most everyone living in France or Germany views themselves as French or German, they do not feel that they compromise their national identity by also viewing themselves as European.[2] Despite the differences in origins and paths between the two organizations, Europe's experience with integration during the past 40 years yields lessons that can facilitate the development of a North American Community.

The first, perhaps most important, lesson is that the European Community has succeeded because, like all great experiments, it began with an idea—that Europe could prosper only if it remained peaceful, which would only be possible if its sovereign states combined in a new cooperative entity. That idea was written into the preamble to the Treaty of Rome,

1. Charles Doran, ''Introduction'' to *A New North America: Cooperation and Enhanced Interdependence*, ed. Charles F. Doran and Alvin Drischler (Westport, CT: Praeger, 1996), xii.

2. Gary Marks, ''Territorial Identities in the European Union,'' in *Regional Integration and Democracy: Expanding on the European Experience*, ed. Jeffrey A. Anderson (Lanham, MD: Rowman and Littlefield Publishers, 1999), 69-91.

and it has been repeated and expanded in subsequent treaties to inspire the people of Europe to embark on a great journey.

In contrast to Europe, North America is more market-driven, more resistant to bureaucratic answers, more pragmatic, and more respectful of national autonomy. Despite these differences, however, North America can learn from Europe on the importance of defining goals that inspire a unity of purpose and on the necessity of establishing institutions that can help translate these goals into cooperative policies. After identifying these goals and organizations, this chapter will offer three proposals: on infrastructure and transportation, trade policy, and macroeconomic policy coordination and the possibility of a common currency. These represent the spine (transportation) and the limbs (trade and finance) of a North American Community. In the next chapter, we will develop specific plans for customs and immigration, energy, regional development, and education. These issues are illustrative of the range of issues that a North American Community could address. We will then discuss the question of how North America should move from a free trade area to a Community of nations and peoples.

This proposal for a North American Community represents a formidable leap for three governments that have not even begun to look across the chasm, let alone consider jumping. In chapter 7, we will examine each government's reservations, and we will ask three questions: Are the plans developed in chapters 5 and 6 feasible? How can the governments be reorganized to increase the prospects for a partnership? And can the fears about the erosion of sovereignty be overcome? Remarkably, we will find that the public in all three countries is significantly ahead of its leaders—that in fact they are ready to consider more serious steps toward political union, provided that their quality of life would improve. Let us, however, start at the beginning.

In the Beginning: Revising the North American Preamble

In comparison with the lofty declaration in Europe's founding treaty, the preamble to the NAFTA Treaty is written more like a business contract. The three governments resolved, in the NAFTA preamble, to ''create an expanded and secure market . . . reduce distortions to trade . . . [and] enhance the competitiveness of their firms . . .'' In response to criticisms raised by unions and environmentalists, the negotiators inserted a pledge at the bottom of the preamble to enforce environmental laws and workers' rights, but the tenor of the language did not change. The governments acted as if they were three large corporations signing a contract to permit their businesses free rein to produce and trade cheaper and better goods.

The governments shortchanged their people by defining the North American relationship solely by commerce. The leaders should return to the drawing board and sketch a vision of the future and of North America's place in it. They have much with which to work. North American society is changing in ways that reflect a convergence in values and interests. Migration has melded all three countries, making Canada and the United States more genuinely multinational and also somewhat more like Mexico. Residents of North America visit each other's countries more than they travel anywhere else in the world. Cities, states, and provinces are becoming partners. Professional societies hold North American conventions. Canada's Museum of Civilization, the US Smithsonian Museum, and Mexico's Museo de Arte collaborated in early 2001 to create "Panorama: The North American Landscape in Art," an online art show exhibiting 300 landscape paintings by artists of the three countries.[3] Society—not government—is in the lead. It is now time for governments to articulate a modern definition of North America that goes beyond dismantling trade barriers and provides direction and added impetus to construct a North American Community.

What makes NAFTA unique in the world is the integration of a developing country with two industrial ones. This experiment is important not just for the people of North America, but for the rest of the world, because a central challenge of the 21st century is how to integrate developing countries into the modern world economy. So the issue for North America is how to assure that the integration is successful and becomes a model worth emulating by other regions. Can a framework of policy coordination be established that can anticipate and solve problems before they become sources of tension? Can it help governments view future opportunities with sufficient clarity so that they will quickly marshal their resources to seize them?

"Integration" can be defined as a process by which two or more parties come together to form a whole or a new relationship. This process usually involves exchanges of goods, people, and cultures. For integration to occur smoothly, the parties need to define the rules for the exchanges and institutions to manage and enforce the rules. Integration does not mean, for example, that the three official languages (and many "unofficial" ones) should be compressed into a single official language, but rather that the continent should permit space for all cultures and languages and offer incentives for people to learn and use each other's languages. Economically, it should mean that no region or group is excluded or left to stagnate. To the contrary, special programs should aim to lift those regions or groups so that they have a stake in their societies and in North America. With some leadership, it should not be difficult to draft a revised

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3. See http://www.virtualmuseum.ca/panoramas.

preamble for a deeper NAFTA, because it can build on norms that have roots in all three countries. Those norms should include:

- respect for cultures, religions, and languages;
- a spirit of inclusiveness, openness, and reciprocity;
- a commitment to democracy, the fundamental rights of the individual, and the rights of individuals to associate with others in groups;
- support for a free market as the best mechanism to produce goods and services, but tempered by the obligation of the Community to assure that the distribution is not unjust, that disparities are reduced among peoples, nation-states, and regions, and that everyone has an equal opportunity to achieve his or her potential;
- the aim of achieving a wider Community in North America, one that respects the differences among peoples and nation-states and encourages experimentation among groups or states, but also one that provides incentives to approach collective problems with a common approach; and
- a commitment to fostering the free, unfettered movement of goods, services, capital, and eventually people, but also to assuring public security and the cooperative, coordinated enforcement of laws by officials of the three governments.

These ideas represent a rough outline of some of the goals that a deeper North American Community might pursue. Each norm or goal requires a fuller exposition, but let me here elaborate on the last one. Although the three countries were only getting used to the idea of a free trade agreement, Mexican President Fox proposed a common market with free movement of labor as well as goods, services, and capital. This is a bold idea, and not one that can be implemented anytime soon, and Fox has said as much. *But he is right to sketch a future picture of the trilateral relationship*, because this picture lifts the thoughts of those working on different bilateral or trilateral issues and helps people understand that the issues that concern them are related to each other—as they are. The precise nature of their relationship does not need to be decided now; indeed, the Europeans, who have been wrestling with these issues for 50 years, are still debating them and remain far from a consensus.

Nonetheless, what is lacking in North America is a picture of the future given by our leaders, and that is what the idea of a "Community" is intended to evoke. The governments should discuss this concept at both conceptual and practical levels. Over time, one hopes that the two levels will converge in forming a Community.

A consensus on general principles can provide a framework to guide the talks on specific policies. However, the proper way to define North

American goals would be through summit meetings of the three leaders, and ultimately through an assembly of the people's representatives.

North American Institutions

If the European Union's mistake was to establish too many institutions, NAFTA made the opposite mistake of failing to establish any that were serious. To grasp problems that are transnational or international, member states of a free trade area have two options: they can react to one crisis or dispute at a time, or they can establish an organization with the capacity to manage or solve problems before they become crises. NAFTA has adopted the first option, and we have seen its limits.

Before proposing new organizations for NAFTA, however, it is worth recounting why they do not exist. In most cases, strong countries tend to resist international organizations because they do not want to be constrained and because their relative power is greater in a bilateral context. This explains the reluctance of the United States,[4] but in North America, the two weaker countries, Canada and Mexico, have been equally cautious, albeit for a different reason. They believe that they could better pursue their interests in a bilateral context.

The historical evidence does not confirm this belief in bilateralism. Rather, it shows that most disputes take a long time to be resolved, and often leave the overall relationship worse than before. It would be far better to handle such disputes in a neutral, rule-based forum. This actually insulates nation-states from their own interest groups, while giving the groups a chance to petition for claims. Some recognize the power of this idea. Hart, a Canadian trade negotiator, analyzed the dispute-settlement mechanism and concluded that "the new, more binding procedures have helped the management of Canada-US relations," and that a rule-based mechanism is "highly desirable . . . for the smaller, less powerful partner."[5] Yet the leaders themselves are either reluctant to accept the need for organizations outside the trade area, or they simply lack the understanding or imagination to create them. And there is yet *another* powerful reason for *trinational* organizations: *They would permit NAFTA to be something more than the sum of two bilateral relationships.*

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4. US policy in the 20th century has alternated between a narrow definition of its interests, when it views international organizations as constraints, and a more visionary approach, when it helped establish critical international institutions: the IMF, NATO, the OAS, the United Nations, the World Bank, and the WTO. See Robert A. Pastor, "U.S. Foreign Policy: Divided by a Revolutionary Vision," chap. 6 in *A Century's Journey: How the Great Powers Shape the World*, ed. Robert A. Pastor (New York: Basic Books, 1999).

5. Michael Hart, "The Role of Dispute Settlement in Managing Canada-U.S. Trade and Investment Relations," in *Canada Among Nations 2000: Vanishing Borders*, ed. Maureen Appel Molot and Fen Osler Hampson (New York: Oxford University Press, 2000), 107, 113-14.

The hesitation has some redeeming value. The EU experience teaches us to be wary of creating new bureaucracies. They grow, particularly in times of crisis, but rarely shrink, even though their time may have passed. The antidote, however, is *not* anarchy, but rather to carefully establish organizations with a clear need and mandate, a small staff, and a ''sunset provision'' of, say, 10 years, which would lead to a phaseout in the absence of a deliberate decision by the governments to extend its lease.

The first such institution to be established should be a North American Commission (NAC). It should be led by 15 distinguished individuals, 5 of whom would be appointed by each of the leaders of the three countries, for a fixed term. Together, they would select a chair, who would alternate, say, every 2 years. It should be staffed by a mix of civil servants and independent professionals designated by the three countries. Its mandate would be to develop a plan for the integration and development of North America.

This preliminary plan—or rather the outline of such a plan—should be developed within 6 months to serve as the agenda for the three leaders at a summit meeting. The plan should begin with a carefully crafted list of goals—along the lines of the revised preamble described above—together with a range of options for achieving these goals. In addition, the NAC might choose one sector—say, transport and infrastructure—and propose a plan. The three leaders, together with representatives from the national legislatures, should respond to the NAC's recommendations and then meet every 6 months to review progress toward its implementation. The NAC should supervise working groups and the NAFTA commissions on labor and the environment and instruct them with precise, operational objectives.

The NAC should have two offices to help prepare sectoral and continental proposals: an Office of North American Statistics to collect data from the three governments and research organizations, and a North American Planning Office to analyze the data. Working with appropriate ministries in the three governments as well as with universities and research centers, the NAC should draft papers on ways to improve cooperation and facilitate integration. It should also consider an explicit ''regional policy'' to reduce disparities within North America.

Lacking a planning body, the three governments were not prepared to respond effectively or quickly during the peso crisis in December 1994. Without a group whose job is to think about the interrelationship of issues, each government—or, more precisely, each ministry—would continue to deal with one issue at a time and fail to see the relationship between uneven development in Mexico and immigration and drug trafficking to the United States. The North American Commission should also serve as a catalyst for the three countries to coordinate selected domestic, foreign, and trade policies.

The NAC also should educate the public on the existence and potential of the region and seek to instill a sense of regional identity. It should try to alleviate anxieties about integration among certain groups and devise policies that respond to NAFTA-related problems. It should provide funding to establish Centers for North American Research and Studies in all three countries. These would be similar to the 10 European Union Centers that the EU funds in the United States. The NAC should also serve as the center of a network of NGOs, business and labor groups, and partnerships between cities and states or provinces and universities.

The North American Commission, in brief, would be very different from the European Commission. Instead of a large, supranational executive, managing the continent's affairs, the NAC would be lean, independent of the governments, and advisory to the three leaders and legislatures. Each leader would continue to rely on his own staff and Cabinet to prepare for meetings and manage relations. The NAC would provide a North American agenda and perspective, encouraging the leaders to take into account the other countries and to contemplate future opportunities and problems. Nor would the NAC be pulled into the business of proposing a tripartite industrial policy when no country is interested in one. But one hopes that over time, and as the three governments become more comfortable with the NAC, that they might delegate more responsibility and seek its advice more often.

Establishing such a Commission will require an act of statesmanship and a recognition that a quasi-independent advisory body is the only way for the three leaders to be drawn toward a common long-term agenda. But there are three other options. The first and most likely is the status quo because many leaders would be reluctant to establish a Commission, which they could not control. But the status quo is an ad hoc bilateral bureaucratic response, such as occurs regularly on immigration and drugs between Mexico and the United States, or on border management between Canada and the United States. This approach, however, tends to produce a narrow, short-term product.

The second approach would rely on a private commission of distinguished individuals established under the auspices of nongovernmental institutes in the three countries. The advantage of such a private commission is that it would be free to propose new ideas; the disadvantage is that it would be unlikely to engage the three leaders in the same way as an organization that they choose to establish.

The third approach would be a classic intergovernmental organization (IGO), a group established by the three governments, managed by its civil servants, and wholly responsible to the three governments. The model would be the European Commission, and it would report to the governments and have supervisory authority over NAFTA affairs. There are assets and liabilities to such an IGO, and in the long-term, this approach might be inevitable and desirable. But the leadership in the three governments do not appear to want to proceed down this path at this time, and a compelling case could be made for developing a new and different kind of system to respond to the unique needs of North America. The question, then, for the prime minister and two presidents is whether they want to raise "North America" to a new level and try to create a legacy that will shape future generations of North Americans. If the answer is "yes", then they need to establish a responsible, semi-autonomous, agenda-setting North American Commission to propose and monitor a plan.

The second organization should be a North American Parliamentary Group (NAPG), which would be composed of legislators from the Canadian Parliament, the Mexican Congress, and the US Congress. In fact, forming this organization only would require merging and revitalizing two existing parliamentary groups. In 1960, the US Congress established the US-Mexican Inter-Parliamentary Conference, and a few months later it did the same with Canada. These groups have met periodically since then, but they remain separate. As such, they reflect the dual-bilateral character of North America. If the three governments commit to North America, it would be logical to merge these two bodies.[6]

The NAPG would broaden the horizons of all three legislatures, but US border-state legislators, who have concentrated on US relations with either Mexico *or* Canada, would probably profit the most from the introduction of a third perspective. There are already some signs of interest by legislators in joining the two perspectives and groups. At the 40th Annual Meeting of the US-Canadian Inter-Parliamentary Group in Quebec in 1998, Val Meredith, a Canadian Member of Parliament from British Columbia, was asked to prepare a report on "Trade Corridors." She took the mandate seriously and explored not just US-Canadian border issues but also those between the United States and Mexico. The report analyzed the costs of not having a continental transport system and offered recommendations on what the three governments should do.[7]

Any serious attempt to coordinate policies on North American issues inevitably collides with the federal structures of the three governments. In Canada and the United States, and increasingly in Mexico, subnational governments have substantial power and autonomy. For that reason, the North American Parliamentary Group should set up "federal task forces" on different issues, involving provincial (and state) premiers (and governors) and legislators. Assuming that the NAPG concludes that a "North American Transportation Plan" is necessary, then each country first will

6. For an elaboration of this proposal, see Robert A. Pastor and Rafael Fernandez de Castro, eds., *The Controversial Pivot: The U.S. Congress and North America* (Washington: Brookings Institution, 1998), chap. 8.

7. See Val Meredith, M.P., *Trade Corridors: A Report to the Canada-U.S. Inter-Parliamentary Group* (Ottawa, 2000).

need to establish uniform procedures, and that will require gaining agreement among the states.

Another idea would be to organize groups from different regions of the country. There is already a Binational Association of Western Governors and Premiers from the United States and Canada, which began meeting informally a decade ago and now meets annually.[8] Governors from both sides of the US-Mexican border have also been meeting regularly. Both groups should be encouraged to meet with the NAPG as well as with the NAC to exchange ideas and concerns.

The third institution should be the Permanent North American Court on Trade and Investment. This would also involve upgrading the existing dispute-settlement mechanism. As we have seen, dispute panels have worked well, but they are running into problems due to their ad hoc nature. Because panelists are not well paid, it has proven more and more difficult to locate expert panelists who do not have a conflict of interest. Moreover, the case law that has accumulated during the past decade requires an investment of time that few people without a conflict of interest would have. That is why the time has come to establish a permanent court and appoint judges for extended terms. The court must also make its proceedings public, particularly on NAFTA Chapter 11 suits, because of the controversy that has swirled around corporate claims that affect environmental or other public policies. Some narrowing or clarification of the scope of Chapter 11 is also needed to reestablish the credibility of the panels and to prevent the erosion of environmental rules.

A fourth set of organizations would involve meetings of cabinet ministers. Since the late 1970s, each new administration in Mexico and the United States gave a new name to binational cabinet meetings. Initially, these meetings oriented ministers with domestic portfolios, but each then pursued his or her own agenda. Most viewed the binational commission meetings as they did cabinet meetings—as diversions from their work. This problem was compounded with the dual bilateralism of North America. These meetings might be more effective if the North American Commission were to set an agenda and to organize them.

One additional idea to promote a North American identity—or at least a sensitivity to the other countries' perspectives—would be to exchange personnel from the executive branch of each government and staff from the legislatures for tours of 2 or 3 years. To the extent that each government begins to look at the others as strategic partners rather than as objects of fear or suspicion, officials might begin to view their work in other governments' ministries as natural and as an opportunity to explore areas of cooperation.

8. "What Border? Together Canadians and Americans Are Redefining the Nature of Their Common Frontier," *Time/Canada*, 10 July 2000, 22-28.

A North American Plan for Infrastructure and Transportation

If the purpose of NAFTA was to reduce transaction costs in doing business between the three countries of North America, then it has failed. The reduction in the tariff barriers has been exceeded by the increase in costs due to delays at the border and bureaucratic impediments and duplications at both borders. ''Crossing the border,'' concludes a May 2000 report by a Canadian member of Parliament, ''has actually gotten more difficult over the past five years.'' The causes are twofold. ''While continental trade has skyrocketed, the physical infrastructure enabling the movement of these goods has not.'' And second, the bureaucratic barriers that confront cross-border business make the infrastructural problems seem ''minor in comparison.''[9]

There are 64 different jurisdictions in North America that set regulations for trucks, and a study undertaken by the three governments under the auspices of the NAFTA Land Transport Standards Subcommittee concluded that ''there is no prospect of developing complete consensus within North America on a common set of truck weight and dimension limits.''[10] The announcement by senior officials that an agreement on a subject as important as the safety of trucks was impossible among the three countries is stunning. The elected leaders should have been embarrassed and would have been, if anyone had been paying attention.

The cost of failing to set uniform standards is exorbitant in terms of safety and cost. Ignoring the different regulations could lead to the deterioration of roads and bridges and endanger drivers and pedestrians. Or truckers could obey the rules, and that would mean that a truck could not travel between Canada and the US-Mexican border because it would be impossible to comply with dozens of incompatible rules.[11] Heavier, long-combination trucks that are popular in Canada and Mexico, for example, are not permitted on US highways.

The problems are actually more severe within the countries than between them. Double-trailer trucks traveling south on the midcontinental corridor from the Dakotas are not permitted in Iowa, and the Oklahoma-

9. Meredith, *Trade Corridors*, 8, 7, 10.

10. NAFTA Land Transportation Standards Subcommittee, Working Group 2, ''Harmonization of Vehicle Weight and Dimension Regulations within the NAFTA Partnership,'' photocopy (October 1997), 2. The authors' frustration, if not parochialism, was evident in their comment that ''there is no other field of public policy which is more complex than truck size and weight limits'' (p. 1). For the number of jurisdictions, see p. 35. There are 51 state jurisdictions (including Washington, DC) in the United States; and 12 provincial ones in Canada; only Mexico has a single set of rules. For this section on transportation, I am especially grateful for the research assistance and papers prepared by Ben Goodrich and Mary Scott Pearson.

11. Meredith, *Trade Corridors*, 11.

based tractor semi-trucks weighing 40,825 kilograms are not permitted in Texas. And it is not just weight limits that prevent trucks from moving from one jurisdiction to another, but also truck configurations (height, width, number of axles). Moreover, the differing standards on sulfur content of diesel fuel can affect truck ignition systems, engine performance, and maintenance.[12]

On the border, the cost of delays is quite steep. The Canadian Trucking Alliance calculated that for every minute that all trucks are held at the border, an additional Cn$8 million is added to the direct costs of cross-border shipping. With an average delay at the most frequently used border crossing between Canada and the United States of about 20 minutes, that means additional costs of roughly $160 million.[13] The wait at the US-Mexican border is much longer, and the ''drayage system'' described in chapter 4—under which containers might be transferred seven times—adds a substantial hidden cost to commerce.

Subcommittees of NAFTA working groups have already prepared books of statistics on the roads, railways, seaports, and airports of all three countries, together with the number of vehicles, the amount of investment, and the description of the standards and regulations applied within each country. The data are impressive, and reflect, as we have come to expect, a major imbalance within North America. In 1996, Mexico had a total of 12.4 million vehicles, of which about two-thirds were cars and one-third were trucks and buses. Canada, with a population of one-third of Mexico's, had 17.2 million vehicles, of which about three-fourths were cars. The United States had 210 million vehicles, of which 68 million were light trucks and 7 million were commercial vehicles.[14] To put it another way, Mexico's fleet of vehicles was roughly comparable to that of Texas, whose population is one-fifth of Mexico's; and Mexico's highway network (242,000 kilometers, with only 49,000 of those classified as main or paved roads) is comparable to that of Kansas, which has just 5 percent of Mexico's population.[15]

From a policy and resource standpoint, the number of overlapping jurisdictions is such that none of the three countries has a national infrastructure and transportation plan, let alone a continental one. The United

12. Barry M. Prentice and Mark Ojah, ''NAFTA in the Next Ten Years: Issues and Challenges in Transportation,'' Transport Institute, University of Manitoba, paper presented at the NAFTA in the New Millennium Symposium, University of Alberta, Edmonton (24-25 May 2001).

13. Meredith, *Trade Corridors*, 9.

14. US Department of Transportation, Statistics Canada, and Instituto Mexicano del Transporte, *North American Transportation in Figures*, BTS00-05 (Washington, 2000), table 12-1.

15. William R. Black, ''North American Transportation: Perspectives on Research Needs and Sustainable Transportation,'' *Journal of Transport Geography* 5, no. 1 (1997), 12-19.

States has invested the most money at the national level, particularly in the past decade with two major laws—the Intermodal Surface Transportation Efficiency Act of 1991, which authorized $150 billion for 6 years, and the Transportation Equity Act for the 21st Century (TEA-21), which authorized $217 billion through 2003. The latter law included a Coordinated Border Infrastructure Program, which allocated about $140 million for both borders.[16] Canada did not have a national investment strategy for its roads since the construction of the TransCanada highway in the 1950s and 1960s. In 1997, the government determined that it would need Cn$16 billion in improvements just to meet the minimal engineering standards on its national highway system.[17] That figure was clearly out of reach, but in response to the US TEA-21 program, the Canadian Parliament in February 2000 decided to allocate $400 million for strategic highway infrastructure—starting in 2002.[18]

Mexico, of course, has the fewest and worst roads and infrastructure. After more than a decade of austerity programs, and a toll road system that went bankrupt, public investment in infrastructure investment fell from more than 10 percent of GDP in the early 1980s to less than 2 percent in 1998.[19] Mexico's private sector analyzed the country's infrastructure and concluded that it needed 34,000 more miles of highways, the expansion of 18 airports and a new one in Mexico City, and significant investments in telecommunications and energy. The total cost was estimated at about *$250 billion*. They hoped a substantial amount of the funds could be raised by the private sector.[20] This is wishful thinking, particularly because the country does not yet have a functioning banking system. The government, however, succeeded in privatizing both the railroads and the airports, and both are more efficient than ever before. One challenge is to build and maintain the roads to connect all the transportation modes.

The good news is that much of the data have been collected, and considerable research and analysis has been done. The overall objective was defined with clarity and conciseness by Meredith: "To ensure our continued economic growth, there is a need to plan, implement and

16. See Surface Transportation Policy Project, *Changing Direction: Federal Transportation Spending in the 1990s*, Executive Summary, March 2000, 5. Also see http://www.istea.org/guide/guideonline.htm.

17. Cited in Prentice and Ojah, "NAFTA in the Next Ten Years," 7.

18. Department of Foreign Affairs and International Trade of Canada, *Canada-U.S. Partnership: Building a Border for the 21st Century* (Ottawa, 2000), 37.

19. Marcelo Giugale, Olivier Lafourcade, and Vinh H. Nguyen, eds., *Mexico: A Comprehensive Development Agenda for the New Era* (Washington: World Bank, 2001), 2.

20. Isabel Becerril and Jaime Hernandez, "Big Needs: $250 Billion Investments Will Be Required for Infrastructure," *El Financiero International Edition*, 22 March 1999, 3.

finance a safe, seamless, integrated continental transportation system."[21] Although her mandate was only to examine the US-Canadian border, she insisted, quite properly, that Mexico should be an active participant, and that the provinces and private and nongovernmental groups should have a stake in the plan. The three governments should negotiate a *common set of safety standards* and *uniform regulations on weight and dimension*. As the NAFTA subcommittee noted, this is not as easy as it appears, but it is also not as difficult as is claimed. Design engineers in all three countries are well trained; their assessments seem to be based on different judgments as to the risks of damage to the trucks, roads, and particularly the bridges. This judgment is, in turn, related to the age of the roads in their country and the cost of investment. To a certain extent, it is also related to the weather. (In the northern climes of Canada, the spring thaw is a particularly fragile time for roads, and therefore the provinces set lower weight standards for trucks.) The engineering studies have been completed. The specific steps should be as follows:

- First, the three national governments should each develop uniform regulations on weight, safety, and configuration of trucking for each nation (perhaps allowing for a few exceptions in special areas, e.g., the Arctic) and then negotiate uniform standards for North America with the other governments.
- Second, the governments should agree to eliminate "cabotage" restrictions, which usually take the form of customs duties on the vehicle or prohibitions on the employment of nonresident drivers. These restrictions are pure protectionism, designed to discourage truckers from working across the border.
- Third, the governments should plan and finance new highway corridors on the Pacific Coast and into Mexico.
- Fourth, the regulatory agencies of the three governments should negotiate a plan that would permit mergers of the railroads in a manner that would serve the interests of the three countries. High-speed rail corridors should be considered between Canada and the United States.
- Fifth, the three governments should begin collaborating on inspections for immigration and customs. (This essential task will be developed in the next chapter.)

Another barrier that needs to be overcome is money. The cost of investing in infrastructure in Mexico is very high, considerably beyond Mexico's current capacity. The World Bank proposed an "infrastructure fund, per-

21. Meredith, *Trade Corridors*, 7.

haps in partnership with an international investment bank.''[22] This idea will be developed in the next chapter.

Before too long, overland trade within North America will confront a barrier manned by bureaucrats and mined by flawed or inadequate infrastructure. This wall can be dismantled and demined only by a concerted effort of the three leaders. ''If the 1990s were the decade of the free trade agreements,'' writes Meredith, ''then the first decade of the 21st century should be the decade of the transportation agreements.''[23]

Trade Policy—Within and Without

The proposed North American Commission ought to draft two papers on trade issues for the three leaders: an internal agenda and an external strategy. The first agenda would cover the trade issues that were either unresolved by NAFTA or have emerged since the agreement. It should also outline the steps that are needed to move the agreement to the next stage—that of a customs union. The second paper would explore the costs and benefits of the three governments adopting a unified approach to trade negotiations with other countries and the WTO.

The trade and investment barriers that remain in North America are the ones that were most difficult to negotiate. They have not become easier, but they have become more controversial. Among the issues that need to be addressed are uniform (or compatible) standards and labeling for products and processes; health and environmental standards, particularly for agriculture (genetically modified food, additives); harmonization of licensing requirements for professionals; coordination and harmonization of competition policies and other regulatory policies, which have cross-border effects; and coordination of inspections of agricultural goods. In some cases, harmonization is neither practical nor desirable, because of varying living standards and administrative capabilities. Instead, it might be better to seek to eliminate incompatible standards, rules, or labeling. With regard to government procurement, Hart estimates that *only* 25 percent of government contracts in Canada and the United States are subject to real competition, and it is less in Mexico.[24]

Agriculture remains the most difficult area for all three countries because of extensive government involvement and subsidies. In 1996, the US Congress passed a farm bill to remove government subsidies to its farmers. At the same time, the United States put increasing pressure on Europe to eliminate its farm subsidies, which averaged $40-50 billion a

22. Giugale et al., *Mexico*, 405.

23. Meredith, *Trade Corridors*, 13.

24. Hart, ''Role of Dispute Settlement.''

year. Then, the global market was glutted, and as the value of the US dollar increased, US crops were crowded out of many markets. The US government reinserted itself into the rural economies. By 2000, US farm subsidies totaled $28 billion.[25]

Mexico continues to protect its corn and seeks to limit imports from the United States of high-fructose corn syrup; the United States protects its sugar and vegetables; Canada, its dairy products. Canadian companies can harvest softwood lumber at very low prices set by the government, and US timber companies complain that the price represents a subsidy. In 1996, under threat of US suits, the Canadian government ''voluntarily'' restricted its exports. That agreement expired in March 2001, and US companies immediately requested countervailing duties of 78 percent on lumber imported from Canada.

None of the governments has shown much interest in trying to come to grips with the broader issue of how farming should be managed in North America in a manner that is fair to the farmers in all three countries and not too costly to the taxpayer. Moreover, for trade to be fair, Canada will have to deal with its monopolistic marketing boards, and the United States with its extensive subsidies to poor rural areas. Lacking the funds, Mexico cannot compete in the game of subsidies.

The softwood lumber issue will be argued in courts and trade panels by legions of lawyers; the victim could very well be the dispute-settlement mechanism. The alternative is for the two, or preferably three, governments to address the underlying problem—which is the unevenness of regulatory schemes. In the case of lumber, roughly 90 percent of the forests are owned by the provinces that sell the lumber to Canadian companies at very low fees, whereas in the United States, perhaps as much as 90 percent of the forests are owned by large and small private firms, and the price is set in the marketplace. This means that the price of US lumber has been much higher than that of Canadian lumber.[26]

One solution would be to privatize Canadian forests. A second would be for the US government to nationalize the private forests. Acceptance of the other's regulatory and ownership system would solve the problem, but neither is feasible. A third idea would be to allow all private foresters, including foreigners, to bid freely on the timber in the Canadian forests. This might lead to a higher price for Canadian lumber, and if so, it would

25. See Timothy Egan, ''Failing Farms Learn to Profit from Wealth of U.S. Subsidies,'' *New York Times*, 24 December 2000, 1, 16; and Edmund L. Andrews, ''No Agreement on Reducing Europe Farm Subsidies,'' *New York Times*, 27 February 1999, B1, 2.

26. See Patti Bond, ''Canadian Timber Deals to Be Probed,'' *Atlanta Journal-Constitution*, 25 April 2001; Anthony De Palma, ''Lumber Dispute Threatens U.S.-Canada Ties,'' *New York Times*, 28 March 2001; and Jimmy Carter, ''A Flawed Timber Market,'' *New York Times*, 24 March 2001, A27.

solve the problem, at least for a time.[27] Given the expanse of British Columbia's forests, this formula, however, is unlikely to lift the price to US levels, and the only US buyers of timber would be large logging firms. Small farmers would still be hurt. Still, a fourth solution would be to replicate the 1996 voluntary export restraint agreement with two modifications: allow the stumpage fee price in Canadian forests to rise gradually, and permit exports of timber from Canada to increase marginally each year. This would encourage an adjustment by both markets.

A significant element of the timber problem—and, for that matter, many other trade problems—is due to foreign exchange rates. As long as the Canadian dollar sells for about two-thirds (65 cents) of the US dollar, Canadian exports will remain cheap, and a surge is likely to have dangerous effects, evoking threats of countervailing duties or antidumping from the United States. If the currencies were in better alignment, protectionist pressures would diminish. In the next section, on macroeconomic policy coordination, we will explore several ways to address this underlying issue.

The "trade remedies" of countervailing duties and antidumping (CVD/AD) have been the source of many trade-related problems within NAFTA and with the other US trading partners. Indeed, one reason for the fiasco at the 1999 WTO talks in Seattle was the Clinton administration's refusal to consider these issues. Whether or not one agrees that CVD/AD are legitimate subjects for global trade talks, it seems improper not to discuss them with our NAFTA trading partners. The truth is that both Canada and Mexico have also begun to use these remedies, and therefore this might be the best moment to consider negotiating a formula for disarmament.

Beyond the internal trade issues, should the three governments of North America adopt a common approach to negotiating the Free Trade Area of the Americas or with the WTO? It would not be easy to reach agreement on a unified trade policy, and it might take some time. However, once the three governments agree to a common external tariff and a customs union, they would have traveled a good distance toward defining common interests in trade policy as they relate to the rest of the world.

Since NAFTA came into effect, Mexico has negotiated nine free trade agreements and Canada has completed three bilateral agreements and is negotiating others. The United States, for its part, has approved preferential trade regimes for the small Caribbean Basin countries and the weak governments in Sub-Saharan Africa, but Congress has not granted the president authority to negotiate on a fast-track basis, and this has inhibited definitive negotiations with Latin America for the Free Trade Area of the Americas.

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27. I am indebted to Gordon Giffin for this idea. Conversation in Atlanta, 1 June 2001.

This haphazard process is frustrating when it is not completely counterproductive, but the question is whether the three governments would not be better served with a common approach. The disadvantage is the one inherent in any international obligation—that is, it constrains choice. For Canada and Mexico, which are concerned about their increased dependence on the US market, it is understandable that they would want to diversify their trading relations with other important countries. This should not bother Washington. There is a *second issue*—how to deal with countries like Cuba and Libya—in which the three countries have markedly different policies. Assuming that it would be more difficult to reach a meeting of the minds on these issues, these countries or issues could simply be exempted from the rest of the agreement.

The advantage of a unified approach, however, is that it would give North America leverage and credibility. Canada and Mexico both have established their autonomy and effectiveness in international forums, and the United States, of course, as the largest trading power in the world, has its own influence. Together, they assemble the perspectives of the three tiers of the international trading system—the highest level; the mid-level for advanced market economies; and what Jeffrey Garten refers to as the ''big emerging markets.'' To the extent that all three governments can integrate their approaches, they could, in effect, act as a surrogate of the entire international system. And the benefit therefore would accrue not just to them, but to all, because—as the world saw in Seattle—the World Trade Organization with its 142 members may have reached the size at which negotiations prove extremely difficult, if not impossible. If North America can negotiate these problems, their formula might be adopted by the WTO.

Macroeconomic Policy Coordination and the "Amero"

As an increasing amount of trade among the three countries is done with the US dollar, and as other countries in the Americas adopt the dollar or peg their currencies tightly to it,[28] some businesspeople in Canada and Mexico also have begun to propose adopting the dollar. Most political leaders, however, are either opposed or show little interest.

At a discussion of this issue in 1998, Thomas Courchene, a Canadian economist, explained to Paul Martin, his country's finance minister: ''With so much trade going to the United States, we simply cannot tolerate the

28. Panama has used the dollar since 1903; Argentina has pegged its peso to the dollar. Ecuador adopted the dollar in February 2000, El Salvador in January 2001, and Guatemala in May 2001. In the most incongruous case of all, Cuba has more and more used it as their currency.

degree of exchange rate variability we've had over the last decade and a half.'' Martin responded vehemently: ''That is not what NAFTA is all about. NAFTA is a trade agreement. It is one thing to contemplate a united Europe consisting of some 20 odd countries—a number of which are of equal size. It's quite another to contemplate that in terms of North America where you would have one very large dominant country and two much smaller ones.'' John Kirton of the University of Toronto agreed: ''There's no way Canadians would go for it as a matter of symbolism, sovereignty, and a matter of history.'' Courchene insisted on the need to discuss the issue, given the cost of exchange rate variability to the Canadian economy, but he conceded that it might be impractical at the current time, even in the United States: ''Americans love to devolve sovereignty to the markets. But not to anybody else.''[29] This captures the sounds of a debate that has just begun.

The current US position on ''dollarization'' for other countries is neutrality.[30] One could argue that is not a bad approach. If the United States were to promote the dollar vigorously as the single currency, our two neighbors would probably react as negatively as they did when the United States first proposed free trade agreements. As Hart put it: ''The combination of US chauvinism and Canadian paranoia dictates than any initiative must emanate from Canada.''[31] The same argument applies to Mexico. It would be better if the two governments approached the United States first, but it would also increase the prospects for success if the United States were prepared to be flexible in its response. The law requires that US monetary policy should not be diverted from its task of assisting the US economy, but officials could offer to discuss privately its ramifications with counterparts in Canada and Mexico.

Dollarization, of course, is only one way to adopt a common currency. Because it raises sensitivities about sovereignty, one might usefully return to the original question regarding its purpose. Those countries, such as Argentina and Ecuador—which have linked or replaced their currency for the dollar—have done so because they were traumatized by hyperinflation, or feared financial volatility. In that sense, the dollar is intended to serve a role similar to that of the gold standard—as an anchor that

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29. Norma Greenway, ''Is a 'North American Dollar' the Best Option for Canada? Finance Minister Quickly Dismisses Idea of Single Currency for Continent,'' *The Ottawa Citizen*, 8 August 1998.

30. See the testimony by US Assistant Treasury Secretary Edwin M. Truman to the Senate Banking Committee, 8 February 2000. He incorporates remarks made previously by Treasury Secretary Lawrence Summers. Truman said: ''We do not have a view on whether dollarization is advisable in general.''

31. Hart, ''Role of Dispute Settlement,'' 24.

prevents political leaders from overspending, or as protection against being buffeted by gale-force financial winds.[32]

There is a second reason to consider a common currency that more nearly corresponds to Europe's decision to adopt the euro. When countries experience a high rate of integration, and trade liberalization is already advanced, the exchange of currencies can become a serious transaction cost. For Canada and Mexico, which export about a third of their output to the United States, dollarization, according to Bergsten, ought to be considered seriously to minimize the costs of trade.[33] Although neither Mexico nor Canada has experienced hyperinflation, both have suffered from foreign exchange costs and crises. The peso crisis of December 1994 shrank Mexico's economy so much that even after 4 consecutive years of 5 percent annual growth, it still had not fully recovered. And Canada has witnessed a continuous, generation-long depreciation of its currency against the US dollar. The question posed by Gibson, a Canadian commentator, is whether there is ''a way of ending the pattern of significant long-term decline that has been the fate of the Canadian dollar over the past generation with the subsequent international erosion of Canadian wealth.''[34]

At a theoretical level, the benefits and costs of dollarization are relatively clear-cut. Advocates judge that the principal benefit for the country adopting the dollar would be financial stability. But foreign investment would also probably increase; the cost of borrowing would decline as access to the dollar market widened; the cost of doing business and trade would decline as firms used a single currency and did not need to hedge against other currencies; fiscal discipline would be steadier; and, to the extent that inflation were reduced, the lives of the poor would improve.

Opponents of dollarization argue that governments would lose sovereignty, seigniorage (the profits from printing money), and a ''shock absorber'' in times of crisis (in the event of a decline in the prices of commodity exports, a rise in interest rates, or the disappearance of investor confidence). A government might keep its prices stable, but it would deny itself a tool to combat recessions and unemployment. Indeed, a major concern of dollarization is that a government would transfer its power to respond to its own business cycles to the United States, whose Federal Reserve is mandated by law to set interest rates only in response to US

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32. The costs of being tied down may be very high, as Argentina discovered in 1999-2001.

33. C. Fred Bergsten, ''Dollarization in Emerging-Market Economies and Its Policy Implications for the United States,'' testimony before the US Senate Finance Committee, 22 April 1999.

34. Gordon Gibson, foreword to *The Case for the Amero: The Economics and Politics of a North American Monetary Union*, by Herbert Grubel, Critical Issues (Vancouver: Simon Fraser Institute, 1999), 2. See also ''Cheap Dollar Is Making Canada the Land of the Spree,'' *New York Times*, 1 August 1999, 11; and James Brooke, ''Is the Dollar Leaving Canada Feeling Drained?'' *New York Times*, 13 November 1999, B1.

economic cycles.[35] Of course, Congress could expand the mandate of the Federal Reserve to take into account the economic cycles of its two North American neighbors, and it could establish two new Federal Reserve districts in Mexico City and Toronto.[36]

An alternative would be to establish a new currency. That, of course, is the point of the euro, and that is the essence of a proposal developed by Grubel in a paper for the Simon Fraser Institute in Vancouver. He makes the case for a North American Monetary Union with a central bank and a common currency, which he dubs the ''amero.''[37] The board of governors would be chosen by the three governments in proportion to their country's population and income. The mandate of the Central Bank of North America would be similar to that of the European Central Bank—to maintain price stability rather than full employment—but it would respond to the economy of the continent rather than just of one nation. The amero would be equivalent to the US dollar, and the Canadian and Mexican currencies would be exchanged at the rate that they are then traded for the US dollar. In other words, at the outset, prices, incomes, and wealth in all three countries would be unchanged, and the power to manage the common currency and earn profits from printing it (seigniorage) would be roughly proportional to the existing wealth of the three countries. The United States would share some of its decision making, and its goals would be continental rather than just national prosperity, but it would remain as economically dominant as today.

Grubel's main arguments are directed at a Canadian audience. He believes that flexible exchange rates ''have contributed to poor economic performance,'' price instability, and lower incomes in Canada. A common currency, in his view, could lower long-term interest rates, expand trade, and enhance productivity in Canada without compromising cultural sovereignty and political independence. He acknowledges that the United States ''has less to gain'' from the union than do Canada and Mexico, except that it would benefit considerably ''from having more stable and

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35. For a full discussion of these issues, see Andrew Berg and Eduardo Borensztein, *The Pros and Cons of Full Dollarization*, IMF Working Paper WP/00/50 (Washington: International Monetary Fund, 2000); Ricardo Hausmann, ''Should There Be Five Currencies or One Hundred and Five?'' and Jeffrey Sachs and Felipe Larrain, ''Why Dollarization Is More Straitjacket than Salvation,'' *Foreign Policy* (Fall 1999); Federal Reserve Bank of Atlanta, ''Responding to Global Crises: Dollarization in Latin America,'' *EconSouth* 1, no. 2 (1999); and Robert Mundell, ''Threat to Prosperity,'' *Wall Street Journal*, 30 March 2000, A30. Mundell, a Nobel Prize winner for his concept of the ''optimal currency,'' writes: ''The biggest danger to world prosperity arises from wide swings, not based in any economic fundamentals, in the exchange rates of these three [dollar, euro, yen] currencies.'' He argues for a single world currency and central bank, but in the interim, combining the currencies and managing them better.

36. I am indebted to Fred Bergsten for this idea.

37. Grubel, *Case for the Amero*.

prosperous countries as neighbors.'' This is a significant proposal, but also one that will take substantial time for the elites and the public to digest and consider seriously.

Grubel's argument has resonated in Mexico, where his paper was adapted, translated, and published as a book,[38] but it will be very hard for Americans to give up the dollar even for an instrument that is its equivalent in everything but name. The strongest argument in favor of the idea is that it is ''fair'' in the US sense of that term; that is, it does not alter the relative power equation in North America, but it provides space for our neighbors to participate in decision making. That is the essence of the idea that Woodrow Wilson and Franklin D. Roosevelt captured in the international organizations that they designed.[39] That is why, in the long term, one would be mistaken to dismiss this idea, even while recognizing that it stands little chance of acceptance any time soon. In the long term, the amero is in the best interests of all three countries.

There are other options. The most likely course is inaction. As trade expands, businesses in Canada and Mexico are more and more using dollars. Foreign currency deposits—almost all US dollars—in Canadian banks have ballooned from 27 percent of total deposits in 1995 to 52 percent in 1998. In other words, Canadian banks hold more US dollars than Canadian dollars on deposit.[40] Similarly, a poll in May 1999 asked Mexicans whether they wanted to have US dollar accounts in their country, and 86 percent responded positively, although they were more ambivalent about replacing the peso with the dollar.[41] Over time, it is possible that so many Canadians and Mexicans will use dollars that ''de facto dollarization'' might save their political leaders from having to make a difficult decision.

In the short term, however, complacency with the status quo is unwise; there have been too many abrupt crises in Mexico and too much creeping deterioration in Canada. At the minimum, the three central banks should share more information and expand their swap arrangements to help each other in the event of a crisis. The United States has had a swap

38. Herbert G. Grubel, *El Amero: Uno Moneda Comun para America del Norte*, adaptacion para Mexico y actualizacion por Manuel Suarez Mier (Mexico: CIDAC y Cal y arena, 2001).

39. For an elaboration of this thesis, see Robert A. Pastor, ed., *A Century's Journey: How The Great Powers Shape the World* (New York: Basic Books, 1999), especially chapter 6 on US foreign policy.

40. Eric Beauchesne, ''Greenback Is Shoving Loonie Aside,'' *The Ottawa Citizen*, 13 July 1999. See http://www.ottawacitizen.com/national/990629/2548950.html. This percentage may be high. The Bank of Nova Scotia and the Canadian Imperial Bank of Commerce, two of Canada's six largest banks, reported that 37 percent and 41 percent, respectively, of their deposits were in dollars in 2000. (I am indebted to Michael Chriszt of the Federal Reserve Bank of Atlanta for this information, 14 June 2001).

41. Julia Preston, ''Mexico Measures Identity in Dollars,'' *New York Times*, 16 May 1999, 16.

arrangement with Mexico since 1941, in which the US Treasury through the Exchange Stabilization Fund (ESF) provided injections of dollars at critical moments to stabilize the Mexican peso. There is little evidence that this exercise succeeded, in part because the amounts were quite small.[42]

In April 1994, Canada, Mexico, and the United States negotiated a little-noticed North American Framework Agreement (NAFA), which included low-level consultations and a swap arrangement involving the US Treasury and Federal Reserve, the Bank of Canada, and the Central Bank of Mexico. The agreement had to be renewed annually, and the amount was paltry. NAFA only contained $6.8 billion—$3 billion from the Fed, $3 billion from Treasury's ESF, and $800 million from Canada. When the peso crisis struck, NAFA was much too small to have any impact. In the end, the United States had to assemble a $55 billion rescue package, of which $20 billion came from the ESF. NAFA was extended for 1 year, the Canadian contribution was increased to $2 billion, and the Bank of Mexico agreed to set aside $3 billion for it. That nearly doubled the fund to $11 billion, but that amount was still trivial as compared with the magnitude of the capital flows in and out of Mexico each year.

It is true that as long as Canada and Mexico have flexible exchange rates, the buffer fund does not need to be that large. But the intensity of integration among the three countries is such that the size of the fund is as important for psychological as for economic reasons. There was some recognition of that fact when the Mexican government negotiated a standby arrangement with the IMF in advance of the 2 July 2000 elections for $16.9 billion—just to help it through the transition.[43]

Whether the governments discuss the amero or dollarization or beefing up the swap arrangement, they should explore ways to mitigate the financial volatility that endangers all three economies. That may mean high-level and routine consultations and, to the extent possible, coordination of their macroeconomic policies. Eventually, the governments should adopt disciplines that could reduce the divergence in inflation, interest rates, and fiscal balances. Absent such steps, movement toward a unified

42. See Anna G. Schwartz, *From Obscurity to Notoriety: A Biography of the Exchange Stabilization Fund*, NBER Working Paper 5699 (Cambridge, MA: National Bureau for Economic Research, 1996). The ESF was established in 1934 to bring stability to the currency markets. Schwartz discovered that Mexico had the longest record of ESF agreements, but she doubts that these or the ones with other governments have succeeded in stabilizing the markets: "The message of the loan packages seems to be that mismanaged countries have a friend at the ESF, which will arrange a rescue" (21). The Federal Reserve also had an arrangement with Mexico since 1967. I am indebted to Ted Truman for his comments on this section.

43. Secretario de Hacienda de Mexico, "Mexico Sends a Letter of Intent to the IMF," 15 June 1999, http://www.shcp.gob.mx/english/iro/. The letter also includes a reference to NAFA. For the agreement's extension, see http://www.federalreserve.gov/fomc/minutes/20000516.htm.

currency might actually exacerbate the financial differences. At the outset, such consultations might involve periodic meetings of senior budget and financial officials of all three governments. In a North America defined by a genuine partnership, a joint statement by these senior officials could have a positive effect on a government whose policies were veering off course toward a bloated fiscal deficit or an appreciating currency.