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NAFTA: Overview of Legal, Economic, and Practical Issues

I. INTRODUCTION

FREDERICK HILL:

This panel focuses on the practical business aspects of NAFTA. As you heard from Elsa Saxod, NAFTA can be broken down into six areas: (1) market access; (2) trade regulation; (3) foreign investment laws; (4) intellectual property laws; (5) service business; and (6) dispute settlement. NAFTA provides a platform and a basis upon which Canada, Mexico, and the United States can join for their mutual benefit. However, since each country is sovereign, we must recognize that the free trade agreement is not a panacea, as each of the three contracting parties must enact implementing legislation to give the agreement effect.

Since each country enacts its own implementing legislation, a panel of experts must be established to resolve conflicts. This panel should also address questions of whether or not there has been a fair interpretation of the law in the particular country involved. An expert panel enables each country to remain sovereign and pursue its own interests while enjoying the basis and a forum upon which to start working with the other nations for their mutual interests.

One issue of particular importance to all three countries is the global environment. We need to work together to protect the environment and to avoid the difficulties that are concomitant with factories and businesses that provide jobs but harm the environment. Mexico has adopted environmental rules parallel to those of the United States. However, it is one thing to have rules, it is another thing to enforce them. Without the resources to enforce these rules, they will not be enforced.

Second, it is important to recognize that here in the United States, as well as in Mexico and Canada, we need to be more competitive. It is a widely accepted principle that the way you protect jobs is to become more competitive. One way to generate greater employment in your country is to focus on exports and exploit the opportunities in the markets. For example, Japan focused on exports successfully. Similarly, the United States, Canada, and Mexico must focus on exports and work together, taking mutual advantage of the opportunity to compete more aggressively.

As President Salinas de Gortari has recognized, Mexico is in a depressed financial state and is thus acutely interested in adapting Mexican policies to its own advantage. The United States and Canada share this same interest. It is in the interest of each of these three countries to change their policies to take the concerns of the global environment and business into account. Interest groups wanting to protect jobs by attempting to delay and defeat the trade negotiations are only providing a short term gain and a long term loss. We, in North America, can learn something from the Japanese in terms of long range planning. We need to focus on the long term, rather than the short term.

II. UNITED STATES MOTIVATION TO ENTER INTO NAFTA

SALVATORE OSIO:*

NAFTA is nothing more and nothing less than a trade agreement. It is not the creation of a common market, and NAFTA has no real resemblance to the European Community. NAFTA is often confused as creating a North American Economic Community. This mistaken perception includes an economically integrated community with free movement of labor, such as workers. The opposite is true. What has politically motivated the United States is the desire to help Mexico create jobs within its borders. If this goal can be accomplished, it is anticipated that it will stem the flow of undocumented illegal aliens seeking employment in this country. However, NAFTA does not deal with immigration. Each country retains its own immigration laws. Present immigration law and amnesty provisions attempting to stop this illegal immigration have failed. The only practical solution is to assist Mexico, and eventually the rest of Latin America, in creating job opportunities so that citizens have an opportunity to find employment without the necessity of leaving their country. The second motivation, both political and economic in nature, is to protect the United States' self-interest against the formation of trading blocks beyond our sphere. Two such trading blocks are the so-called Yen Block and the European Community.

From the United States' standpoint, NAFTA is a self-protection

* B.A., University of Southern California; J.D., University of Southern California School of Law, 1962. Salvatore Osio is a member of the California State Bar Association specializing in international law and finance. As the Managing Partner of North American Ventures, Mr. Osio negotiates joint ventures and arranges the financing for United States-Mexico enterprises. He was one of the organizers for this Symposium.

mechanism. The United States has already reduced its tariffs, quotas, and barriers to trade. About one-half of all products from Mexico come into the United States without any tariff whatsoever. The balance and weighted average of the tariff imposition on Mexican products to this country is about three and one-half percent.

Presently, the United States and Mexico have many petty rules and regulations that impede the free flow of goods. By way of example, the United States restricts the entry of avocados through its borders due to health regulations. This restriction is in force even though the avocados are for export to Japan. This is simply a way of preventing Mexico from using United States port facilities to export to Japan in order to enhance and protect its own avocado industry. NAFTA will eliminate this type of petty restriction. However, the trade agreement is practically in full force and effect, since Mexico adopted and entered into GATT in 1986. Under President Miguel de La Madrid and his successor, President Salinas de Gortari, Mexico has moved from an import substitution economy to a free market economy. A revolutionary fast-track approach has in fact brought Mexico into the free trade community. Mexico has adopted a new foreign investment law, it has relaxed its import restrictions, and it has already adopted an intellectual property law. The free trade agreement that is being negotiated bilaterally with Canada is a formalization of already existing practices. This agreement will provide a smooth process by which the three countries can deal with one another. NAFTA will establish a precedent for future integration of a North American Economic Community.

III. MEXICO'S MOTIVATION TO ENTER INTO NAFTA

JORGE CAMIL:*

This discussion will focus on the Mexican viewpoint of the NAFTA. A related concept that will be explored is whether the government is abdicating the stewardship of the economy. An observer of the recent Mexican political and economic scene would conclude that the Mexican government still advocates the strong Presidential system in place since the 1910 Mexican Revolution. From that day forward Mexico has seen strong governmental intervention in all aspects of domestic and foreign investment. This economically stifling

* J.D., University of Houston, 1971. Mr. Camil is a partner at Camil Abogados, Mexico City. He specializes in financing and banking law, with an emphasis in international transactions. He was one of the organizers for this Symposium.

encroachment has only increased over the years. Yet, today we witness the movement toward trade liberalization in Mexico's joining GATT. President Salinas has instituted a massive privatization effort, consisting of the sales of hundreds of inefficient government-owned companies ranging from huge telephone companies to copper mines. Then, there is the momentous reversal of the bank nationalization of 1982. As a consequence of this reversal, the government has committed to auction off, within the course of one year, each of Mexico's eighteen commercial banks.

Another example of the shift toward trade liberalization is the passage of the foreign investment regulations in 1989. For the first time in fifteen years, foreign investors will be able to have controlling equity positions in Mexican corporations. The government is also prosecuting overly powerful union leaders who, for many years, were the very lifeline of the political system. Moreover, the government has also pressed for passage of new financial legislation and amendments to the existing legislation which would allow for foreign equity participation in banking, bonding companies, factoring houses, and leasing corporations. The government has also sought deregulation, not only in foreign investment, but in transfer of technology, truck manufacturing, petrochemicals, and telecommunications.

Perhaps these types of provisions are commonplace in a free market economy such as the United States. However, these provisions mark a surprising shift from tradition for Mexico. Mexico has moved from one of the most closed economies in the world to one of the most open, in the course of the last five years. The economic model instituted by the government after World War II was responsible for Mexico's enormous rates of growth of six to eight percent per annum. This old economic model was called *Desarrollo Estabilizador* or "developing with price and monetary stability" and was predicated upon import substitution. This policy of import substitution consisted of the government closing the borders to the importation of a product whenever a domestic company could prove that it was manufacturing the particular good, no matter how costly or inefficiently. The favorable consequence of this economic policy was that Mexico was able to establish a solid industrial base. This was an accomplishment because after World War II, it would have been easier for Mexico to import all of its goods and services from the United States instead of producing its own. Thus, the creation of a Mexican industrial base

was a salutary product of the Government's policy of import substitution.

Unfortunately, this policy produced negative results. Mexico's policy of import substitution forced the Government to subsidize the Mexican peso. The economic impact of this action is best understood by a statement made by an economist: "the cheapest commodity in Mexico was the Mexican peso." For almost a quarter of a century, the Mexican government was committed, through the central bank, to buy and sell unlimited amounts of dollars and pesos at the rate of 12.50 pesos to the dollar. Instead of furthering industrial promotion, this arbitrarily set exchange rate created a massive capital flight which was one of the causes of the fiscal crisis that erupted in 1982.

Import substitution also resulted in social neglect. The government, in expending its limited resources on subsidizing inefficient and costly industry, was unable to provide necessary services such as welfare, health, and education. Eventually, the government attempted to correct this inequity by instituting a new policy of income distribution, which was known as *Desarrollo Compartido*. The policy of development with income distribution, in place from 1970 until 1972, created a welfare state with the government subsidizing goods and services. The government's acquisition of corporations that were bankrupt or about to declare bankruptcy led to massive government growth with the government involved in all aspects of commercial and manufacturing enterprises. Mexico financed the incredible deficit resulting from such a policy primarily through external debt. Mexico went from \$4 billion in external debt in 1970 to \$20 billion in the course of six years, and then to \$100 billion in the course of the next six years.

A careful observer of Mexico may, considering the tendency of the Mexican economy to shift from the right to the left following the volatile political pendulum, validly question whether the current Mexican government's endorsement of NAFTA is only temporary. The answer to this question is the Mexican Government's commitment to free trade. In contemplation of NAFTA, Mexico is making a serious commitment to the international community. The signing of NAFTA will be a treaty under Mexican law and Mexico has an impeccable record of fulfilling its international obligations. Such treaty arrangements are not matters that a new administration can disown or dishonor. Mexico has committed to modernization not only for the benefits of NAFTA, but because there are no other options. Mex-

ico must either modernize or it will experience a serious economic, political, and social crisis. Modernization, President Salinas said, has ceased to be an economic option. It is an imperative.

FREDERICK HILL:

If NAFTA is indeed entered into, it will be a bilateral agreement between two countries, and it would seem that it would be valuable to foreign investors who go to Mexico because it would be something they could rely upon. It would significantly decrease the chance of a new administration coming in when President Salinas finishes his term and adopting different foreign investment regulations. Is that something that can give foreign investors comfort?

JORGE CAMIL:

Foreign investment regulation is a very important issue because investors considering making large investments in Mexico may be justifiably concerned about the ease with which the 1989 regulations could be changed. The current regulations are the equivalent of an Executive Order in the United States that could be changed tomorrow by another Executive Order. Foreign investors would like to see a change in the foreign investment law itself that would allow controlling foreign investment. The reason that the law was not changed is that President Salinas, in the first part of his administration, did not have a sufficient majority to change the foreign investment law. In addition, foreign investment has become a touchy political issue, and in order to amend such a law it is necessary to have not only the majority in Congress but also an educating process which implies lobbying with the various political parties. But there is no question that an amendment of the law has been discussed by officials in the Salinas administration, and by the President himself. In fact, he has insinuated that this is a priority in the administration, that change could happen any time now, because the President now has a much more comfortable majority in Congress.

IV. CANADA'S FREE TRADE AGREEMENT WITH THE UNITED STATES AS IT RELATES TO NAFTA

FREDERICK HILL:

We are fortunate to have on our panel Henri Alvarez from Vancouver, Canada, who will provide insight on developments since 1988, when the United States-Canada Free Trade Agreement was signed and on Canada's expectations regarding NAFTA.

HENRI ALVAREZ:*

This section will discuss Canada's perspective on the Free Trade Agreement between it and the United States. The focus of this section will be on the dispute resolution mechanisms which Canada has always considered a very critical part of the Free Trade Agreement. Canadians generally have a cautious reaction to the Free Trade Agreement. Canada, like Mexico, is one of the two mice next to the United States elephant and they have to tread carefully in most of their dealings with the United States. The Free Trade Agreement was negotiated in the context of the largest bilateral trade between any two countries. In 1986, bilateral trade between the United States and Canada amounted to over \$170 billion, and has increased substantially since then. The agreement is a long and complex document. It is difficult to describe, and it is still too early to determine, from an economic or financial standpoint, the impact of the agreement. Many of the provisions under the agreement are intended to be incorporated over time. The best example of this is the elimination of tariffs, which are to be phased out progressively between now and January 1, 1998.

The objectives of the Free Trade Agreement between the United States and Canada are stated in the preamble. They are: (1) the elimination of barriers to trade in goods and services; (2) the facilitation of conditions for fair competition; (3) the liberalization of conditions for investment; (4) the foundation for future cooperation; and (5) the establishment of a procedure for joint administration of the agreement and the resolution of disputes. Within these goals, Canada's particular interest was to overcome what it perceived to be growing United States protectionism which would jeopardize Canadian access to the United States market.

Canada has traditionally relied heavily on exports to the United States. More recently, Canada saw the United States applying its laws in an increasingly arbitrary fashion in response to the growing strength of special interest groups within the United States. The best example of this was the experience with soft wood lumber which continues to be a hot topic of discussion between the two countries. The United States, on the other hand, took the general approach that it wanted greater control over what it perceived to be Canadian subsidi-

* L.L.B., University of Ottawa, 1980; Ph.D., Institut Universitaire de Hautes Etudes International, Geneva, Switzerland, 1984. Mr. Alvarez is a partner at the firm of Russell & DuMoulin, in Vancouver, B.C. He specializes in employment and labor law, and commercial arbitration. He also serves as an adjunct professor at the University of British Columbia.

zation of goods. Under the present Free Trade Agreement, and I suggest under the NAFTA discussions, one of the main topics of discussion will be subsidies and subsidization. Canadians maintain that the United States engages in subsidization, while the United States refuses to admit such a policy. Another item of critical interest to Canada in the negotiations is to create a binding dispute resolution mechanism, both generally with regard to implementing enforcement of the agreement and, more specifically, with regard to the question of countervailing and dumping duties imposed by both countries.

What in fact did the Free Trade Agreement provide for? First, it addresses national treatment with regard to investment and trade in goods and services in both countries. The agreement adopts and builds upon the GATT rules to which both countries already subscribe. The foundation for the implementation of, and many of the rules at the basis of, the agreement are the GATT rules. Moreover, the two bi-national panels dealing with major questions of general application of the treaty have looked specifically at the interpretation of GATT itself. The goal of eliminating all tariffs by January 1, 1998, as mentioned previously, includes a very lengthy and complicated section on the questions of Rules of Origin. They deal with the facilitation of trade with regard to customs administration and the elimination of quantity restrictions. Agreement on technical standards will not be used as unnecessary obstacles to trade. Additionally, the elimination of agricultural subsidies typifies many of the areas of the agreement where the parties agree to work together to achieve the elimination of subsidies, and specific reference is made to ongoing GATT negotiations, including the Uruguay Round. Well, you will immediately identify that there is a problem here, because if we are to wait for the Uruguay Round to provide a resolution, it may take some time.

The Free Trade Agreement also establishes a working group to draft a new set of rules regarding subsidies and countervailing and dumping duties. This area was a major bone of contention during the negotiations, and in fact the negotiations nearly broke off completely on the question of the definition of subsidies and rules governing subsidies and duties. In the end, under Chapter 19, a working group is to draft a new set of rules within seven years of the January 1, 1989 implementation. Failing that, either party is free to give six months notice and bring the Free Trade Agreement to an end. This will likely be a major point of negotiation in the NAFTA agreement, because it

continues to be important to the United States and Canada in the context of the Free Trade Agreement.

The agreement also provides for increased access to government procurement in each country, deals with investment, and calls for national treatment on the establishment of new businesses. In addition, it addresses certain "grandfathering" of rules on investment in existing businesses with a certain liberalization with regard to those businesses.

Chapters 18 and 19 deal with dispute resolution. Chapter 18 deals with general disputes and alleged breaches of the agreement. Chapter 19 deals specifically with countervailing and anti-dumping duties. The dispute resolution mechanism is something quite new and is perhaps one of the most useful aspects of the agreement. It provides for notification by the parties of changes in their legislation or measures they will take that are likely to affect the terms of the agreement in any substantial way. It also requires negotiations and consultation under the terms of the agreement. There is also the establishment of the United States-Canada Free Trade Commission, which will deal with disputes arising under the Free Trade Agreement. This bi-national review panel will deal with dumping and countervailing duties, but also will deal with review of legislative amendments in both Canada and the United States.

The Free Trade Agreement between the United States and Canada, as it currently stands, provides for a panel composed of five members, two from each country with a fifth member selected by those panel members. The panel will review legislation, or changes in legislation, to see whether it would substantially affect obligations of either state under the agreement. If there is an affirmative finding of a substantial effect, the panel can recommend changes to the legislation. Failure to implement the recommended changes will give the right to either party to terminate the agreement on sixty day notice.

What is the Canadian perception of how Canada benefits from the Free Trade Agreement with the United States? It is too early to say, particularly financially. At this time, many areas in Canada are suffering through difficult economic circumstances. Although certain groups in Canada, such as labor groups, have a tendency to identify the economic difficulties with the Free Trade Agreement, it is difficult to say conclusively what the impact of the Free Trade Agreement, if any, is in that regard.

There is no doubt that the Free Trade Agreement will have a

fairly substantial effect on the Canadian economy. It is going to require reorganization because the Free Trade Agreement appears to give a comparative advantage to the United States in many areas. But there continues to be quite a debate in Canada as to the benefits to Canada through the Free Trade Agreement. Currently, many businesses are relocating to the United States to take advantage precisely of the liberalization of trade. The question is, will the short term pain that some sectors of the Canadian economy are suffering be outweighed by the long term advantages? I am confident that they will, but I think Mexico should also bear in mind that any Free Trade Agreement with the United States will require certain reorganization, and there will naturally be a shifting in the economy for both the United States and Mexico.

It is clear that there are new opportunities afforded to Canada as a result of the Free Trade Agreement. And it may well be that any perceived disadvantages would have occurred in any event. It is really a question of time and which segments of society will be able to further their own interests and for how long.

One area of concern is the question of anti-dumping and countervailing duties. The problem that emerged was a lack of agreement on new rules in this area. The understanding was that the national laws of each country, as they stood at the time of implementation of the agreement, would continue to apply. The only difference was that instead of challenging the decisions by, for example, the Canadian International Trade Tribunal, you would go to a five member panel of Canadians and Americans for review to insure that either United States or Canadian law was properly applied. To date there have been approximately fifteen panels constituted, with mixed success. Fourteen of them were at the request of Canadian parties and one was at the request of a United States party. Some critics point to the fact that a partisan approach to resolving the dispute may exist, depending upon whether there are three Canadians or three Americans on the panel. In general, though, it has worked fairly well. There have only been six determinations that have actually gone through to final decisions by panels, and those have all been accepted or implemented. One recent decision is quite controversial in the United States. It deals with chilled pork from Canada, and has caused quite a furor in the United States to the point that the United States asked for an extraordinary challenge to a panel decision. The challenge was denied and Canada is quite pleased about that. On the other hand, there

have also been losses, but despite this, it is encouraging that both countries are making mutual attempts to resolve the disputes. Neither party demanded resolution through a neutral third party for determination. The panels consist of United States and Canadian citizens. There are also time limits built into the agreement which expedite the process and negotiation of those disputes.

On the larger issue, there have been two panels constituted to consider general alleged breaches of the Free Trade Agreement. The first case dealt with Canadian regulations on salmon and herring. Originally, Canada had regulations which prohibited the export of any salmon or herring in an unprocessed state. This did not sit well with the United States' fish processing industry. The regulation was challenged before GATT and a GATT panel found in the United States' favor. Canada then changed its regulations based on what it perceived to be environmental considerations and management of the natural resource. The new regulation stated that two species of salmon and herring had to be landed in Canada prior to export. The purpose of the landing requirement was to aid in taking statistics to control use of the stocks. This amendment was challenged before a bi-national panel under Chapter 18 of the Free Trade Agreement. The panel, chaired by a Canadian law professor and made up of three Canadians and two Americans, held in favor of the United States' position that this landing requirement constituted a restriction on trade. The matter was sent back to the Canadian government for consideration. Subsequently, an agreement was reached between the United States and Canada on a certain percentage of fish that could be landed. Interestingly, although Canada, under international law, has the right to set whatever restrictions it wants on fishing within its exclusive economic zone, the Free Trade Agreement took precedence over that right. That will probably be something of concern to all countries in negotiating NAFTA. There has also been one other decision under Chapter 18 dealing with the importation of lobsters from Canada, which the United States claimed were under minimum size requirements.

V. RULES OF ORIGIN

SALVATORE OSIO:

One of the sore points in the negotiations that has surfaced is the Rules of Origin. The United States' concern in this area is that either Canada or Mexico will be used by trade competitors, specifically Ja-

pan, as a platform to enter the United States. The United States and Canada have a 50% origin of product content requirement. In order for a product to be classified as North American and enter into the United States with duty-free status, at least half of it must originate in North America. Recently, Honda Corporation was caught with its hand in the cookie jar and was fined approximately \$16.5 million. Honda exported cars from Canada to the United States as if they were Canadian-made, meaning over 50% of the products were Canadian. United States investigations revealed that, through a myriad of Canadian subsidiaries, the products were more than 50% Japanese. So disguised, they entered into the United States market place. The United States is insisting with Mexico that under the North American Free Trade Agreement, 85% be Mexican products before they enter the United States. Of course, Canada would like there to be no restrictions in order to allow more investment into Canada. What is the general attitude of the Canadians toward this Honda issue?

HENRI ALVAREZ:

I would suggest that for both Canada and Mexico, the Rules of Origin would be favorable to those countries if they were as relaxed as possible. Both Canada and Mexico are looking for foreign investment, and we see every advantage in having other countries set up factories in Canada to assemble parts manufactured elsewhere. Particularly for Canada, it is an essential source of foreign investment.

SALVATORE OSIO:

The rules of origin have turned out to be the hottest topic in the negotiations, and it is obvious that Canada and Mexico benefit if the Rules of Origin are relaxed. Dr. Jaime Serra Puche, the Secretary of Commerce of Mexico, is now favoring the so called "classification" test as opposed to a "products test." For example, if Mexico would import grapes from Chile, with whom it has a Free Trade Agreement, and then processes the grapes and converts them into wine and exports the wine to the United States, under the Rules of Origin products test, these are the same grapes in a liquid form, although fermented, coming into the United States. Therefore, they are still Chilean grapes. Now then, the grapes have been transformed into wine. However, from Mexico's standpoint it would be more beneficial to adopt a "classification" test rather than a "products" test. Through the assembly and other labor-intensive processes, goods are

transformed or finished into a different product which would be "classified" as made in Mexico.

Well, the automotive agreement and the Rules of Origin are two very complex areas of negotiation. For example, to the delight of lawyers, there are pages and pages on the Rules of Origin. The Rules of Origin interpretation will be very lucrative for lawyers. With regard to the auto pact, there has been, to a certain extent, a "grandfathering" of it. In Canada, it is a sacred cow. But there has also been some weakening of the auto pact which has always provided for a requirement for manufacturing in Canada of certain auto parts and free exchange back into the United States. There has been liberalization of that requirement, and we are seeing certain parts manufacturing plants in Canada closing and relocating to the United States. Although the auto pact is being maintained in principle, in practice, we see a certain erosion.

JORGE CAMIL:

I think that the auto industry will be a very interesting area to watch in the negotiations and the early stages of the implementation of NAFTA. For instance, last year the Government of Mexico largely deregulated and liberalized the truck market and the auto industry, which is the most important industry in Mexico after oil, and accounts for the largest amount of exports in the country. As a consequence of extreme pressures from the big three, Ford, General Motors, and Chrysler, threatening to leave Mexico if there was a complete liberalization and deregulation of the auto industry, the government backed down and came out not with one automotive decree, which has been the case with every political administration in Mexico since 1964, but with two decrees: one decree regulating the auto industry which is still subject to a lot of protectionism, and one decree regulating the truck industry, which is practically deregulated. Starting next year, it will be possible for anybody to import trucks into Mexico or to manufacture trucks or to establish new manufacturing plants. It did not take the government more than five seconds to realize that the truck industry could be deregulated very easily, because it consisted of five truck manufacturers which are all Mexican corporations fully controlled by Mexican investors. With the auto industry, it is also five companies, the big three plus Nissan and Volkswagen, but they are 100% owned by foreign investors. In order to not aggravate the foreign investors, they deregulated the truck industry while leaving the auto industry subject to a large amount of protectionism. One

of the problems for NAFTA will be to determine where the auto companies decide is the most appropriate country to produce a particular model. They may produce a deluxe car in Mexico and they may produce the more economic cars in Canada. How this will affect Canada and Mexico as very active participants, particularly in the area of auto parts, which is where Mexico is the large exporter, is something we should watch very carefully.

VI. CANADA AND NAFTA

HENRI ALVAREZ:

I would just like to close on the view Canada has in conducting NAFTA negotiations now. Canada is apprehensive, seeing that there are many natural advantages in Mexico which may impact on the Canadian economy. On the other hand, the business community has identified many good opportunities for trade and investment with Mexico. I think Canada feels a bit forced. Canada is at the negotiating table, first and foremost, because they do not want the United States and Mexico to negotiate a deal without it. Canada wants to be included and is anxious to protect what it perceives are gains in the Free Trade Agreement with the United States. And there will be some interesting issues because Canada was able to exempt the application of the Free Trade Agreement, for example, to its cultural industry. Mexico was anxious to exempt certain parts of the petroleum industry from NAFTA. I think Canada viewed it as essential to be at the table to protect its interests, because otherwise much of what was achieved in the Free Trade Agreement could be undone by way of a United States-Mexico deal. But speaking in a positive vein, I think there is a considerable interest in NAFTA for Canada, despite a very vocal opposition from our labor sector.

JORGE CAMIL:

Although there will be a panel on foreign investment, it is important to comment right now. Some of the companies that have benefited from Mexico's old economic model of import substitution and industrial integration have been the foreign companies that have been operating in Mexico prior to the passage of the foreign investment law in 1973. Some of the strongest advocates today against Mexico's liberalization of foreign investment regulation are the foreign companies, the big multinationals that have been operating in Mexico and have a captive market. Think about what I just said about the auto industry.

Closing the border, therefore, excluded the articles produced by their own competitors in their home countries. This has been a wonderful situation. It is no secret that foreign investment has really thrived in Mexico despite the closed economy. Now some of these corporations, subsidiaries of European or United States companies, are the strongest advocates against change because they see that they themselves will have to be as competitive, as efficient, as highly industrialized and technically prepared as they are in their own home countries.

FREDERICK HILL:

I think that is a very good point that illustrates what I said earlier. We have special interest groups, and, in this case, it is the United States automobile manufacturing firms that are in Mexico. We need to raise the level of awareness and we need to recognize that, while we have these special interest groups that will make their needs known, in order to protect all three economies we are going to have to realize that the special interest groups should not dictate, and that the leaders that we have in Mexico, the United States, and Canada are really looking for the best interest of the economy as a whole. We need to encourage everyone to support this kind of development, because if we do not, the special interest groups may prevail. They will prevail for their profit in the short term, but I can assure you that, in the long term, they will not be competitive globally. And if they are not competitive globally, they will not survive in business. As you can see from what we have said so far, Rules of Origin and subsidies are two very hot items. President Salinas responded to a question by saying, "We are not in favor of subsidies. We do not intend to continue giving subsidies because Mexico has learned the lesson that subsidies simply create inefficiency. The companies must be competitive and subsidies simply breed inefficiency." We have an opportunity with Mexico that we have never had before.

VII. FOLLOW-UP ON MEXICO AND NAFTA

FERNANDO CERVANTES:*

The purpose is to explore where the business opportunities are. We are facing a new global world where business people and lawyers

* Fernando Cervantes graduated in 1966 from the Escuela Libre de Derecho, Mexico City, D.F.; he received a Masters Degree in 1968 in Comparative Law from Southern Methodist University; he is also a graduate of the Advanced Business Program for the Instituto Panamericano de Alta Direccion de Empresa at the Harvard Business School. Currently he is a Senior Partner in the firm of Cervantes y Asociados S.C. Tijuana, Baja California.

have to be visionaries and see where the new business opportunities are. I have some comments on the previous excellent presentations. The first has to do with the statement that our Canadian colleague made regarding Canada's doubts about the Free Trade Agreement. We have our own doubts too, but I think we should be realistic. We could call this new treaty the "No Choice Treaty." The reason is that the United States has lost its competitiveness worldwide. In the 1980s the United States clearly lost its competitive edge over countries like Japan. On the other hand, Mexico obviously needs the treaty. We cannot continue to live as we have over the past twenty years in a closed economy. So we have to change.

In order to understand the legal changes that have taken place in Mexico, you first must understand what has happened politically and socially and how that has been reflected economically and legally. If Mexico and the United States sign an agreement, Canada cannot remain alone. Thus, the agreement must be recognized by everyone, including politicians, groups, labor, and environmentalists. We must decide how we can resolve a situation realistically.

My second comment is that it is important for the United States, and foreign investors in general, to understand that all the recent changes that have taken place in Mexico, predominantly over the last year, are not changes of opportunity. By "opportunity" I mean changes like those that occurred in Mexico during the early 1980s such as the *maquiladoras* boom. *Maquiladoras* are foreign companies that are in Mexico to assemble products, importing materials, components, and equipment duty-free to Mexico, and exporting the finished assembled product. Basically, the opportunity comes from low labor rates. As any society becomes more prosperous, its labor rates increase. Therefore, cheaper labor becomes more and more attractive. As I have always said, I hope my children do not live in a *maquiladora* country. Therefore, the changes that are taking place in Mexico are in-depth changes. Why are these changes taking place? Jorge Camil mentioned some economic factors and I agree with Jorge. However, I would also consider the political aspect, which, to me, is very important.

In 1987, Mexico had a political crisis. The President of Mexico admitted that the so-called "system" failed. We are interested in the continuity and the stability of Mexico as much as you are, but we must provide the means for continuing growth. We must consider the political side. The PRI, which has been in power for over sixty years,

now suddenly admits that unless they change they will lose power to the opposition. The world has changed and socialism is no longer a viable alternative. Obviously, communism is not. I do not think Mexico has a choice. We must change if we want to have stability.

VIII. LABOR OPPOSITION TO NAFTA

SALVATORE OSIO:

The concern that I have heard more often than any other is the concern of labor in the United States. Certain segments, particularly the rust belt in the Northeastern United States and certain industries, such as the textile industry, are concerned with the massive displacement that may take place if those industries access more economical labor. Politically, the opposition of labor to NAFTA is significant. If Congress does not adopt NAFTA, it will be due to the influence of labor. How do the other panelists feel about labor's opposition to the treaty?

JORGE CAMIL:

I think that is a very important issue. My reply to labor concerns will be that we do not need the Free Trade Agreement. However, with Mexico entering the GATT and with Mexico's liberalization of import licenses and tariffs, etc., there is a free flow of products into Mexico that did not exist before. Those Mexican industries that have been producing costly and inefficient products must either shape up or see their companies disappearing and more imports coming from the United States. Efficiency necessitates this change. We have that today with Mexico's liberalization of its economy. The fact that this modernization process will be perfected and reflected in a document which will be the Free Trade Agreement is totally immaterial. Any bad consequences of the Free Trade Agreement on United States labor already exist today. Rather, the effects have been good for United States industry in causing a massive importation.

The most important industry is the auto industry. We have seen today a massive importation of auto parts that had previously been produced in Mexico. If automobile parts, such as engines, transmissions, and axles, are not produced or manufactured in Mexico, they do not qualify as Mexican products entitling them to government assistance and subsidies. Those subsidies have disappeared and Mexico has seen a massive importation of auto parts from the United States and Canada. This is beneficial to United States industry.

These opportunities will increase under a Free Trade Agreement situation.

FREDERICK HILL:

Mexico has been known and treated as a country where it is very difficult to get through bureaucratic processes. Do you think that a free trade agreement will improve this situation? I recognize that Mexico has advanced already by opening up its borders and by adopting a very recent new intellectual property law. United States technology that is exported and used in Mexico will have greater protection, but do you think NAFTA will help free up the Mexican opportunities by actually getting approvals and actually engaging in business transactions and investments there?

JORGE CAMIL:

No agreement of any kind, free trade or otherwise, is going to change the minds of people or the minds of bureaucrats. This is not going to be a panacea. Mexico has astutely addressed some of these issues. For example, before the 1989 foreign investment regulations, an investor wanting to have a majority or controlling participation in a Mexican company would need to wait for approval under the old 1973 law for up to two years. No one can wait two years to make a strategic corporate decision regarding where to invest \$100 million! Under the new regulations, an authority must answer an investor within a certain time period or the investment is considered automatically approved. The government has changed the law because it recognized that bureaucracy is a problem.

There is absolutely a practical improvement in this respect. The deregulation of transfer of technology is another case where Mexico has alleviated bureaucracy. Before the deregulation, a technology agreement with a Mexican company had to be translated and presented to the technology registry. Now, a free contract situation exists. In contemplation of the Free Trade Agreement, Mexico has shrewdly preempted many problems before the negotiations.

SALVATORE OSIO:

I have an observation on the employment issue and our labor unions. Due to Mexico's commitment to the import substitution economy over the last fifty years, it created a highly inefficient industry relying more heavily on labor than technology or modern equipment. Now, Mexican industry needs to be robotized; it needs new

technology; it needs new investment. Mexican industry cannot compete with the United States. For example, a consortium from Taiwan earmarked \$25 million to set up a joint venture with a Mexican manufacturer to produce lighting equipment. After spending approximately \$200,000 in due diligence, we discovered that, in order to compete in Mexico in a joint venture with a local manufacturer, we would have to triple the investment to almost \$75 million, buy all new equipment, and start from scratch in order to be competitive. We realized that United States companies were highly robotized with state of the art equipment. Labor became an insignificant cost factor. As a consequence, the United States, through its technology, through its capital intensive manufacturing processes, and through mass assembly, will be able to compete more effectively in the vast majority of cases. As a result, there will be a tremendous boom to United States industry almost across the board.

Some labor intensive industries will obviously not be able to compete with Mexico. The textile industry, with its sewing operators, is a good example. That type of industry will transfer to Mexico because labor is the principal factor in production. Those industries do not depend on robotization and high technology. There will be labor displacement. But Mexican industry, because it cannot compete with United States industry, will suffer the greater consequences. As a result, Mexican imports will create jobs in the United States. Regrettably, labor unions are not focusing on the greatest benefit in the United States, a net gain in United States employment through a net increase in exports to Mexico.

HENRI ALVAREZ:

I do not think we should be too optimistic about the benefits of free trade for labor. Being governed by democratic governments, competing political forces exist. There are strong lobbyists in all countries which continue to have interests contrary to free trade. We should not underestimate the resistance to change, but rather we should prepare for it. In fact, the negotiators should take these concerns into account.

There has been concern about the Fast Track Negotiation. Canada felt it was pressured into the last agreement. We were told it had to be done by a certain date or we would lose the fast track and never reach an agreement. Although that approach will bring the parties to the altar, and almost any deal is better than no deal, I think we must take care to negotiate the agreement with workable language. The

agreement between the United States and Canada has been criticized. Mexico should consider some of the concerns that were raised before the conclusion of that agreement. While I hope that we achieve the results that you say will come easily, I am reluctant to agree.