

PERSPECTIVES

NAFTA comes into force – with a glimmer of a social clause

Signed in August 1992, the North American Free Trade Agreement (NAFTA) between Canada, the United States and Mexico came into force on 1 January after having successfully passed its most critical test – the vote in the United States House of Representatives which opened the way to ratification by the Senate. It drew world attention for its symbolic significance: as agreement on the GATT Uruguay Round wavered in the balance, this vote was seen as an advance sign of whether the world would opt for more free trade or protectionism.

Within ten to 15 years, all customs duties will be abolished between the three partners. Within the next five years, 65 per cent of Mexico's industrial and agricultural imports from its northern neighbours will cease to be taxed. Once the treaty is ratified, duties on automobiles and spare parts exported to Mexico will be reduced by 50 per cent. Three-quarters of spare parts will be traded duty free in five years' time and vehicles in eight years on condition that at least 62.5 per cent of their components are manufactured in a NAFTA country. In the textile industry, the ceiling for duty-free trading will be progressively lifted – from US\$250 million as soon as the agreement is ratified to US\$700 million after six years – and abolished altogether within ten years for garments finished in a NAFTA country. The Mexican telecommunications market as well as banks and insurance companies will also progressively open up to investors from the North. Lorries registered in any of the three countries will be able to circulate freely in the other two. Mexico will drop the clause limiting inward investment by American companies to those engaged in export activities. In agriculture, Mexico will also immediately end its system of mandatory import licences for agricultural produce, making trade completely free within 15 years.

The entry into force of NAFTA should accentuate trends which have been in evidence since Mexico's accession to GATT in 1986 and the implementation of the Free Trade Agreement (FTA) between Canada and the United States in 1989. Certainly, trade within the area will be enhanced, economies will tend to specialize and the Mexican economy will be liberalized.

From signature to ratification

In Canada public opinion has never been highly favourable to the treaty. The Government endeavoured to preserve the advantages of its existing agreement with the United States, particularly with respect to the protection of "cultural industries" and its freedom to finance its health insurance and social programmes independently. The trade unions strongly opposed the accord: "it's *déjà vu*, ... the FTA has caused the loss of one in six manufacturing jobs ... we have seen what the FTA has given our country, and we know what awaits us with the NAFTA ..." declared the Canadian Labour Congress. On the other hand, the Canadian Manufacturers' Association as well as the Canadian Exporters' Association welcomed the possibility of gaining access to the growing Mexican market and the simplification of procedures in the arbitration of trade conflicts.

In the United States, too, large exporting companies have been among the most fervent supporters of NAFTA, owing to the prospect of setting up production units in Mexico where industrial labour costs US\$1.80 per hour compared with US\$14.77 at home and C\$16.02 in Canada. It is a prospect which has unleashed the anger of the AFL-CIO union federation: "the treaty is a bad deal both for American workers and consumers, for the long-term health of the American economy, as well as for Mexican workers who will be exploited by American firms".

"Mexico leaves the Third World." That is how many commentators announced the signature of NAFTA. An estimated 600,000 new jobs are hoped for. In Mexico, only the Democratic Revolution Party opposed the agreement. The economic liberalization policies implemented by President Salinas for several years aimed to prepare the country for open borders with its northern neighbours. None the less, Mexico has retained national ownership of its oil fields as specified in the Constitution.

Ratification of the treaty has posed no real problem in Mexico. In Canada there was a broad Parliamentary majority in favour, although many had reservations. In the United States, while the Senate vote was a formality, the House of Representatives showed itself far more sensitive to the concerns of the patchwork of various opponents of the treaty – industries threatened by competition, environmentalists and trade unions.

In response to their concerns, however, candidate, and subsequently President, Clinton committed himself to negotiating supplemental labour and environmental agreements with Canada and Mexico before the treaty was submitted to Congress for ratification. The two Supplemental Agreements, which were signed on 13 August 1993, were thus critical for gaining approval of NAFTA. Under the terms of both agreements, tariffs can be re-established in the event of violation of labour or environmental standards, and both follow essentially the same rationale: national standards may not be lowered in order to attract firms based in partner countries; each

State is committed to enforcing current legislation in its territory; and a procedure is established for the resolution of disputes, which includes, as a last resort, sanctions up to and including the re-establishment of tariffs in the branch in question. The agreement on labour cooperation can thus be regarded as the first glimmer of a social clause.

The labour agreement

This agreement, whose official title is the North American Agreement on Labor Cooperation, recalls in its preamble that the parties to the NAFTA have resolved to:

- create an expanded and secure market for the goods and services produced in their territories;
- enhance the competitiveness of their firms in global markets;
- create new employment opportunities and improve working conditions and living standards in their respective territories; and
- protect, enhance and enforce basic workers' rights.

Annex 1 enumerates the guiding principles that the Parties are committed to promote subject to their own domestic law (without establishing common minimum standards for their domestic law). These guiding principles are:

- freedom of association and protection of the right to organize;
- the right to bargain collectively;
- the right to strike;
- prohibition of forced labour;
- labour protection for children and young people;
- minimum employment standards (minimum wage, remuneration for overtime);
- elimination of employment discrimination;
- equal pay for women and men for equal work in the same establishment;
- prevention of occupational injuries and illnesses;
- compensation for occupational injuries and illnesses;
- protection of migrant workers equivalent to that enjoyed by nationals of the host country.

The three States are thus committed to applying their own labour laws in a transparent way and to guaranteeing that workers and employers have access to appropriate tribunals which will consider any complaints and ensure a fair and equitable hearing. There is also provision for workers and employers to cooperate and regularly exchange information and statistical data with a view to improving knowledge of each other's institutions and social legislation and promoting innovation, productivity and quality.

Institutions

To achieve these goals, the Commission for Labor Cooperation has been established. It consists of a Council (comprising the labour ministers of the three countries) and a Secretariat. The former will oversee the implementation of the Agreement and formulate recommendations for future action. It must submit a report on the operation and effectiveness of the Agreement within four years. The Council is also responsible for cooperation, collecting data, publications and resolving questions of interpretation of the Agreement which may arise between the Parties. Article 11 lists areas of cooperation which, in addition to those given in Annex 1, include human resource development, productivity improvement, labour statistics, and technical assistance for the development of labour standards.

The Secretariat is the executive body. It is responsible in particular for preparing reports setting out information supplied by the three Parties on:

- labour law and administrative procedures;
- trends and administrative strategies related to the implementation and enforcement of labour law;
- labour market conditions such as employment rates, average wages and labour productivity; and
- human resource development issues including training and adjustment programmes.

This institutional machinery is supplemented by the National Administrative Offices (NAO) which are responsible for ensuring that information circulates freely between the Secretariat, governmental agencies in their own country and their counterparts in the other two countries. Finally, independent Evaluation Committees of Experts (ECE) may be established for the purpose of reporting to the Council where it has not been possible to resolve a dispute concerning the Agreement through direct consultations between the Parties.

Resolution of disputes

If an ECE final report indicates that a Party is failing to enforce its own standards in the area of occupational safety and health, child labour or minimum wages, either of the other Parties may address a petition to the Secretariat and the two other Parties. Procedures involving several stages are then initiated. If the matter cannot be resolved within a specified period, the sequence is as follows:

- consultations between the Parties with the technical assistance of the Council (60 days);
- nomination by the Council and the Parties of a special Arbitral Panel comprising five qualified independent members (15 to 45 days); the Arbitral Panel will hear the Parties and investigate all the relevant facts

before publishing an initial report (within 180 days after the last panellist was selected) containing its recommendations. The Parties will reply, and a final report will be drafted (within 60 days). The Parties can then agree on an action plan based on the recommendations of the Arbitral Panel (within 60 days);

- where disagreement persists, the Panel may impose an action plan (after 120 days) which the Party complained against must accept (or propose an equivalent plan). Should the Party concerned fail to do so, it will be liable to a monetary enforcement assessment (within 90 days);
- if the Party complained against does not meet any of these obligations, the complaining Parties are empowered to suspend NAFTA benefits in an amount equivalent to that of the monetary enforcement assessment.

Canada has been able to ensure that, if it is complained against, the complaint will be dealt with by a court of competent jurisdiction in Canada to which the matter will be referred by the Commission.

The environmental agreement

The second of the NAFTA Supplemental Agreements concerns the environment. Environmental organizations fear that the most polluting activities will be shifted to regions where the rules are less stringent or little enforced. They cite the example of the *maquiladoras*. These enterprises are based in Mexico, mostly along the United States border, and take advantage of “free zone” status to produce goods exclusively for export. They stand accused of causing serious environmental damage. Using a system identical to that of the Agreement on Labor Cooperation, this Agreement provides for the establishment of mechanisms for monitoring environmental conditions in the three countries, proposing forms of cooperation, and eliminating abuses. If one of the Parties fails to comply with its own laws and regulations, it is liable to financial or tariff penalties. The newly established North American Development Bank together with the World Bank and the Inter-American Development Bank will place US\$8 billion at the disposal of the US-Mexico Border Environmental Commission, itself newly created for the purpose. The latter will implement various clean-up projects along the border.

Criticism tempered

In the United States it soon became clear that the Supplemental Agreement on the Environment was more ambitious than that on labour cooperation – hence the satisfaction of environmentalists, who became more favourably disposed to the NAFTA than they had been immediately after it was signed. On the other hand, the opposition of the trade unions remains as vigorous as ever. According to Mr. Lane Kirkland, President of the AFL-CIO, the Supplemental Agreements contain nothing which would make NAFTA acceptable to wage-earners. The same tone prevails in Canada, where the President of the Canadian Federation of Labour,

Mr. James McCambly, said that "With or without the so-called side agreements, the NAFTA has no effective provisions to recognize the importance of labour conditions in our trading relationships", while according to the Canadian Labour Congress "the NAFTA 'side deals' ... won't hire one unemployed worker nor will it do anything to protect workers' rights in any of the three countries or stop the flow of Canadian jobs from going South". On the other hand, the reaction in Mexico has been quite different – the Confederation of Mexican Workers welcomes the fact that national sovereignty is respected, and the same positive reaction has been noted among employers' and business associations.

Accompanying measures

Since major restructuring is to be expected as a result of the emphasis on a regional division of labour, an accompanying financial package has been drawn up. The Government of the United States will allocate US\$90 million to provide assistance and retraining for workers who lose their jobs in the 18 months following – and as a result of – the entry into force of NAFTA. At the same time, the Governments of Mexico and the United States will each invest US\$225 million in the new North American Development Bank. The latter will borrow US\$3 billion for loans to communities adversely affected by the treaty, as well as for clean-up operations in the border area.

A social clause?

It is clear that the main virtue of the Supplemental Agreements is that they discourage "social dumping" and counteract the tendency to adopt the lowest common denominator in labour and environmental standards. In that sense, they act as social and environmental clauses, the difference being that they refer not to minimum common or international standards, but to standards defined under national legislation in the respective countries.

The length of the procedure should also be noted; over two years may elapse before trade sanctions are enforced. Such sanctions are, in fact, subject to three conditions: there must have been a persistent failure to enforce the existing social provisions; there must be a similar law in the complainant country; and the dispute must concern the production of goods or services traded between the Parties. In addition, sanctions are only possible in the areas of child labour, minimum wages and occupational safety and health. The restriction is criticized by the AFL-CIO, which deplores the fact that sanctions are not provided in cases concerning freedom of association, the right to bargain collectively, and forced labour.

Economic impact

The Supplemental Agreements should not impede the overall economic thrust of the treaty, particularly since the latter confirms trends which are

already being felt at regional level. The United States expects that the treaty will result in a greater opening up of the Mexican market, to which American exports have tripled since 1986 (the year of Mexico's accession to the GATT), and an intensification of its investments in that country. The same applies to Canada, in those areas where it enjoys comparative advantage, such as some telecommunications, transport and state-of-the-art electronics. But it is in Mexico that the most spectacular, but also the most varied, effects of NAFTA are anticipated. Imports should rise considerably and the trading deficit should deepen with the reduction/elimination of the 12 per cent customs duty and import licences protecting 20 per cent of production. Mexico also expects to see growth in direct foreign investment. Here, too, the trend is already evident, since Mexico in 1992 became the world's major beneficiary of such investment. At the same time, voices are heard predicting that Mexico may become one huge *maquiladora* capable only of producing goods of low added value using labour-intensive methods, with no lasting benefits to the country.

Restructuring and employment

The accelerating trend towards regional specialization will inevitably lead to restructuring, with effects on employment that are a matter for debate. In the United States, for example, the balance of jobs lost to Mexico vis-à-vis jobs created by the opening up of the Mexican market will be a positive one according to the Department of Labor (64,000), the Institute of International Economics (130,000) and the Massachusetts Institute of Technology (150,000); the AFL-CIO, however, predicts a net loss of 500,000 jobs.

In Mexico, the consensus is that 600,000 jobs will be created, that is 2 per cent of the active population. It remains to be seen whether this will be enough to absorb the flood of jobseekers leaving the land as a result of the drastic restructuring of the country's agriculture – restructuring which is inevitable given the combined effects of the free trade agreement (i.e. competition from the far more productive agricultural sector in the North) and of the December 1991 land reform which abolished all limits on the size of agricultural holdings. This is in addition to the downward pressure on wages, whose already low levels constitute the main attraction for investors. It also remains to be seen whether the economic benefits of free trade will make up for its social and political costs.

Sources: US Government Printing Office: *The NAFTA Supplemental Agreements* (Washington, DC, 13 Sep. 1993). *Wall Street Journal* (New York), 18 Nov. 1993. *New York Times* (New York), 19 Sep. 1993. *Financial Times* (London), 14-15 Aug. 1993. *Le Monde* (Paris), 16 Aug. 1993. *Excelsior* (Mexico), 14 Aug. 1993. Canadian Labour Congress: *Press release* (Ottawa), 13 Aug. 1993. Canadian Federation of Labour: *Press release* (Ottawa), 13 Aug. 1993. K.S. Pham and M.A. Veganzones: "La zone de libre-échange nord-américain: trois stratégies pour un accord", in *Economie et statistique* (Paris), No. 264, 1993-4. R. Grinspun, M.A. Cameron and colleagues: *The political economy of North American free trade*, (New York, St. Martin's Press, 1993). ILO: *Social and Labour Bulletin* (Geneva), 1992, No. 4, p. 423, No. 3, p. 322 and No. 2, p. 258. Information provided by the ILO offices in Mexico, Ottawa and Washington, DC.