Trading Up
Consumer and Environmental Regulation in a Global Economy

David Vogel

Harvard University Press
Cambridge, Massachusetts
London, England
1995
Preface

The subject of this book grew out of my longstanding interest in government regulation of business. This is my third book on the politics of consumer and environmental regulation. In my first book on the subject, National Styles of Regulation: Environmental Policy in Great Britain and the United States, I explored government regulation from the perspective of comparative politics. Fluctuating Fortunes: The Political Power of Business in America examined the politics of protective regulation in the United States. This book moves beyond the realm of national politics to explore the relationship between protective regulations and international politics.

The origins of this project lie in a paper I wrote in 1989 that compared consumer protection policies in the United States and Japan. While researching this paper, I became aware that the impact of Japanese consumer protection standards extended beyond Japan's borders. To the extent that these regulations served as non-tariff trade barriers, they affected not only Japanese companies and consumers but also American firms seeking to export to Japan. American trade officials were pressuring Japan to change its regulatory policies on the grounds that they imposed disproportionate burdens on non-Japanese firms. The American effort was in turn vigorously opposed not only by Japanese domestic producers—for whom these regulations were a source of competitive advantage—but also by a number of Japanese consumer groups who claimed that the American demands threatened the health and safety of the Japanese public. During the following two years, my research on the politics of food safety and environmental
standards within the European Community exposed similar linkages between international trade and national regulation.

Until recently, students of environmental and consumer regulation paid little attention to the international dimensions of national regulatory policies. Virtually all studies of protective regulation, including my own, have been either national or comparative in focus. With the exception of the literature on international environmental issues and agreements, there have been few efforts to place the making of national regulatory policies in an international context. Likewise, relatively few studies of trade policy have examined the significance of consumer and environmental regulations as nontariff trade barriers, or explored the role of environmental and consumer organizations in shaping the debate over and the terms of trade agreements. Both these omissions are understandable since it is only relatively recently that the linkages between these formerly distinctive policy areas have become politically salient.

Thanks in large measure to the controversial 1991 General Agreement on Tariffs and Trade (GATT) tuna-dolphin decision and the 1990–94 debate in the United States over the environmental impacts of the North American Free Trade Agreement (NAFTA), the linkages between trade and regulatory policies have moved to a more prominent place on both the policy and scholarly agenda.

Since 1991, reports and papers on this subject have been issued by the United States Office of Technology Assessment, the U.S. Environmental Protection Agency, the Organization for Economic Co-operation and Development (OECD), The International Institute for Applied Systems Analysis, and the World Bank.¹ There have also been three edited volumes and two policy-oriented books.² Since 1992, numerous scholarly articles have been published on the subject of trade and regulation, mostly in law reviews.³

This book both draws upon and seeks to contribute to this rapidly growing literature on the relationship between trade policy and protective regulations. It is also distinctive in a number of respects. Most writing in this topic has focused on environmental issues, primarily in the context of a specific trade agreement, most frequently the GATT. The scope of this study is considerably broader. It focuses on the relationship between trade policy and both consumer and environmental regulation. In addition, it describes and compares the regulatory dimensions of a number of different trade agreements, including the GATT, the GATT Standards Code, the Free Trade Agreement (FTA) between the United States and Canada, and the North American Free Trade Agreement among the United States, Canada, and Mexico. It also examines the regulatory policies of the European Union (EU, formerly the European Community) in considerable detail.⁴ It treats the EU as an important case study on the relationship between economic integration and protective regulation, one with important implications for other agreements to reduce trade barriers, most notably NAFTA. In addition, it explores the ways in which the increasingly salient relationship between regulatory and trade policies have affected American politics and policies.

Virtually the entire scholarly literature on trade and regulation has been written by either lawyers or economists. This is the first extensive study of the subject by a political scientist. As such, it places particular emphasis on the role of nongovernmental actors—producers and environmental and consumer organizations—in shaping national preferences and international policy outcomes. It examines the interaction of two policy regimes, one of which, namely, trade policy, has always had an international dimension, while the other, regulatory policy, is rapidly acquiring one.

While I do address the debate over the impact of trade on environmental quality, that is not the central theme of this book. Rather, my primary focus is on the relationship between trade agreements, treaties, and conflicts and regulatory standards, especially those which directly affect the movement of goods across national borders. I do explore international environmental issues and treaties, but only in the context of their relationship to trade policies. This book is essentially a comparative study of six trade agreements and treaties and their relationship to national environmental and consumer regulations.

Although I do not offer any explicit policy suggestions, my analysis does have important political implications. I show that the incompatibility between freer trade and more effective regulation has been exaggerated. The fear on the part of many environmental and consumer

¹On November 1, 1994, following ratification of the Maastricht Treaty, the name of the European Community (EC) was officially changed to the European Union (EU). This book primarily uses the former term to describe specific developments that occurred prior to November 1994, and the latter to refer to European integration in historical or comparative terms.
groups, especially in the United States, that trade liberalization and agreements to promote that liberalization will weaken national regulatory standards is misplaced. On the contrary, I demonstrate how the former can, and frequently has, strengthened the latter. Rather than weakening the power of nongovernmental organizations in "greener" nations, trade liberalization and agreements to promote it can enhance the ability of NGOs to strengthen the regulatory standards of their nation's trading partners. In fact, increased economic interdependence has been associated with stronger, not weaker, consumer and environmental regulations. By contrast, "ecoprotectionism" threatens both free trade and, ironically, the improvement of environmental quality and consumer protection as well.

Because numerous consumer and environmental regulations have implications for trade agreements and policies, and vice versa, the scope of this book is potentially large. I have chosen to describe and assess the relationship between trade policy and protective regulation by emphasizing those linkages which either have become politically salient or which illustrate broader political trends. My logic of case selection is thus both broad and selective.

To explore the impact of the Treaty of Rome and the Single European Act on consumer protection in Europe, I examine one policy area in depth, namely, food safety regulation. This decision reflects not only the political and economic importance of trade in agricultural products within the EU, but also the critically important way in which the Union's efforts to reduce nontariff barriers in this sector have affected the legal and political development of the single market. I discuss the relationship between environmental protection and European economic integration by examining the development of national and Union standards for automobile emissions, chemical safety, and recycling. The highly contentious and prolonged debate over the formation of each of these regulatory policies illustrates the interaction of national economic interests and national regulatory preferences; together, these three case studies provide an overview of the impact of national and Union environmental regulations on intra-European trade. They also demonstrate how and why trade liberalization within the EU has contributed to the strengthening of environmental standards for traded goods.

My treatment of the GATT and environmental regulations is more exhaustive. I analyze each of the trade disputes that have come before dispute panels due to the (alleged) use of national environmental regulations as trade barriers. I also discuss a number of other trade disputes stemming from the divergence in national regulatory standards. In addition, I review and assess the growing debate over the impact of trade liberalization in general, and the GATT in particular, on both national and global environmental standards.

No formal dispute settlement proceedings have taken place under the Standards Code, which was adopted as part of the Tokyo Round GATT agreement in 1979. There has been, however, one highly a\-nomious trade dispute involving differences in consumer protection standards in the EU and the United States which the Standards Code avoided. It stemmed from the 1986 decision of the (then) European Community to ban the sale of beef from cows that had been fed growth hormones, which in turn severely restricted beef exports from the United States. Because of the political significance of this dispute and the economic importance of international trade in agricultural products, I examine in detail the role of food safety standards as trade barriers by reviewing a number of trade disputes between the United States and the EU, as well as between Japan and its trading partners.

There have been a number of both formal and informal trade disputes stemming from the role of national consumer and environmental regulations as nontariff barriers under the EU and the GATT Agreement. I examine each of them and assess the impact of their settlement on both American and Canadian regulatory policies. Since no dispute settlement proceedings have taken place under the North American Free Trade Agreement, I focus instead on the role of public interest groups in affecting the debate over the approval of NAFTA by the U.S. Congress and in shaping the terms of the final agreement.

I have benefited from the opportunity to present various portions of this book at a number of workshops, conferences, and conventions. The chapters on EU environmental policy, and the GATT and environmental regulation, as well as the material on Japanese consumer regulations, were presented at the annual meetings of the American Political Science Association. The chapter on EU consumer policy was presented at a biennial conference of the European Community Studies Association. The material on the EC-United States beef hormone dispute was originally prepared for a conference on "Reconciling Regulation and Free Trade," organized by the Centre for European Policy.
Studies in Brussels. In addition, I presented drafts of both chapters on EU regulatory policies at workshops sponsored by the Center for European Studies at Harvard University organized by Nicholas Zeigler. I also presented drafts of the first and last chapters at the Workshop on Institutional Analysis at the Haas School of Business, directed by Oliver Williamson. The comments I received from participants at each of these presentations helped me to develop and clarify my analysis.

A number of my colleagues at Berkeley and other universities have been generous enough to read through all or sections of this manuscript and offer me the benefits of their comments and criticisms. I am pleased to acknowledge the assistance of Vinod Aggarwal, H. Landis Gabel, John Goodman, Ernst Haas, Peter Haas, Robert Kagan, Jonah Levy, Richard Lyons, Thomas McCraw, Francis Van Loo, and Steven Weber. I particularly wish to express my appreciation for the careful and critical readings of the entire manuscript by Steve Ch tattovich of the Competitiveness Policy Council, Abram Chayes of the Harvard Law School, David Mowery, my colleague at the Haas School, Richard Steinberg of the Berkeley Roundtable on the International Economy, and David Yoffie of the Harvard Business School. This book in no small measure reflects the knowledge and insights of each of these individuals, and I am very much in their debt.

I am especially pleased to acknowledge the contribution of my research assistant and friend, Tim Kessler, a graduate student in political science at the University of California, Berkeley. He competently and cheerfully assisted me at every stage of this project, from the original research through the various drafts. Whatever coherence this book possesses owes much to his valuable assistance. Serena Joe of the staff of the Haas School also provided much-appreciated assistance in manuscript preparation. David Stolzgros and Susan Wallace Bohmer assisted with the final editing.

As always, my deepest thanks go to my wife, Virginia, for her editorial assistance, encouragement, and endurance. As she can amply testify, writing books doesn’t seem to be getting any easier.

The research and writing of this book were primarily supported by a series of grants from the Alfred P. Sloan Foundation, administrated through the Consortium On Competitiveness and Cooperation at the University of California, Berkeley, Center for Research in Management. I wish to express my appreciation to the Center’s director, David Teece, for recognizing the importance of this project and for helping me to secure the funding needed to pursue it. Financial assistance was also provided by the Social Science Research Council, the UC Berkeley Committee on Research, and the Haas School of Business.

Reducing Trade Barriers in North America

The impact of trade liberalization on environmental and consumer standards played an important role in the debate over both the Free Trade Agreement, between the United States and Canada, and the North American Free Trade Agreement, which extended the free trade zone to include Mexico. In the case of the FTA, this debate primarily took place within Canada; in the case of NAFTA, it took place largely within the United States. In part due to the political strength of nongovernmental organizations in the United States, and in part due to the strength of the United States' government relative to Mexico's, NAFTA is a much greener trade agreement than the FTA. Thus, while the regulatory provisions of the FTA closely resemble that of the GATT, NAFTA bears a closer resemblance to the Single European Act. While the FTA has had relatively little discernible impact on the regulatory policies of either the United States or Canada, NAFTA is likely to contribute to a shift in national regulatory standards and their enforcement toward those of the largest and most powerful North American nation.

The Free Trade Agreement

In early 1986 the United States and Canada began negotiations aimed at reducing or eliminating trade barriers between the two countries. An agreement was finalized in the fall of 1987 and signed by President Reagan and Prime Minister Mulroney on January 2, 1988. On the whole, the American business community strongly supported the FTA, although there was some opposition from various natural resource and agricultural producers. However, neither American consumer nor environmental groups participated in the congressional debate over its ratification. It was approved by Congress in the fall of 1988, acting under fast-track negotiating authority.

The response to the agreement in Canada differed markedly from that in the United States. Following its passage by the lower house, the agreement was stalled in the Senate. Prime Minister Mulroney then dissolved Parliament and called for a new election. This election was dominated by the issue of free trade and the long-term impact on Canadian society of closer economic integration with the United States. Many Canadians expressed concern that the removal of trade barriers to American goods would both overwhelm Canadian producers and undermine Canada's political and cultural autonomy. The leader of Canada's Liberal opposition party claimed that Mulroney had "sold Canada down the river."

The Politics of Ratification

The effect of the trade agreement on Canadian environmental policy figured prominently in the public debate over the treaty. For the most part, Canadian environmentalists strongly opposed the FTA. In particular they objected to the treaty's impact on the conservation policies of both the provincial and central governments of Canada. A clause in the FTA prohibited the Canadian government from limiting exports of nonrenewable resources, including energy, unless domestic sales were similarly restricted. This provision was criticized not only for undermining Canada's control over its natural resources, but for biasing Canada's energy and resource policy toward extraction and away from conservation.

Environmental and consumer groups were also troubled by the agreement's potential impact on Canadian regulatory policies. According to its critics, the agreement's provisions left unanswered some critical questions. For example, would differences in environmental requirements and conservation programs between Canada and the United States be considered "subsidies" and therefore constitute unfair trade practices? Would the agreement require Canada to modify some of its future regulatory standards—either upward or downward—to bring them more in line with those of the United States?
The FTA's commitment to the harmonizing of American and Canadian pesticide standards particularly worried Canadian environmentalists, since they considered American standards to be too lax. Pesticide approval in the United States is based on a balancing of risks and benefits, while the Canadian Pest Control Products Act only focuses on the safety of the proposed pesticide. According to a Canadian environmental lawyer, "The difference between the two approaches ... explains why there are twenty percent more active pesticide ingredients registered for use in the United States and over seven times as many pesticide products." 96

Environmentalists also criticized the Canadian government for negotiating a comprehensive trade agreement likely to have a significant impact on the Canadian economy without attempting to assess its environmental ramifications. They were disturbed as well by the Canadian government's statement that "the free trade agreement is a commercial accord ... not an environmental agreement ... The environment was not, therefore, a subject for negotiations; nor are environmental matters included in the text of the agreement." 96

The opposition of Canadian environmentalists to closer economic integration with the United States in part reflected the ongoing and long-standing dispute between Canada and the United States over American "exports" of acid rain to Canada. For more than a decade, the Canadian government had been unsuccessfully pressuring the United States to require coal-burning power plants near the Canadian border to curb their emissions of sulphur oxides. Numerous bills to curb these emissions had been introduced in Congress, but none had been approved due to both opposition from the Reagan administration and a lack of agreement within Congress about how the costs of abatement were to be allocated among the states. In 1988 the Province of Ontario joined with several American states whose forests and lakes were also being damaged, as well as with American environmental organizations, to request that the Environmental Protection Agency enforce Section 115 of the Clean Air Act, which addresses international pollution controls. After EPA refused to do so, a lawsuit was filed, which was still pending while the debate over Canadian ratification of the FTA was taking place.

While public opinion polls reported that the majority of Canadian voters opposed the trade agreement, the Conservative Party won a majority of seats in the new Parliament. As a result, the treaty was officially ratified by Canada in December 1988 and went into effect the following month.

The Terms of the Agreement

The Free Trade Agreement subsumes rather than supersedes each nation's current trade laws or obligations. But while based primarily on GATT and GATT principles, its scope and coverage are significantly greater in a number of respects. The FTA phases out all tariffs between the two countries over a ten-year period. In addition, the agreement applies the GATT principle of national treatment to all government policies that restrict trade. Thus, while each nation maintains its policy independence, whatever policies it enacts must be applied equally to all goods, regardless of where they are produced or the nationality of the firm that produces them. However, these principles apply only to new or changed regulations, not to existing ones— even if the latter violate the principle of national treatment.

The treaty specifies that health, safety, environmental, or consumer regulations are not to be considered trade barriers; it affirms that the "right to maintain regulations to protect human, animal and plant life, the environment ... is a sovereign issue for each country to decide." Nevertheless, it also states that regulatory actions whose effect is to restrict trade will only be permitted if it can be demonstrated that they "achieve a legitimate domestic objective," and it specifically precludes the use of standards-related measures as disguised trade barriers. In addition, Article 608 commits the two countries to recognize each other's accreditation systems for testing facilities, inspection agencies, and certification bodies.

Equally important, both nations agreed to coordinate their product standards to reduce their role as trade barriers by establishing "equivalent" (defined as "having the same effect") technical regulations and standards and, in the case of agricultural products, to move toward harmonization. The agreement's chapter on agriculture specifically pledges both nations "to make equivalent or to harmonize, where possible, testing and evaluation procedures, labeling requirements and residue tolerances for certain chemical products," including fertilizers and pesticides.

The FTA also contains a much stronger mandate than the GATT Tokyo Round agreement to ensure compliance with the agreement by
subnational governments. This reflects the fact that both the United States and Canada are federal systems in which state and provincial governments play important regulatory roles. The language of the FTA is similar to that of the Uruguay Round agreement, both are required to "ensure that all necessary measures are taken in order to give effect to its provisions, including their observance ... by state, provincial and local governments." The legislation approved by both nations implementing the trade agreement further states that "its provisions prevail over any conflicting state law." The FTA established a Canada-United States Trade Commission, whose principle participants are the senior trade officials from each country. It oversees the working of the agreement and resolves disputes arising from its interpretation or implementation. If disputes cannot be settled within thirty days after being referred to the Commission, they are sent to an arbitration panel. FTA dispute panels operate on a strict timetable and their decisions must be accepted by both parties. This latter provision parallels the tightening of dispute settlement procedures in the newly established World Trade Organization.

Conservation Trade Disputes

The first trade dispute between Canada and the United States under the FTA involved a conservation issue whose origins predated the treaty. In 1980 Canada began to prohibit the export of unprocessed herring and salmon. Canadian officials argued that this regulation was necessary to enable them to maintain quality controls over their fish exports and thus ensure their access to a highly competitive international market. During the mid-1980s, the United States complained to the GATT, which in 1987 ruled against Canada on the grounds that Canada had not imposed comparable restrictions on domestic food processors and consumers (see Chapter 4).

Following the adoption of the GATT panel's report on Canadian fish exports, Canada revoked its regulations prohibiting the export of unprocessed herring and salmon. However, it also imposed new regulations. It now required that five species of salmon as well as all commercial harvest of roe herring caught in waters off Canada's west coast be first brought ashore at a licensed fish landing station in British Columbia for biological sampling—after which they could be exported. Canadian officials argued that this requirement was necessary in order to enable them to promote the conservation of these important species, which were being depleted due to inadequate fisheries management.

The United States complained that although the new regulations were worded so that they did not directly affect exports, their clear effect was discriminatory since the burden of compliance fell exclusively on exporters. By contrast, fish purchased by Canadian processors would be landed in Canada in any event. Accordingly, the Canadian requirement was really an export restriction due to "the extra time and expense U.S. buyers must incur in landing and unloading, as well as dockage fees and product deterioration." American officials went on to argue that the law's real purpose was to protect British Columbia's fish processing industry from American competition, since fresh fish has to be processed as soon as it is brought ashore. In sum, "the Canadian landing requirement was an environmental policy acting as a disguised restriction on international trade." After consultations between the two nations failed to resolve the dispute, the United States had the choice of seeking settlement under either the GATT or the FTA. It chose the latter. But whichever venue it had chosen, the legal basis of the American complaint was identical, since the relevant provisions of the GATT had been incorporated into the FTA.

The dispute panel concluded that the Canadian regulation, while ostensibly an internal measure, was in fact a trade restriction, since it imposed a "materially greater commercial burden on exports than domestic sales." According to the panel, "the cost of complying with the landing requirement would be more than an insignificant expense for those buyers who would have otherwise shipped directly from the fishing grounds to a landing site in the United States." The second issue addressed by the panel was whether or not the Canadian rule was justified by the "exception" clause of Article XX of the GATT, which also had been incorporated into the FTA. Drawing upon the criteria established by the 1987 GATT ruling on Canada's export ban, the panel argued that for Article XX to be applicable, the primary aim of the trade restriction had to be conservation. Employing a cost-benefit test, it concluded that this was not the case, since it was highly unlikely that Canada would have imposed the same requirements "if its own nationals had to bear the actual costs
of the measure.15 Moreover, the landing requirement failed the "proportionality test," since Canada could have achieved the same conservation objectives by exempting a portion of the catch from the landing requirement. The panel specifically suggested that allowing between 10 and 20 percent of the fish catch to be exported directly would not adversely affect Canada's conservation program.

The reaction of the two governments to the panel ruling suggested the depth of their differences over this long-standing commercial dispute. Canada's Ministry of International Trade, Fisheries and Oceans issued a press release that accepted the panel's report, but added that it had "found that a landing requirement is a legitimate conservation measure."16 American officials, in turn, offered a rather different interpretation. Noting that the panel members had suggested an alternative to the landing requirement, they complained that Canada had read "the findings in the narrowest way possible to maximize protection for west coast interests."17 Officials from both nations were troubled by the resulting impasse. A U.S. government official predicted that the dispute "could have adverse effects for the FTA," while his Canadian counterpart acknowledged that the dispute over the meaning of the panel's ruling did not augur well for the future of an agreement whose purpose was to liberalize trade.18

However, both nations did agree to accept the panel's primary recommendation, specifically that Canada could require that between 80 and 90 percent of fish caught in Canada be processed there, even if they continued to disagree over the meaning of the panel's ruling.Canada continued to insist that the panel had upheld its sovereign right to impose conservation programs; an advisor to the Canadian government told a Senate committee that "Canada had got what it wanted from the panel report because it can still require 80 to 90 percent of the catch to be landed for conservation purposes."19 American officials in turn also declared "victory," since the panel had upheld their complaint that "the landing requirement was an unfair trade restriction disguised as a conservation measure."20

Following additional negotiations both sides announced a compromise agreement: 73 percent of the catch must be first landed in Canada, while the remaining 27 percent could be directly exported. The Americans regarded this outcome as satisfactory, but it upset both the government and fisheries processing industry of British Columbia. B.C. International Business Minister Elwood Veitch predicted that "this decision will have negative impacts on this important resource and the industry that supports it."21 The executive director of the Fisheries Council of British Columbia complained that "what the panel decision actually does is strike down a legitimate resource conservation scheme and recommend substitution of an expensive, loophole-laden, unmanageable dual reporting scheme."22 A Canadian environmental lawyer concluded that "the salmon and herring case illustrates that in a contest between environmental and trade objectives, the former is not likely to come out the winner," adding that "the implications of this precedent for other conservation programs are very serious."23

The following year another trade dispute broke out between the two countries over fishing rules, this one brought by Canada against the United States. In order to conserve its domestic lobster stocks, the United States had limited the harvesting and marketing of lobsters below a certain size. However, the mixing of smaller Canadian lobsters with American lobsters had made it difficult for American officials to enforce this restriction, since American fishermen frequently used fraudulent documentation to "prove" the Canadian origins of their undersized (and under-age) lobsters. In addition, a number of U.S. lobster fishermen complained that the federal size requirement put them at a competitive disadvantage vis-a-vis their Canadian competitors. Accordingly, in 1989 the United States amended the Magnuson Act to make it unlawful "to ship, transport, offer for sale, sell, or purchase, in interstate or foreign commerce, any whole live lobster . . . at a size below that specified by the Act."24 This restriction applied to all lobsters, regardless of where they were originally harvested.

This legislation significantly restricted sales of mature Canadian lobster in the United States, since due to the warmer temperature of Canadian waters, Canadian lobsters mature more quickly and reproduce when still relatively small. Canada argued that because the ban on the importation of smaller sized lobsters affected only Canadian imports, the size limitation was, in effect, a "trade restriction which the United States is attempting to disguise as a conservation measure."25 Canada claimed that the Americans were seeking to deprive them of the competitive advantage they enjoyed because their lobsters matured earlier. According to Canadian officials, nearly one-third of Canadian lobster exports were affected by the prohibition, resulting in an annual loss of 40 million dollars. The United States countered
that the minimum size requirement was an internal measure that applied equally to domestic and foreign lobsters, not a border control targeted at imports. And because it treated Canadian and American lobsters alike, it was consistent with the GATT principle of national treatment.

In a divided (3–2) vote, the panel upheld the American position on the grounds that the minimum size provisions enacted by the United States were “primarily aimed” at the conservation of American lobsters. The minority opinion, however, took strong issue with this conclusion, arguing that the United States should have been required to demonstrate that its legitimate conservation objectives could not have been met by alternative measures, such as the special marking of Canadian small lobsters or by requiring that lobsters be sorted by size prior to their importation into the United States.

The minority report also reviewed the legislative history of the amendment to the Magnuson Act. While it found a number of statements that underscored the conservation rationale for the lobster size restriction, it also found evidence that another important purpose of the legislation was to remedy the fact that “U.S. lobster fishermen were at a competitive disadvantage because they were subject to more stringent conservation regulations than the Canadians.” The minority report concluded that the United States “had not made their case strongly enough to lead . . . to the conclusion that the measures were primarily aimed at conservation.”

By contrast, the majority opinion acknowledged that although the Magnuson Act was in part motivated by perceptions of “unfairness” on the part of American lobster fishermen, this did not render the American size restriction illegitimate; on the contrary, it explicitly acknowledged the legitimacy of these perceptions. Surprisingly, neither the majority nor the minority report chose to address the Canadian claim that its lobsters reached sexual maturity at a smaller size than American lobsters because of differences in water temperature.

Environmental Trade Disputes

Ironically, notwithstanding the fears of Canadian environmentalists that the FTA would force Canada to weaken its regulatory standards, the first environmental dispute between the two countries following the enactment of the FTA was prompted by the relative strictness of American standards. In 1989, following nearly a decade of public discussion and legal proceedings, the U.S. Environmental Protection Agency banned the use of asbestos on the grounds that it posed an unreasonable risk to health and the environment.

A number of American firms challenged the EPA rule on the grounds that the agency’s rule-making procedure was flawed. However, the ban’s economic impact on Canadian producers was more serious, since Canada supplied 94 percent of the asbestos used in the United States. Equally important, the Canadian asbestos industry feared that the U.S. rule would create a “dangerous precedent” by encouraging the European Community to establish a similar standard. Subsequently, a Canadian mining company and three Canadian labor unions joined the American plaintiffs in their suit against the EPA ban. They argued that “EPA failed to consider the effect of the ban on foreign firms and their employees who supply the U.S. market.” More substantively, they contended that the ban was not based on adequate scientific evidence, to failing to distinguish the health hazards of different kinds of asbestos fibers. Both Canadian parties claimed that they had a direct interest in the EPA’s rule and that, under the terms of the Toxic Substances Control Act, they were entitled to petition for judicial review.

On May 22, 1990, the Canadian government filed an amicus brief in support of the Canadian litigants. It argued that “American treaty obligations under the GATT granted the plaintiffs legal standing to protest EPA’s actions, since the treaty requires nations to indicate that their environmental decisions meet international standards, thus preventing countries from using arbitrary environmental rulings as de facto trade barriers.” Canada claimed that because the EPA ban was not supported by sufficient scientific evidence, it constituted an import provision which violated the GATT, as well as an unnecessary obstacle to trade according to the terms of the GATT Standards Code. Canada also argued that the U.S. rule violated Article 603 of the FTA, which prohibits both parties from adopting standards-related measures that create unnecessary obstacles to trade, unless they achieve “a legitimate health objective.” According to the Canadian government, “to the extent that the EPA rule bars the importation of products that do not cause unreasonable risks to life or health, the rule is not necessary to achieve a legitimate domestic objective, and therefore runs counter to U.S. FTA commitments.”
The Fifth United States Circuit Court of Appeals struck down the EPA rule prohibiting the importation, manufacture, processing, and distribution of most products containing asbestos. However, it based its decision solely on arguments about domestic law advanced by domestic parties. The court denied standing to the Canadian plaintiffs on the grounds that “EPA was not required to consider the effect on people or entities outside the United States”; it further noted that “international concerns are conspicuously absent” from the Toxic Substances Control Act. The court suggested that GATT, not the American judicial system, was the appropriate forum for addressing the effects of American domestic regulations on international trade. Canada did not, however, file a formal complaint with either the GATT or the FTA.

Although American courts refused to hear the Canadian petition, the filing of the suit was politically significant; it marked the first time that American environmentalists became aware of the potential impact of the FTA on domestic regulatory policies. Not surprisingly, American public interest organizations were extremely upset by Canada’s effort to use the FTA to undermine an American regulatory policy. According to Ellen Haas, the executive director of the Public Voice for Food and Health Policy, “The Canadian challenge sends a chilling message for U.S. regulators faced with making decisions to ban hazardous chemicals.” An article in the Progressive predicted that had the Canadian position prevailed, an additional 1,900 American lives would have been lost by the end of the decade. The suit also alarmed Canadian environmentalists, for whom it confirmed their long-standing suspicion about the treaty’s potential for abuse by producers seeking to weaken the regulatory standards of their trading partners.

The two nations have also been involved in a series of trade disputes stemming from each other’s recycling laws. In each of these cases, environmentalists and domestic producers have found themselves on the same side, both seeking to defend environmental policies that also impeded trade. While there is no federal recycling requirement, thirteen American States have enacted recycling laws to encourage the use of recovered materials in newsprint in order to reduce their urban landfill problem. These laws require that certain types of pulp and paper consumed in the state contain a minimum recycled content, which ranges up to 50 percent. The Canadian pulp and paper industry urged Canada to challenge the legality of these laws. According to the Conference Board of Canada, “From the viewpoint of the Canadian pulp and paper industry, . . . United States recycling legislation is a disguised non-tariff barrier to trade because Canada does not have the supply of recycled fibre to maintain market share in the United States.” Canada’s largest pulp and paper firm specifically urged the Canadian government to challenge American newspaper recycling laws “as a ploy of United States newsprint producers seeking to gain competitive advantage.”

The American state laws have imposed a real hardship on Canada, which is the world’s largest producer and exporter of newsprint. Historically, Canada exported 85 percent of its domestic production—75 percent to the United States and 10 percent to Europe. However, since it is expensive to collect and ship waste paper from urban centers in the United States hundreds of miles to Canadian paper mills to transform it into newsprint and then ship it back to the United States, the American recycling requirements have shifted the location of new newsprint production facilities from proximity to forests to proximity to waste paper. Thus, between 1989 and 1992 the percentage of American newsprint imported from Canada declined from 36.3 to 30.3. Canada, however, has not filed a challenge to the United States under either the FTA or the GATT in part because it is unclear if such a challenge would succeed. Needless to say, American environmentalists, as well as American firms involved in the recycling business, have strongly defended American recycling requirements.

In 1992 another trade dispute emerged between the United States and Canada over recycling, this time with American producers challenging a Canadian regulation. It raised issues strikingly similar to the Danish bottles case, which had been decided by the European Court of Justice four years earlier. The dispute dates from the mid-1980s, when the United States began to complain about Canadian restrictions on the sale of American beer in the province of Ontario, where the American market share was only 4 percent. Following a GATT dispute panel decision which addressed the discriminatory distribution practices of provincial liquor boards, a tentative agreement was reached in the spring of 1992. However, the following week Ontario announced a doubling of the tax on all nonrefillable alcoholic con-
tainers to 10 cents a can. This tax increased the retail price of American beer sold in aluminum cans from $1.98 to $2.35 per case.

The Province of Ontario described the levy as a “green tax” whose purpose was to encourage the use of bottles, which are refillable. Provincial officials contend that glass bottles are more environmentally efficient, since they can be used an average of 15-18 times; they are also much less likely to end up in garbage cans and landfills. They claimed that without the additional tax, their province’s extensive recycling efforts would be undermined: consumers would switch to less expensive imported beer sold in aluminum cans, thus forcing Canadian brewers, most of whom used bottles, to switch to cans as well. According to a Canadian official: “Ten cents seems to be the correct level to make it an effective incentive to change consumer behavior.”

American beer companies, along with American trade associations representing aluminum and can manufacturers, claimed that the Canadian tax was a protectionist weapon disguised as an environmental regulation, since virtually all Canadian beer was sold in bottles, while most beer imported from the United States was sold in cans. The Canadians countered that American brewers could avoid the tax by switching to “environmentally friendly” bottles; the Americans replied that the extra weight made bottles too expensive to ship. They also argued that using aluminum cans actually consumes no more energy than the washing, transportation, andrefilling of bottles. As further evidence of the protectionist intent behind the Canadian action, they noted that Ontario had only taxed nonrefillable alcohol containers, not cans of soft drinks, juice, andfood—an argument similar to that made by the European Commission in the Danish bottles case (see Chapter 3). The position of the Province of Ontario was strongly backed by Canadian environmental organizations. Zen Makuch, a lawyer with the Canadian Environmental Law Foundation, argued that “the United States has to play by our rules.” He added: “The U.S. system should not be imposed on us, when ours is more environmentally sound.” However, a columnist for the Toronto Star agreed with the United States, describing the tax as “a smoke screen for protectionism.” Since the imposition of the 10-cent tax, the consumption of beer in Ontario in nonrefillable beverage containers has declined by 60 percent.

In July 1992 the United States imposed a 50 percent ad valorem tax on beer from Ontario, though this was due to the continuing impasse over the broader issue of market access rather than to the beer can tax. A year later a comprehensive settlement was reached that removed a variety of barriers to exports of American beer, and the United States rescinded its tax. Due to the intervention of the Clinton White House, which did not want to use the FTA to force the Canadians to rescind an environmental regulation, especially in light of the upcoming debate over the environmental impact of NAFTA, Ontario’s beer can tax was allowed to stand—much to the chagrin of American brewers, who have seen their market share fall still further since the imposition of the Canadian environmental levy.

In 1992 another trade dispute broke out over the alleged use of a protective regulation as a nontariff barrier. The previous year, after two decades of pressure by the Food and Drug Administration, Puerto Rico agreed to adopt the system used in the U.S. states for certifying and inspecting dairy facilities. This policy change ended Puerto Rico’s imports from Quebec, Canada, of ultra-high temperature milk processed for long shelf life. Canada promptly challenged the new Puerto Rican standard as a violation of the FTA. In its brief, the United States stated that the case “is of great significance to the Free Trade Pact as it will be the first to interpret the rights and obligations of the United States and Canada with respect to the enforcement of technical standards designed to protect public health and safety.”

The dispute panel issued its decision in June 1993. It noted that although “standard-setting is a significant prerogative of States . . . standards have an effect on imported goods which cannot be ignored.” However, it went on to state that the FTA “affords broad discretion in the setting of health standards applicable to imported products,” provided that these standards applied equally to domestic and imported products and are not intended to afford protection to domestic producers. Accordingly, it concluded that the American regulation did not violate the FTA.

Criticisms

Environmental and consumer groups on both sides of the border have continued to criticize the FTA. For example, in 1991 American consumer groups blamed the FTA for allowing possible meat to enter the United States as a result of the “streamlined” meat inspection system.
established a month after the FTA went into effect. According to Lori Wallach, a staff attorney with Public Citizen’s Congress Watch, “One of the little-noticed results of the Canada FTA . . . was the dismantling of meat inspection along the U.S.—Canadian border.” Under the new system, only one truck in fifteen is inspected; the rest, she contended, was a “terrifying increase in meat imports contaminated with feces, pus-filled abscesses and foreign objects such as metal and glass.” American officials claim that the Canadian meat inspection system is equivalent to that of the United States; the American Food Safety Inspection Service informed Congress that it has “more confidence in the Canadian inspection system’s ability to ensure wholesome meat than they do that of other countries.” However, in 1991 the U.S. Department of Agriculture agreed to withdraw a proposal to end all American meat inspections along the Canadian border.

For their part, Canadian environmentalists have continued to argue that the FTA has undermined the quality of Canada’s physical environment, though their criticism has centered primarily on “the structural and economic realities” of free trade itself, rather than on the impact of the FTA on specific domestic regulations. To date, only one Canadian conservation policy has been successfully challenged under the dispute-settlement procedures established by the FTA: British Columbia’s fish landing requirement. And this decision resulted in a compromise.

Nor has the trade agreement affected Canadian pesticide regulations. Indeed, even before the FTA went into effect, American and Canadian regulatory decisions were tending to converge. Of the ten high-profile pesticide controversies that have taken place in either country since 1970, the two countries have responded identically in eight of them. Of the remaining two, the American regulation was stricter in one case, while the Canadian standard was stricter in the other.

Canadian regulatory officials have tended to follow the lead of their counterparts in the United States, primarily due to the greater scientific resources available to American officials, the dominance of the American media, and the greater size of the American market. These three factors predate the FTA and overshadow it in significance. In 1990 the Canadian government announced that while it will continue to per-
for export to the American market, illustrating the role of one dimension of the California effect—the lure of greener markets—in strengthening regulatory standards for traded goods.60

NAFTA

The regulatory dimensions of the FTA—at least in the United States—were soon overshadowed by the debate over the environmental impact of the proposed North American Free Trade Agreement (NAFTA), which would extend the FTA to include Mexico. Unlike the debate over the FTA, American consumer and environmental organizations were highly visible participants in the debate over approval of NAFTA. In marked contrast to the experience of their Canadian counterparts a few years earlier, their political impact was substantial.

The Environmental Challenge

Following the conclusion of the FTA, the United States began negotiations with Mexico with the goal of creating a free trade zone throughout North America. Much of the impetus for this initiative came from Mexican President Carlos Salinas de Gortari, for whom the expansion of trade and investment with the United States was critical to his plans to liberalize and modernize Mexico’s stagnant economy. American opposition to NAFTA was spearheaded by citrus and vegetable growers, the American textile industry, and the AFL-CIO, all of whom feared competition from Mexican producers. However, in addition to this expected economic opposition, from the outset much of the criticism of NAFTA focused on the treaty’s impact on environmental and consumer protection in the two countries. American consumer and environmental organizations expressed a number of concerns about the proposed agreement.

The first had to do with the environmental impact of Mexico’s maquiladora factories. As a result of an earlier agreement to permit goods produced or assembled by factories in Mexico located near the American border to enter the United States duty-free, nearly 2,000 factories, mostly American-owned assembly plants, had located in this region. But due to the lax enforcement of Mexico’s environmental

laws, these plants were generating substantial amounts of pollution, much of it toxic. The National Wildlife Federation regarded the issue of border pollution as its highest priority in U.S.-Mexican environmental relations.61 The National Toxics Campaigns reported that many maquiladoras were disposing of their hazardous wastes illegally, contaminating rivers and streams.62 Environmentalists pointed out that contamination levels in the Rio Grande were many times greater than those considered safe for recreational use.63 Nor were the effects of this pollution confined to Mexico. Raw sewage dumped into the New River in northern Mexico had been carried across the border to California, while Tijuana’s lack of adequate waste disposal had polluted beaches in San Diego. In San Elizario, Texas, where a shared aquifer had been contaminated, 35 percent of the children contracted hepatitis by the time they were eight years old, and 90 percent of adults contracted it by the age of 35.64 An American environmental writer predicted that “if Bush gets his version of free trade between the United States and Mexico, this systematic poisoning of an entire region… could prove impossible to stop.”65

A second related issue focused on the environmental impact of increased American investment in Mexico in general. Many environmental organizations feared that NAFTA would encourage American firms to take advantage of Mexico’s laxer enforcement of its pollution laws to relocate their production throughout all of Mexico, thus further exacerbating Mexico’s pollution problems—and at the same time costing American jobs. Craig Merrihew, the San Francisco co-director of a grassroots organization opposed to NAFTA, stated: “We think the experience across the border is the best predictor of what will happen under a broader agreement. It’s a wild-West, dump-and-run kind of situation that has turned the 2,000 mile border into one big Love Canal.”66

A third concern revolved around the trade agreement’s impact on American regulatory standards. Many public interest groups feared that a free trade agreement with Mexico would result in downward harmonization of consumer health and safety standards, since America’s stricter product standards could potentially be challenged by Mexico as nontariff barriers. Mexico is the largest supplier of produce to the United States, and many pesticides prohibited or suspended by EPA are used by Mexican farmers.67 In testimony before
Congress on NAFTA, American environmental groups frequently cited the Canadian challenge to the American ban on asbestos as a precursor to the kinds of legal challenges to American regulations that Mexico might mount were NAFTA to be approved.19

A fourth related issue—which also drew on the experience of the FTA—concerned the impact of NAFTA on border inspections. According to Lori Wallach of Public Citizen, “If meat from Canada has proven a serious concern to American consumers, the danger of re-inspecting meat from Mexico, not to mention Mexican fruit and vegetables, is many times greater.”20 She warned that “if the Mexico agreement follows the pattern of the U.S.-Canada agreement, effective border inspection would be all but stopped.”21

The Mobilization of Opposition

For American environmental groups, often frustrated by their inability to have a greater impact on environmental policy outside the United States, the political opportunity offered by NAFTA was unprecedented: the debate over the treaty in the United States provided them a vehicle for influencing the environmental policies of a developing country. As Stewart Hudson of the International Program Division of the National Wildlife Federation put it, “We have to take a stand here and set a correct model.”22 For their part, Mexican environmentalists also saw NAFTA as a unique opportunity: working with their counterparts in the United States to shape the treaty’s terms could enable them to dramatically increase their hitherto limited leverage over Mexican environmental policy.

The participation of environmental groups in the anti-fast-track coalition helped legitimate congressional opposition to the extension of presidential fast-track negotiating authority, since “opposing fast-track on environmental grounds was easier than arguing the concerns of labor with the attendant risk of being accused of being in the pocket of ‘special interests.’”23 The environmental issue quickly became a focal point for legislators opposed to trade liberalization. Thus House Majority leader Richard Gephardt (D-Mo.), long a prominent opponent of liberal trade policies, stated in a public letter to President Bush that his willingness to support NAFTA depended not only on the treaty being rewritten to protect American jobs, but also on the inclusion of strict environmental safeguards. He argued that “neither

Mexico nor Canada nor America is benefited by a system that beignly looks upon massive air pollution, poisonous pesticides and child labor as ‘comparative advantages.’24 Evoking the “circle of poison” argument, Gephardt stated that American farmers “cannot and should not have to compete against farmers who use pesticides that fail to meet U.S. standards.”

As the debate over NAFTA heated up in the spring of 1991, both the Mexican and American governments began to recognize that the environmental critique of NAFTA threatened the trade agreement’s approval in the U.S. Congress. To demonstrate his commitment to environmental protection to the United States, President Salinas dramatically closed Mexico City’s largest oil refinery, a major source of air pollution. On the American front, two months later, the USTR agreed to appoint five representatives from environmental organizations to its top-level NAFTA advisory committees, and the White House pledged to conduct parallel negotiations to develop a border environmental plan with Mexico.

Following these preliminary concessions on the part of the Bush administration, the Natural Resources Defense Council and the National Wildlife Federation agreed to support an extension of fast-track authorization. While most environmental organizations and consumer groups continued to oppose fast track, the President had succeeded in splitting the environmental movement. The support of the NRDC and the NWF played a critical role in securing congressional approval of the administration’s request for an extension of fast-track negotiating authority for both GATT and NAFTA. However, the administration’s victory was a close one: fast track passed the House by only thirty-nine votes.

Two months after fast track passed the U.S. Congress, the United States and Mexico released a draft plan committing both countries to cooperate to improve environmental quality along their common border.25 EPA administrator William Reilly stated that the plan was intended to “reassure those who have concern about the consequences of free trade.”26 It called for additional investment in waste water treatment plants, increased restriction on cross-border shipments of hazardous wastes, and the hiring of more officials to enforce environmental laws in Mexico. The following month, USTR Carla Hills assured environmentalists that NAFTA would not be rushed through until proper safeguards were in place. She promised
that the United States was "not going to bend environmental and safety commitments," adding that "we've no intention of letting pesticides come in from Mexico as we wouldn't from Italy or France."

In January 1991 both governments announced an integrated plan to clean up the American-Mexican border. The plan committed approximately one billion dollars over three years—about two-thirds of which would come from Mexico—to build water treatment plants, better roads, and solid waste disposal sites along the border. The plan represented the first large-scale attempt to integrate the environmental strategies of the two governments, and it clearly acknowledged the linkages between natural resources and trade. It included funds to construct a 200 million dollar plant to end the water pollution from Tijuana that had closed San Diego beaches, as well as a 19 million dollar sewage treatment facility in Nuevo Laredo, Mexico. In addition, the World Bank approved loans of $0 million dollars to improve environmental enforcement and 200 million dollars to reduce air pollution in Mexico City. To address the latter problem, Mexico enacted legislation requiring that all new vehicles be equipped with catalytic converters.

To emphasize its own commitment to environmental regulation, and at the same time diffuse environmental opposition to the trade agreement, the Mexican government began a crack-down on polluters, doubling the number of its inspectors along the border and temporarily closing hundreds of maquiladoras for failing to comply with Mexican environmental regulations. It also passed legislation requiring all new industries to submit environmental impact reports. Sergio Reyes Lujan, under-secretary of ecology in Mexico, promised that Mexico would not become a haven for polluters. He stated, "There should be no doubt that any factory rejected by the United States will not be acceptable in Mexico."

Mexican officials argued that NAFTA would help improve the quality of Mexico's environment, both by making Mexico richer and by removing the incentive for firms to locate along the border rather than in the less crowded interior.

By early 1992 environmental objections to NAFTA were shaping the national debate. David Orrman of the Friends of the Earth expressed his astonishment at the number of members of Congress who supported the demands of the environmental movement that the trade agreement and environmental regulation be explicitly linked.

gressman Bill Richardson (D-N.Mex.), a supporter of free trade, called the environment a "wild card" issue, noting that forty members of the House had voted in favor of fast track with the understanding that the treaty would explicitly address environmental issues. He predicted that "what will decide the free trade agreement will not be the commercial side . . . but the environmental issue."

Bush administration officials continued to insist that a free trade pact would improve Mexico's environment; EPA head William Reilly argued that NAFTA would provide Mexico with "the money to reduce pollution, apply new technologies, support government programs and pay for inspectors, regulators and prosecutors.

While acknowledging that the gap between Mexican and American environmental standards was a legitimate cause for concern, Reilly cautioned environmentalists against holding the trade agreement hostage to force changes in Mexican environmental law—and in doing so play into protectionist arguments and risk the possible defeat of the agreement.

NAFTA was officially signed by the heads of state of all three nations shortly after the 1992 U.S. presidential election. However, upon assuming office, President Clinton declined to submit the trade agreement to Congress. Instead, the administration began to negotiate a number of changes in the agreement, including the addition of a supplementary environmental agreement. The changes were announced in the summer of 1993, when the administration submitted the treaty along with the side agreement to Congress.

The Terms of the Agreement

The specific regulatory provisions of NAFTA go significantly beyond the FTA in three important respects. First, NAFTA makes a more ambitious effort to reduce the role of regulations as trade barriers. Second, NAFTA explicitly attempts to prevent trade liberalization from undermining domestic regulatory standards. Finally, the dispute settlement mechanisms established by NAFTA's side agreement on the environment permit the use of both fines and trade sanctions to en-
force its provisions. In brief, NAFTA seeks to prevent its signatory nations from using regulations to gain a comparative advantage either by making them too strict or too lax.

The agreement prohibits any country from lowering its environmental standards to attract investment and does not prevent its parties from imposing stringent environmental standards on new investments, provided they apply equally to foreign and domestic investors. It also requires all three countries to cooperate on improving the level of environmental protection, and it encourages, but does not require, the upward harmonization of regulatory standards.

As the direct response to the concerns of environmentalists over the implications of the GATT decision in the tuna-dolphin case, the agreement specifically states that the provisions of several international environmental agreements—including the Montreal Protocol, the Basel Convention on hazardous wastes, and CITES—take precedence over NAFTA. In some cases, it also allows each nation to continue to enforce “generally agreed international environmental or conservation rules or standards,” provided they are “the least trade-restrictive necessary for securing the protection required.” While this latter clause essentially echoed the “proportionality” doctrine of the European Court of Justice, it leaves open to question whether trade restrictions can be used to enforce the way a product is made or caught in another country if there is no international environmental treaty—precisely the issue that lay at the core of the tuna-dolphin dispute between the United States and Mexico.

NAFTA also attempts to limit the ability of its signatories to use national standards for protectionist purposes. A Committee on Standards-Related Measures will attempt to develop common criteria for assessing the environmental hazards of products as well as methodologies for risk assessment, while a Committee on S&P Measures will seek to harmonize these standards “to the greatest extent practicable” and to minimize their negative trade effects. This latter provision represented an attempt to address a longstanding series of disputes between Mexico and the United States over their respective uses of S&P standards to restrict trade in agricultural products.

For example, in 1989 Mexico had required that U.S. swine be vaccinated for hog cholera thirty days before export—even though U.S. hogs had been free of this disease for more than a decade. For its part, the United States required that Persian limes grown in Mexico under a chlorine-based treatment before export in order to eliminate citrus canker, which Mexican growers claim has been eradicated. The United States has also restricted imports of avocados from Mexico, claiming they contain worms, even though worms have not been found in this fruit in Mexico for nearly fifty years. Thus, like the European Union and the World Trade Organization, NAFTA is intended to contribute to reducing the use of regulatory standards that are little more than disguised trade barriers.

At the same time, because the United States was able to exercise more influence over the provisions of NAFTA than over the final terms of the Uruguay Round GATT agreement, the former’s treatment of sanitary and phytosanitary standards is more explicit about each country’s right to establish or maintain its own standards of protection. While the GATT states that in choosing its level of protection a nation should attempt to minimize negative trade effects, NAFTA permits each nation to determine its own regulatory standards, subject only to the constraint that they have a scientific basis. Thus, unlike the GATT, NAFTA does not subject S&P standards to the least-trade-restrictive test. Nor does NAFTA permit a dispute settlement panel to substitute its scientific judgment for that of a national government.

Equally important, NAFTA permits each nation to maintain its existing federal and subfederal environmental standards. Products that do not meet these standards can be banned, provided that the country’s standards are nondiscriminatory and are scientifically based. New standards can be challenged on the grounds that they are discriminatory in their design or application. If one party questions another’s standards, the burden of proof is on the complaining country to show that a regulatory measure was inconsistent with the agreement—in contrast to the GATT, which places the burden of proof on the country which enacted the regulation.

The agreement’s most innovative feature is its Supplemental Agreement on the Environment, though this agreement is not part of NAFTA itself. It was negotiated by the Clinton administration with considerable input from U.S. environmental organizations. The Supplemental Agreement establishes a Commission on Environmental Cooperation, headed by a Secretariat and Council composed of the senior environmental officials from each country, and advised by representatives of environmental organizations. Addressing some of the criticisms of GATT dispute procedures made by environmental
groups following the tuna-dolphin decision, it extends to citizens the right to make submissions to the commission on any environmental issue, requires the Secretariat to report its response to these submissions, and permits, under certain circumstances, its reports to be made public. In fact, the agreement provides more opportunities for non-business participation than current U.S. trade law, which only permits aggrieved producers to file complaints with or sue the International Trade Commission, the body responsible for enforcing American trade laws.

In addition, the Commission was given the authority to consider the environmental implications of both processes and production methods or, in its words, the “environmental implications of products throughout their lifecycles.” While the side agreement does not require any of the three signatories to enact new environmental laws, it does authorize the use of fines as well as trade sanctions if existing laws are not enforced, though only fines can be applied against Canada. Although the Commission is empowered to address any environmental or natural resource issue, the range of issues subject to dispute settlement panels is limited to the enforcement of those environmental laws which are related to trade or competition among the parties. However, as the discussion of EU environmental policies in Chapter 3 reveals, the potential range of regulatory policies that fall within this definition is extremely large; it certainly includes production standards for traded goods. NAFTA thus subjects more national regulatory policies to international scrutiny than any other trade agreement negotiated by the United States.

NAFTA and the FTA

An important reason why environmental issues played a prominent role in the debate over the terms and approval of both the FTA in Canada and NAFTA in the United States is to do with geographic proximity. Because of their common borders, both nations had long been directly affected by the environmental policies of their southern neighbors: the air and water pollution generated by the factories located on Mexico’s northern border had created serious pollution problems for the southwest region of the United States, while the pollution generated by American midwestern coal burning utilities had contributed to Canada’s acid rain problem. Both sources of cross-

border pollution had been the subject of long-standing international negotiations, but no satisfactory solution had been reached by the time the negotiations over trade agreements had begun. Moreover, the existence of long borders had made the monitoring of cross-border trade difficult.

Yet the differences between the debate over the FTA in Canada and the NAFTA in the United States were equally striking. What is distinctive about NAFTA is the extent to which environmentalists in the United States were able to affect the terms of public debate, as well as the content of the agreement itself. Their impact stands in marked contrast to the minimal influence of Canadian environmental groups with respect to the FTA. What accounts for this difference?

One factor has to do with the relative strength of American nongovernmental organizations vis-à-vis national policy-makers. The U.S. environmental movement is better organized than its Canadian counterpart and, because of the structure of the American political system, enjoys greater access to the policy process at the national level. Moreover, there has generally been much more public concern about environmental issues and more public support for effective environmental regulation in the United States than in Canada.

A second factor has to do with the enormous gap between the levels of economic and political development between Mexico and the United States on the one hand and Canada and the United States on the other. While the GNP of the United States is significantly larger than that of Canada, the per capita income of the two countries is roughly similar. Moreover, the United States and Canada have comparable political systems: they are stable democracies, with independent judiciaries and competent public administration.

Mexico, on the other hand, is a newly industrializing country. The gap in per capita income between the United States and Mexico is substantial; while Mexico’s population is more than one-third the size of the United States, its GNP is only about 4 percent as large. Not only are its environmental problems an order of magnitude greater than those of both the United States and Canada, but Mexico does not possess sufficient political or administrative resources to address them adequately, at least in the short run. Indeed, many of the most important differences between Mexican and American environmental policies have to have less to do with regulatory standards—many of which are comparable—than with their enforcement. Never has a free trade
agreement been attempted between nations with such different political systems and economic resources. It is in part for this reason that while the cross-border environmental disputes between Canada and the United States were not resolved until after the FTA was signed, those between Mexico and the United States became a integral part of the negotiations surrounding the approval of NAFTA in the United States.

A third factor had to do with the GATT ruling in the tuna-dolphin case. This ruling was made in August 1991, just two months after Congress had renewed the Bush administration’s request for fast-track negotiating authority. While the GATT ruling had nothing to do with NAFTA per se, it significantly increased public awareness in the United States both of the potential conflict between trade agreements and domestic environmental regulations and of the magnitude of the gap between Mexican and American environmental standards. Significantly, the tuna-dolphin case figured prominently in the anti-NAFTA literature produced by consumer and environmental groups.

The Politics of Ratification

The debate over NAFTA sharply divided the environmental community, as it did the business community. A number of organizations, including Friends of the Earth, Public Citizen, and the Sierra Club, strongly opposed NAFTA. They viewed the agreement as both too weak and too powerful: they feared that the environmental side agreement would be ineffective in making Mexico enforce its environmental laws, and that at the same time the agreement itself would be highly effective in making the United States lower its regulatory standards.

But just as significant, six major national environmental organizations, including the Natural Resources Defense Council, the Audubon Society, the Environmental Defense Fund, and the World Wildlife Federation, endorsed the agreement. They concluded that the provisions of the supplementary environmental agreement, on which they had insisted and which they helped the Clinton administration negotiate, offered adequate regulatory safeguards, though they were disappointed that it did not include any specific procedure for raising environmental standards or their enforcement to the highest common denominator.26

The opposition of some environmental and consumer groups to the agreement was not able to prevent its narrow approval by the United States Congress in November 1993. Moreover, as the vote approached, their concerns were overshadowed by the debate over the agreement’s perceived impact on the U.S. economy: it was the trade-union movement, not environmental and consumer groups, that ultimately constituted the most important and influential component of the anti-NAFTA coalition.

Nevertheless, NAFTA marked a new level of environmentalist participation in the making of American trade policies. Previous debates over trade agreements negotiated by the United States had been dominated by interest groups whose primary concern was their economic impact. Now, for the first time, the regulatory dimensions of a trade agreement were politically salient, and environmental groups became active participants in the making of American trade policy.27

Moreover, American NGOs did have a major impact on the terms of the agreement and specifically on the inclusion of an environmental side agreement.28 Unlike labor unions, a number of environmental organizations were willing to support free trade with Mexico in exchange for specific provisions in the side agreement. This in part explains why the powers granted to the Commission on Environmental Cooperation far exceed those granted to its counterpart on labor standards. Literally hundreds of meetings took place between executives of large environmental groups and administration officials. And the support of environmentalists was, in turn, critical to the agreement’s congressional passage. As a result of the input and influence of American environmental organizations, NAFTA is a far greener trade agreement than either the FTA or the GATT: not only does it make more of an effort to reduce the use of regulations as trade barriers, but it seeks both to maintain existing regulatory standards and to strengthen regulatory enforcement.

In addition, the debate in the United States over the environmental implications of NAFTA itself led to substantial changes in the enforcement of Mexican environmental policies. For example, the Mexican government, which rarely inspected its industrial plants prior to the debate over NAFTA, conducted more than 11,000 such inspections in 1992 and 1993, resulting in the partial or full closure of several hundred facilities, including seven in Mexico City. It also established the office of environmental attorney-general to prosecute both domestic
and foreign industries. The budget of the Mexican Secretariat of Social Development (SEDESOL), the agency responsible for formulating and implementing Mexican development policy, increased from 4.3 million dollars in 1988 to 88.4 million dollars in 1992. Moreover, annual government spending on environmental protection grew tenfold between 1988 and 1991. Mexico also significantly tightened its automobile emission standards, bringing them into closer alignment with those of the United States. And Mexico's willingness to change the practices of its fishing fleet so as to further reduce dolphin mortality after its victory in the GATT against the United States was a direct response to the NAFTA negotiations.

In a sense, what the debate over the environmental impact of NAFTA accomplished was to make Mexico's access to the American market contingent on improvements in Mexican environmental quality. Thanks to the influence of American environmental organizations, the United States not only pressured Mexico into strengthening the enforcement of its current environmental regulations, but increased its long-term influence over Mexican environmental policies. By agreeing to the supplementary environmental agreement, Mexico has subjected its environmental policies to continuous scrutiny from American producers and American environmental groups. Moreover, because the U.S. market is so much larger, trade liberalization is likely to promote the adoption of American product standards, just as they are being increasingly adopted by Canadian producers as a result of the FTA.

Indeed, this has already begun; in order to promote automotive exports to the United States, Mexico has matched American automotive fuel economy standards; and in 1993, in anticipation of NAFTA's approval, Mexican trucking firms began to order new diesel engines from the United States which meet the emission requirements of the 1990 Clean Air Act Amendments. Thanks to both these pressures from American environmentalists as well as their own interest in having identical standards throughout North America, U.S. multinationals are likely to require their Mexican subsidiaries to adhere to produce standards similar to those of the United States, once again illustrating the market dimensions of the California effect.

NAFTA remains essentially a trade agreement. The United States, Canada, and Mexico have not created a common market, let alone a North American equivalent of the European Union. Nevertheless, thanks to the provisions of the environmental side agreement and the much larger size of its domestic market, NAFTA has provided the United States with the potential to play a role in strengthening Mexican regulatory policies analogous to Germany's role in strengthening European regulatory standards. On one hand, the institutions created by NAFTA are far weaker than those of the European Union, thus giving the United States much less legal leverage over Mexico than Germany has been able to exercise over its southern neighbors. But on the other hand, the relative size of the U.S. market within North America is far greater than that of Germany's within the EU, thus giving the United States considerably more economic leverage. Accordingly, "The environmental parallel accord for NAFTA is the beginning, not the end, of negotiations on natural resources issues in North America." It is worth recalling that it took the EC more than fifteen years to begin to have a significant impact on the environmental policies of the Community's less green and poorer member states. NAFTA's impact on Mexican environmental regulation is likely to look considerably different fifteen years from now.

There is another even more important parallel between NAFTA and the EU. Like the EU, NAFTA is likely to expand its number of signatories. Chile has already expressed interest in joining, as have a number of other Latin American nations. And just as the EU has insisted that future member states adopt its regulatory standards, so is the United States likely to insist that any nation joining NAFTA agree to a Supplementary Agreement on the Environment similar to that negotiated with Mexico. Thus, just as the expansion of the EU to central Europe will help strengthen those nations' regulatory standards, so will the expansion of NAFTA southward become an important vehicle for the upward harmonization of third world regulatory standards within the Americas. Though overshadowed by the controversy surrounding the greening of the GATT, in the long run both regional trade agreements are likely to play a much more important role in promoting the export of stricter regulatory standards.
The California Effect

The tensions between protective regulation and free trade could, in theory, lead to one of two opposite and exclusive outcomes: either free trade will triumph at the expense of protective regulation, or the opposite will occur. According to the first scenario, trade liberalization will steadily undermine national regulatory standards. Finding that the costs of compliance with the strict standards demanded by their citizens have made their products uncompetitive on global markets, and no longer able to protect their industries by tariffs, national governments will be forced to progressively weaken their consumer and environmental regulations. Their competitors would then respond by lowering their standards still further, thus producing a downward spiral of regulatory standards. Likewise, the increasingly powerful international institutions established by trade agreements and treaties will become progressively more vigilant in their scrutiny of protective regulations that “interfere” with trade, thus inhibiting many nations from enforcing regulatory standards stricter than those of their trading partners. Consequently, the influence of consumer and environmental organizations over regulatory policies would decline.

Alternatively, precisely the opposite outcome may occur. Nations may enact an increasing number of regulatory standards that disadvantage imports, including making access to their domestic markets contingent upon other nations adopting production standards similar to their own. According to this scenario, dispute settlement mechanisms would become toothless in the face of these ecoprotectionist challenges to trade liberalization. Correspondingly, protectionist pro-

ducers and their environmental and consumer allies would increase their political influence over both trade and regulatory policies. A number of the developments described in this book are consistent with each of these scenarios. In some cases, increased international scrutiny of domestic regulatory policies has expanded, while in others international institutions have proven unable or unwilling to exert effective discipline over national regulatory standards that restrict trade. The decisions of the GATT dispute panels in the tuna-dolphin case, the GATT’s success in preventing restrictions on imports of hardwoods from South Asia, and the European Union’s Luxembourg, food additive, and packaging directives illustrate the role of trade agreements in weakening some national regulations. Alternatively, Ontario’s beer can tax, Denmark’s recycling laws, the paper recycling regulations of American states, and the EU’s hormone ban demonstrate the growing importance of protective regulations as nontariff barriers. Not only are there important conflicts between trade and regulatory policies, but their number and significance is likely to increase as regional and international efforts to promote economic integration clash with the continued disparity of national consumer and environmental regulations. The constantly changing and continually expanding regulatory agenda poses a never-ending challenge to trade liberalization. But at the same time, these cases belie a broader and rather counter-intuitive pattern—a third theoretical outcome of the conflict between trade and regulatory policies. True, the steady growth of regulation has interfered with trade, while trade agreements are increasingly interfering with regulation. But what is more significant is that, on balance, both global and regional economic integration has increased while consumer and environmental standards have become stronger. Given the reasonable expectation that the strengthening of one should result in the weakening of the other, what has made this non-zero-sum outcome possible?

The Impact of Regulation on Trade

Local, national, and, in the case of the EU, regional environmental and consumer regulations do continue to represent important obstacles to trade. Doubtless in the absence of the substantial expansion of health, safety, and environmental regulation over the last three de-
success in reducing nontariff barriers to trade in food and food processing. This effort has been strongly supported by Europe’s export-oriented food producers, processors, and distributors, all of whom hoped to benefit from the removal of national regulatory barriers to trade in animals, plants, food, and beverages. The same dynamic accounts for the decision to restrict the use of sanitary and phytosanitary measures as nontariff trade barriers in the Uruguay Round GATT agreement. The initial pressure for incorporating an agreement on S&Ps standards into the GATT came from American grain processors, among the world’s most important agricultural exporters. But their initiative was supported by a number of other nations, whose food producers and processors also wanted enhanced access to one another’s markets, including that of the United States. Likewise, the restrictions on the use of food processing standards as nontariff barriers in the North American Free Trade Agreement reflected the interests of both Mexican and American agricultural exporters.

Moreover, the limited success of NGOs in the United States, acting either alone or in cooperation with producers, on restricting American exports of various “hazardous” products was largely due to the greater political influence of American exporters. Thus it was the opposition of the American chemical industry which prevented congressional passage of the “circle of poison” legislation. And the influence of export-oriented American manufacturing and service firms helped defeat proposals to “tax” imports of manufactured products produced according to laxer environmental standards.

The interests of particular firms or the structure of particular economic sectors is not, however, sufficient to explain the extent to which the use of national regulations as trade barriers has been constrained. For example, the decision of the European Court of Justice in Cassis de Dijon can hardly be attributed to the political or economic influence of the French liqueur industry, let alone the German alcoholic beverage importer whose complaint initiated the case. Moreover Cassis preceded the Single European Act, which did have substantial business support. And while export-oriented European firms undoubtably played a critical role in the passage of the SEA, their influence does not adequately explain the EU’s subsequent progress in reducing nontariff barriers for so many products in so many sectors.

The second explanation for the compatibility between trade expan-
sion and protective regulation has to do with the structure and authority of international institutions. Thus the success of the EU's 1992 program owes much to the fact that the Union created a set of institutions, in which norms, legal principles, and decision-making rules have significantly facilitated both the harmonization of national regulatory standards and the reduction of national protective regulations that restrict trade. In particular, the European Court of Justice has emerged as a powerful institution, comparable in many respects to the Supreme Court of the United States. Its articulation of the principle of mutual recognition, and its application of this principle to strike down numerous national product regulations, have made an immeasurable contribution to European economic integration. Likewise, the EU's decision to establish a system of weighted voting for directives affecting the single market has played a critical role in facilitating the adoption of Union-wide regulatory standards.

Moreover, the EU's 1992 program helped change the outlook of both large and small firms throughout Europe. By encouraging them to think about markets in regional rather than national terms it affected the way they defined their interests. Instead of focusing on the maintenance of domestic regulations and standards that restricted imports, they began to increasingly challenge the regulations of other member states which limited their exports. The result was to create a degree of business support that did not exist before for the idea of the single market and the removal of trade barriers.

The GATT is a much weaker institution than the EU. Nonetheless, it too has played a role in limiting the use of regulations as trade barriers. Significantly, no GATT signatory has yet imposed a tax on imported products which are produced according to laxer environmental standards, in spite of substantial domestic political support for such a measure from protectionist producers and environmentalists in a number of countries, including the United States. Governments have resisted such a tax—and domestic pressures for it—because it would undermine the logic of liberalized global trade and threaten the broad range of benefits provided by open markets.

The response of the international community to the decision of the tuna-dolphin dispute panel provides another indication of the importance of institutional rules. Although this panel's ruling was widely criticized on both environmental and legal grounds, and not officially adopted by the GATT Council, it nonetheless has affected a number of national policies. Even the United States, which chose to ignore the panel's ruling with respect to Mexican tuna imports, has since hesitated to impose additional trade restrictions which would be inconsistent with the panel ruling. Moreover, when the EU subsequently issued its own directive to reduce dolphin deaths caused by tuna fishing methods, in deference to the ruling of the GATT dispute panel, it did not extend its scope to non-EU-owned fishing vessels. Likewise, it was the European Commission's unwillingness to be subject to GATT dispute settlement proceedings that led it to resist the pressures of the European Parliament to impose restrictions on imports of wood from tropical forests. Austria also withdrew its labeling requirement for imports of tropical wood because of pressure from the GATT. And the United States carefully structured its ban on exports of unprocessed logs to make it GATT-consistent.

The FTA has had less impact on removing regulatory barriers to trade between the United States and Canada in part because these barriers were less significant to begin with. However, NAFTA is likely to play a much more important role in reducing regulations that restrict trade, in large measure because of the relative importance of existing regulatory trade barriers between Mexico and the United States.

The third reason why the increase in regulation has not been more disruptive of trade has to do with the increasing importance of international environmental treaties and agreements. These accords establish minimum, relatively uniform regulatory standards for both products and processes, thus enabling nations to cooperate in addressing common environmental problems while preventing free-ridding. They now encompass a wide range of regulatory policies formerly under the control of national governments, including trade in endangered species of both plants and animals, hazardous waste, fishing methods and fisheries management, the production of CFCs, sulphur emissions (acid rain), and the pollution of international waters. While their enforcement is uneven, they have established rules which have significantly contributed to reducing trade conflicts stemming from divergent domestic environmental standards and cross-national environmental spillovers. Although these treaties and agreements are most important at the international level, they have also played a role in the coordination of environmental standards and their enforcement in North America.
The California Effect

Finally, it is important to note that freer trade does not require that nations adopt uniform production standards, since differences in national production costs are an important reason why trade occurs in the first place. Nor does it require that nations adopt identical product standards for traded goods. They can, for example, also agree to recognize one another’s standards, consider them to be equivalent, or accept one another’s tests. Rather, the compatibility of trade and regulation primarily requires that national regulatory standards for traded products be designed in such a way as to minimize the obstacles they impose on imports.

The Impact of Trade on Regulation
What has been the impact of trade liberalization and agreements to promote it on national regulatory standards? Has the reduction in both tariff and nontariff barriers undermined national efforts to protect consumers and improve the environment?

International trade as a proportion of GNP has significantly increased in every industrial nation since the late 1960s. Yet during this same period, environmental and consumer regulations have become progressively stricter. All industrial nations and a number of industrializing ones now devote substantially more resources both in absolute and relative terms to environmental and consumer protection than they did in 1970.

Compatibility
Since the early 1970s few major economies have experienced a greater increase in their exposure to international competition than that of the United States; between 1970 and 1980 both its imports and exports as a share of GNP more than doubled. And yet American regulatory standards have become substantially stronger during the last quarter-century. The proportion of American GNP devoted to pollution control stood at 1.5 percent in 1972; it has been higher every year since, averaging more than 1.7 percent between 1980 and 1986 and increasing to 2.2 percent in 1992. Annual expenditures on compliance with federal environmental regulations totaled $90 billion in 1990 and increased by approximately $30 billion following passage of the 1990 Clean Air Act Amendments.

Similarly, across the Atlantic the Single European Act’s goal of creating a single European market was in large measure motivated by the interests of European business managers and political leaders in strengthening the ability of European industry to compete successfully in the global economy. Yet this same amendment to the Treaty of Rome also authorized and has contributed to a significant strengthening of EU environmental and consumer regulations. Likewise, since the early 1970s Japan has both emerged as a major international exporter and has significantly increased its environmental expenditures.

The compatibility between increased exposure to the global economy and the strengthening of domestic regulatory efforts is also borne out by the experience of Mexico, a developing nation. Since 1986 Mexico has significantly opened up its economy to foreign competition, while between 1988 and 1991 government spending on environmental protection increased ten-fold. The approval of NAFTA will serve to re-enforce both, especially to the extent that Mexico’s per capita GNP moves above the level at which the World Bank estimates that national per capita emission levels begin to decline due to an increase in resources devoted to pollution control.

The United States itself provides the clearest example of the compatibility of strict regulatory standards and extensive economic interdependence. As a union of member states, the United States itself is a highly integrated market whose Constitution permits few restrictions on interstate commerce, especially for traded goods. While many regulatory standards are set by the federal government, a number of federal regulatory statutes only set minimum standards. For example, states are permitted to enact stricter controls on automobile emissions than those required for the nation as a whole. States also are free to impose tougher standards on stationary sources of pollution and restrictions on land use. Furthermore, recycling requirements are set by state and local governments.

While states do compete with one another to attract investment, they have generally not chosen to do so by lowering their standards for environmental or consumer protection. On the contrary, many state standards are stricter than federal ones. A number of states have enacted more stringent controls over the use of pesticides, beef hormones, and PCBs than the federal government. Several state and local governments have also established ambitious recycling programs,
bases on the use of specific materials in packaging, and strict standards for solid waste disposal and incineration. A number of states also have established their own, stricter air pollution control standards; those imposed on both individuals and businesses by the Southern California Air Quality Management District are among the strictest in the world.

Nor is the United States unique. Subnational governments in other federal systems, including Canada and Australia, have enacted consumer and environmental regulations stricter than those required by their central governments. Indeed, it was precisely the increasing propensity of local governments to establish their own tougher regulatory standards that led the drafters of the GATT agreement on sanitary and phytosanitary standards to include a provision holding central governments responsible for the regulatory standards of subnational political units.

The Costs of Compliance

To be sure, some national regulatory standards have been lowered or delayed as a result of international competitive pressures. For example, in the United States the automobile emission standards of the 1977 Clean Air Amendments were modified by Congress as a response to the American automobile industry's competitive difficulties, while in the early 1980s automobile safety requirements were delayed for similar reasons. And in 1993, the German government agreed to modify its recycling requirements following complaints from German firms that some of these requirements were placing them at a competitive disadvantage. There is also growing concern in Europe that some Union environmental standards have reduced the international competitiveness of European firms and that this may well temper the EU's willingness to impose new regulations on industry. Indeed, California is also finding itself under pressure to modify some of its environmental standards in order to retain and attract investment.

There are undoubtedly trade-offs between international competitiveness and domestic expenditures on protective regulations. Global competition does constrain domestic regulatory policies as it constrains both national fiscal and monetary policies. But these constraints have left governments with substantial discretion to enact regulations stricter than those of their trading partners. Thus, in spite of several cases of trade regulation conflict, over the long run economic interdependence has been positively associated with the strengthening of regulatory standards.

Why hasn't increased regional and international competition led regions, nations, or subnational governments to compete with one another by enacting less stringent consumer and environmental regulations? In other words, why don't national health, safety, and environmental regulations exhibit the "Delaware effect?" In light of recent trends in labor markets, it seems puzzling that regulatory policies have not followed the same pattern as wages—which have been adversely affected by increased international competition in most industrial nations. To take one important example, why have real wages, fringe benefits, and employment security for American automobile workers declined, in part due to increased international competition, while over the same time period automotive safety, emission, and fuel economy standards have been progressively strengthened?

One important reason is that for all but a handful of industries, the costs of compliance with stricter regulatory standards have not been sufficient to force relatively affluent nations, or subnational governments, to choose between competitiveness and consumer or environmental protection. For in marked contrast to labor costs, the costs of compliance with protective regulations have been modest. According to Martin Houélin, the environmental director at the consulting firm KPMG Peat Marwick in London, "The international differences in the cost of labor are generally so much more important that the environment pales into insignificance." This is not to say they are nonexistent: many expenditures to improve environmental quality do reduce output and lower the rate of productivity growth. But in the aggregate, increases in national levels of pollution control expenditures have had little effect on the growth of economic output. Nor have American states with stronger environmental policies experienced inferior rates of economic growth and development.

While production standards obviously can and do affect corporate plant location decisions, for all but a handful of industries the effects are not significant. Within the United States, differences in environmental standards have not been a major factor in plant siting or expansion decisions. Studies of international corporate location decisions reach similar conclusions: only a relatively few heavily polluting industries have shifted their production from the United States largely
because pollution control expenses are generally not large enough a share of total costs to make relocation economical. Environmental control costs comprise less than 2 percent of total production cost for most U.S. industries, even though American standards are relatively stringent.

Likewise, expenditures on environmental compliance have not had a significant impact on the trade performance of most American industries. Significantly, Japan, with which the United States has its largest trade deficit, has relatively strict environmental regulations. The OECD reports that "very little evidence exists of firms being transferred abroad in order to escape the more stringent environmental regulations at home." In fact, "multinational companies are increasingly adopting the same environmental standards for their plants, regardless of the country in which they operate." Accordingly, Stewart concludes, "There is no reason to suppose that international competition for comparative advantage will lead nations to adopt inappropriately low environmental standards."

Finally, just as industrial production often imposes public costs, so do protective regulations produce public benefits. Thus expenditures on air pollution may increase agricultural output while improvements in water quality may result in better fishing yields or increased tourism. Equally important, improvements in environmental quality and product safety can improve the health, and thus the productivity, of a nation's workforce and thus reduce national health-care expenditures. They can also create opportunities for export markets for pollution control equipment. In short, while the economic benefits of regulations are difficult to measure, and have often been exaggerated, they are far from inconsequential.

This does not mean that nations are free to impose whatever environmental regulations they wish on firms engaged in international competition. For while stricter environmental standards may not make a nation poorer, neither do they make it richer; greater wealth leads to a preference for strong regulatory standards, not the reverse. But the fact that laxer regulatory standards are not, for all but a handful of industries, an important source of competitive disadvantage, only helps explain why the reduction of tariffs and other trade barriers has not resulted in a Delaware effect, that is, movement toward lower regulatory standards. It does not explain why or how trade liberalization and agreements to promote it has contributed to raising them; that is, it does not explain the "California effect."

The California Effect

The Delaware effect does apply to some public policies, but the evidence suggests that protective regulations have not usually been among them. On the contrary, a number of national consumer and environmental regulations exhibit the California effect: they have moved in the direction of political jurisdictions with stricter regulatory standards.

The California effect can be seen literally in the history of American automobile emission standards. The 1970 Clean Air Act Amendments specifically permitted California the option of enacting stricter emissions standards than those required for the rest of the United States, an option which California chose. Consequently its standards remained stricter than those of any other state. In 1990, Congress brought national emission standards up to California's and once again permitted California to impose stricter standards. It also gave other states the option of choosing either national or California standards. In 1994 twelve eastern states requested that the federal government permit them to adopt California's new standards. These standards in turn are likely to become the basis for the next round of minimum federal requirements. California has now had America's strictest automotive pollution control standards for more than three decades. Thus, instead of states with laxer standards undermining those with stricter ones, in the case of automobile emissions precisely the opposite has occurred: California has helped make American mobile emissions standards steadily stronger.

The term "California effect" is meant to connote a much broader phenomenon than the impact of American federalism on federal and state regulatory standards. The general pattern suggested by this term, namely, the ratcheting upward of regulatory standards in competing political jurisdictions, applies to many national regulations as well. This pattern has three components: two relate to market forces, and the third has to do with politics. First, to the extent that stricter regulations represent a source of competitive advantage for domestic firms, the latter may be more likely to support them. Second, rich na-
tions which have enacted greener product standards force foreign producers to adjust to them in order to continue to enjoy market access, thus helping in turn to raise foreign product standards. Third, agreements to reduce trade barriers can provide richer and more powerful greener nations with the opportunity to pressure other nations into adopting stricter product and production standards.

The Interests of Domestic Producers

How can international competition turn industrial opponents of tougher standards into self-interested promoters of them? First, knowing or anticipating that the burdens of compliance will fall disproportionately on their international competitors may well make domestic producers more willing to support stricter regulations than they would have in the absence of foreign competition. For example, the beer bottlers of both Denmark and Ontario would probably not have supported stricter recycling requirements had not these regulations also served to help protect their domestic markets. Similarly, the success of European consumer groups in persuading the EU to completely ban the use of growth hormones in beef production was facilitated by the support the ban received from Europe’s small, relatively inefficient but politically powerful cattle farmers. Likewise, Germany’s willingness to support stricter domestic and EU standards for automobile emissions and packaging stemmed in part from the extent to which these standards benefited domestic producers. And the Thai government would not have imposed such severe restrictions on cigarette marketing in the absence of competition from American cigarette companies.

From this perspective, more liberal trade policies, rather than pressuring nations to lower their regulatory standards, may actually provide nations with an economic incentive for strengthening them. By contrast, since relatively closed economies can rely on tariffs and quotas to restrict imports, they have less need to adopt protective regulations that advantage domestic producers. In some cases, these regulations may amount to little more than disguised forms of protectionism. Nor do stricter standards necessarily improve consumer or environmental protection. Nonetheless, the self-interest of producers can play a role in strengthening regulatory standards for a number of internationally traded products. In short, Baptist-bootlegger coalitions can serve to advance the legitimate interests of both Baptists and bootleggers.21

The Lure of Green Markets

The second way in which international trade can drive national regulatory standards upward has to do with market access. The argument that trade promotes the strengthening of environmental standards has primarily rested on the impact of trade on promoting domestic economic growth, hence increasing both the demand for regulation and the ability to pay for it. The evidence demonstrates that another important factor enabling greener countries to promote the export of stricter standards to less green countries has to do with the size and importance of the former’s domestic markets.

Political jurisdictions which have developed stricter product standards force foreign producers in nations with weaker domestic standards either to design products that meet those standards or sacrifice export markets. This, in turn, encourages those producers to make the investments required to produce these new products as efficiently as possible. But having made these initial investments, they now have a stake in encouraging their home markets to strengthen its standards as well, since their exports are already meeting those standards.22 Thus, the willingness of Germany’s automobile manufacturers to support stricter EU standards was in part due to their previous experience in producing vehicles for the American market. It was precisely the firms supplying the largest, wealthiest automobile market in Europe who took the lead in pressuring the EU to adopt the product standards already set by the world’s largest, richest market, the United States. They made common cause with German environmentalists to demand the adoption of “US 83” standards by the EU. Significantly, half of German automobile sales in the United States are in California, the political jurisdiction with the world’s strictest automotive emission standards.

Indeed, German producers stood to benefit from the EU’s adoption of American standards, since they could then produce similar vehicles for both markets at lower cost. Likewise, the subsequent willingness of the French and Italian manufacturers to support the stricter standards of the Small Car Directive stemmed in part from the experience
they had gained in producing cars for export to greener markets in Europe and the United States as well as their fear of losing additional export markets to their greener competitors. Significantly, the one European country whose bottlers welcomed Germany's strict packaging law was Denmark, whose producers enjoyed a competitive advantage in recycling their own products due to Denmark's previously enacted recycling legislation.

The pull of greener markets has also served to drive regulatory standards upward in North America. The expansion of trade between the United States and Canada following the Free Trade Agreement prompted Canada in 1993 to establish automobile emission requirements similar to those imposed on vehicles sold in America three years earlier. As barriers to imports of Mexican products to the United States gradually decline as a result of NAFTA, Mexican producers will be forced to redesign their products to meet American regulatory standards. And those producers who do so will then have an interest in pressuring the adoption of similar standards by Mexico, since this will provide them with a competitive advantage over their more domestically oriented competitors. At the same time, American exporters to Mexico may also become a source of political support for making Mexican regulatory standards more similar to those of the United States, since that will enable them to design similar products for both markets.

The pattern of chemical regulation also illustrates the role of international trade and competition in strengthening regulatory standards. It was the enactment of the Toxic Substances Control Act by the United States that prompted the European Union to enact the Sixth Directive. The EU feared that unless its standards were comparable to those of the United States, it would be deprived of access to one of the world's largest chemical markets. As a result, it established a much stricter system for the introduction and marketing of chemical products. Once again, stricter American standards drove those of its major trading partner upward.

In the area of conservation, both the United States and the EU have repeatedly used restrictions, or the threat of restrictions, on access to their large domestic markets to force their trading partners to upgrade their regulatory standards. It was the economic pressure of the EU which forced Canada to end its killing of baby seals and which persuaded both the United States and Canada to end the use of leg-traps to catch fur-bearing animals. Likewise, the large size of its domestic market has provided the United States with the leverage to influence the fishing practices of several of its trading partners, thus helping to protect a variety of species, including whales, turtles, and dolphins.

The impact of both these effects of trade liberalization is limited. Specifically, trade liberalization is most likely to encourage a nation to raise its domestic regulatory standards when doing so provides domestic producers with a competitive advantage. This is often the case, but not always. Likewise, the impact of greener markets on promoting the export of stricter standards primarily applies to product standards. While this encompasses virtually all consumer protection regulations as well as those environmental regulations which apply to products, it excludes those environmental standards that seek to address the harms caused by how products are produced. And the latter are extremely significant: thus there are a number of environmental problems in less developed nations, ranging from deforestation to hazardous levels of urban air pollution, which will not be improved by global market forces. This is, however, another mechanism by which trade liberalization can raise standards, one capable of affecting a much broader range of domestic regulatory policies. This has to do with the terms of trade agreements and treaties.

The Politics of Integration

To the extent that treaties or trade agreements provide formal mechanisms for establishing harmonized or equivalent standards, they provide an opportunity for richer, more powerful countries to play a greater role in setting those standards. If the five trade treaties and agreements discussed in detail in this book were ranked in terms of the extent to which their signatories have agreed to reduce the use of regulation as trade barriers, the most powerful would be the Single European Act, followed by the Treaty of Rome, the North American Free Trade Agreement, the Free Trade Agreement, and the various rounds of the General Agreement on Tariffs and Trade. If these same five treaties and agreements were to be ranked in terms of the extent to which they contain provisions designed to either maintain or strengthen the regulatory standards of their signatories or members, the rankings
would be identical. Paradoxically, the more authority nations concede over the making of national regulatory standards, the more likely these standards will be strengthened.

The reason for this relationship is not that international agreements to promote trade liberalization automatically strengthen regulatory standards; in principle, they can just as easily weaken them. It is politics that makes the difference. Specifically, trade agreements and treaties are likely to maintain or raise regulatory standards when a powerful and wealthy nation insists that they do so. In turn, the powerful nation’s willingness to demand that trade liberalization be accompanied by the maintenance or strengthening of health, safety, and environmental standards is in large measure due to the influence of its domestic NGOs and, in many cases, its domestic producers as well. But the ability of a powerful nation to impose its preferences on its trading partners is also dependent on the degree of integration: the more integration, the greater its influence.

Thus, the most important factor driving EU environmental standards steadily, if unevenly, upward has been the power and preferences of Germany, the member state with the largest economy and Europe’s most powerful environmental movement. By strengthening the power of the Union over the regulatory policies of its member states, the SEA has in turn increased the leverage of Germany, along with the Netherlands and Denmark, over the environmental policies of the rest of the Union. The SEA could have attempted to promote integration at the expense of stricter consumer and environmental standards. That it did not do so was a reflection of the political and economic power of those member states which warned both policy objectives to be achieved simultaneously.

Similarly, NAFTA is a much greener trade agreement than the FTA for one simple reason: the United States insisted upon a Supplementary Agreement which extends international supervision over the enforcement of Mexican domestic production standards as well as over the content of a wide range of product standards. It did so primarily because powerful domestic environmental constituencies, whose support the Clinton administration needed to persuade Congress to support NAFTA, demanded it. But the United States in turn was able to insist upon this condition because it was wealthier and more powerful than Mexico. The impact of NAFTA on Mexican regulatory policies and preferences will continue to be strongly influenced by the United

States, the North American nation with both the largest economy and the most influential environmental pressure groups. However, because the international institutions established by NAFTA are weaker than those of the EU, the United States will have less influence over Mexican regulatory policies than Germany, Denmark, and the Netherlands have had over those of Italy or Greece. But at the same time, NAFTA gives the United States more leverage over Mexican regulatory policies than it had under the GATT.

The frustration of environmentalists with the GATT stems in large measure from the extent to which GATT rules limit the ability of nations in which green pressure groups are especially influential to use trade policies to change the environmental policies of their trading partners. Accordingly, “greening the GATT” essentially means expanding the legal basis on which the United States, but also the EU and a number of other countries, can use their economic power to influence the regulatory policies of countries with a weaker commitment to environmental protection. This, however, has not yet occurred, in part due to a lack of consensus regarding the appropriateness of such a shift by the international community in general and the EU, the United States, and Japan in particular. Accordingly, the scope of the California effect remains weakest at the global level. But at the same time, compared with both NAFTA and the EU, the GATT also has much less authority to weaken national regulatory standards.

International agreements and treaties to reduce the role of regulatory standards as trade barriers have constrained the ability of green countries to establish and enforce regulatory standards as strict as their NGOs and some domestic producers have preferred. But what is striking is how infrequently this has occurred and how little it has adversely affected consumer or environmental quality. With the partial exception of British Columbia’s fish landing requirements, the Free Trade Agreement between the United States and Canada has not required either nation to weaken its regulatory policies. In the case of every other FTA trade dispute—including the American restriction on sales of lobsters below a certain size, American states’ recycling requirements, Puerto Rico’s milk processing standards, the American asbestos ban, and Ontario’s tax on beer cans—the nation with the stronger regulation was allowed to maintain it, notwithstanding its impact on trade. If anything, the FTA has probably been too differential to Canadian and American regulatory policies: surely the United
States could have been required to devise a less trade-restrictive way of protecting its small, sexually immature lobsters from unethical American lobstermen than restricting the sales of all small lobsters.

In the case of the GATT, dispute panels have issued decisions in only seven cases involving the use of regulations as non-tariff trade barriers. In two cases, the dispute over America’s Superfund tax and American CAFE standards, the stricter national regulation was found to be GATT-consistent. In the case of the five other disputes that came before dispute settlement panels, national rules were successfully challenged. But two of these essentially involved commercial disputes between Canadian and American fishermen with few environmental consequences. In the case of the complaint brought by the United States against Thailand’s restriction on sales of American cigarettes, the dispute panel found the import ban to be inconsistent with the GATT, but it upheld Thailand’s much more important marketing restrictions on all cigarettes.

This leaves the two cases involving American restrictions on imports of tuna, both of which were decided against the United States, along with a variety of other more informal efforts on the part of the GATT to discourage import restrictions based on production standards. But the GATT’s constraints have as much to do with the unilateral nature of these restrictions as with their extraterritorial scope. As the unanimous support of GATT signatories for Mexico in its dispute with the United States reveals, the GATT places a high value on multilateralism. In practice, it is highly unlikely that the newly established World Trade Organization would uphold a complaint against an environmentally related trade restriction that was strongly supported by both the United States and the European Union, let alone one taken pursuant to an international environmental treaty. Moreover, trade restrictions represent only one mechanism that countries can employ to influence the regulatory policies of other nations. They are much less effective than international environmental agreements, especially when the latter include subsidies.

The international institution that has played the most important role in challenging national environmental and consumer regulations has been the European Union. EU directives have frequently prevented the Union’s greener member states—most notably Germany, the Netherlands, and Denmark—from enacting stricter regulations for traded products on the grounds that these threaten the single market.

But these ceilings have been more than counter-balanced by the Union’s role in progressively strengthening the regulatory standards of the EU’s other member states. Moreover, in some cases, most notably the beef hormone ban and the small car directive, the EU’s interest in preserving the single market has led it to adopt the regulations of the member state with the strictest standards. Thus, on balance the EU has strengthened both environmental and consumer standards within western Europe. Equally important, the EU’s regulatory directives cover all consumer and environmental standards which directly affect the health, safety, or environment of its member states and their citizens.

Any assessment of the impact of trade agreements and treaties on national regulatory standards must distinguish between regulations that actually protect the public and those which are actually disguised forms of protectionism. Virtually all of the protective consumer regulations that have actually been eliminated or modified as a result of national obligations under an international agreement or treaty fall into the latter category. This is true of the literally thousands of food labeling and composition standards of the member states of the EU, as well as Japanese S&CP standards that have been modified as a result of pressures from its trading partners. Subjecting these regulations to international scrutiny has made consumers better, not worse, off. In these cases, the benefits of trade liberalization have paralleled those of domestic economic deregulation.

It is true that as the authority of international institutions over national regulatory standards increases, so does the possibility that legitimate national regulatory policies will be undermined. Moreover, the distinction between consumer and environmental protection and consumer and environmental protectionism is not always obvious: it is not always possible to sharply distinguish between the California and Delaware effects. Thus, both NAFTA and the WTO’s Agreement on Sanitary and Phyto-sanitary Standards could result in weakening some regulations that arguably do enhance consumer protection. But if the experience of the EU is any guide, on balance they are much more likely to improve public welfare by forcing the elimination or modification of the large number of national regulations which mainly benefit producers. And if the experience of the FTA is any indication, highly visible national regulations that are strongly supported by NGOs often manage to escape international review.
Indeed, it is more likely that regulations which are barely disguised forms of protectionism will be maintained than it is that regulations which provide clear public benefits will be weakened.

Finally, it is important not to equate the California effect with regulatory convergence. The ratcheting upward of regulatory standards is a dynamic process. As the standards of regulatory laggards are strengthened, so are the standards of the regulatory leaders likely to change as well. The regulatory agenda of green countries is highly unstable: new issues, and new regulations, keep emerging. As a result, the California effect may not reduce the disparity among national regulatory standards; indeed, it may even increase them. What it does do is ratchet national regulatory standards upward.

Regulation and Political Power

The argument that rich, powerful countries can strengthen the regulatory standards of their trading partners through both economic and political mechanisms is premised on the association between national wealth and power, and national preferences for stricter environmental and consumer regulations. The California effect requires both that political jurisdictions with stronger regulatory standards be rich and powerful, and that nonstate actors in rich and powerful political jurisdictions prefer stronger regulatory standards. Accordingly, it is unlikely that Delaware would have been able to insist on its own stricter automobile emission standards, let alone serve as a model for the rest of the United States. California’s impact on both American and European regulatory standards is a function of the size of its “domestic” market.

Thus, had Portugal been the EU’s greenest member state and Germany been indifferent to stronger regulatory standards, the impact of the EU on European environmental standards would have been rather different; they might well have been driven downward. A similar outcome might be expected to occur in North America if Mexican environmental pressure groups were relatively strong and those in the United States relatively weak. Likewise, relatively few of their trading partners would care if India or Finland, rather than the United States or the EU, had made access to their domestic market contingent on improvements in the international or domestic conservation practices of their trading partners. Likewise, if support of Germany and the United States for stronger regulatory standards were to diminish, their trading partners would find themselves under less pressure to raise their regulatory standards.

Nor is there anything automatic about the commitment of richer countries to improve the regulatory standards of their trading partners. The former’s policy preferences are dependent on the preferences of domestic constituencies. For example, it is unlikely that an Asian common market or free trade zone dominated by Japan, a rich nation with a weak environmental movement, would exhibit the same pattern of regulatory policy-making that has occurred in Europe or is beginning to occur in North America. While Japan does have extremely strict domestic product standards which its trading partners have to meet, it has not played a leadership role in seeking to address global environmental issues. Nor has it attempted to use its considerable economic and political leverage to link Asian economic integration to the strengthening of environmental standards in other Asian nations. Indeed, it is Japan itself which has been subject to pressures from its trading partners, most notably the United States, to improve its environmental practices, especially in the area of wildlife protection. Moreover, while Japan has relatively strict product standards, their international impact is limited by the fact that Japan imports relatively few manufactured goods from its less green trading partners in Asia.

The future regulatory impact of an organization such as the Asia-Pacific Economic Cooperation group will primarily depend on whether Japan chooses to use its political and economic influence to improve the environmental practices of its trading partners. And this in turn will depend in part on the preferences and political influence of Japanese environmental organizations, which to date have been both less influential and less interested in environmental problems outside their nation’s borders than their counterparts in the United States and the EU. By the same token, were China to replace the United States as the world’s largest economy and its regulatory policies to remain unchanged, the dynamics of global regulatory policy-making would be altered significantly. In sum, the impact of increased integration on regulatory standards depends on the policy objectives of powerful nations, which are largely determined domestically.

To date, increased economic integration has, on balance, contributed to strengthening national regulatory policies, especially for
traded goods and—in the case of the EU and, to a lesser extent, NAFTA—for domestic production standards as well. Whether or not it continues to do so depends on the preferences of the world’s richest and most powerful nation states. The increased integration of regional and global markets in a “borderless world” has not led to a decline in the importance of national power. On the contrary, the globalization and regionalization of regulatory policy-making has extended the influence of both producers and nongovernmental organizations in rich and powerful countries over the regulatory policies of nations with whom they trade and with which their economies have become integrated. In the final analysis, the impact of trade and trade agreements on regulatory standards is determined by the interaction of domestic and international politics.

Notes


3. For comprehensive bibliographies, see Bibliography of Trade and Environment Literature (Paris: OECD, 1993), and Esty, Greening, pp. 281–306.