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What Would a Better NAFTA Look Like?

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The North American Free Trade Agreement (NAFTA), which lays out rules for how companies in Mexico, Canada, and the United States cross borders to do business, has become something of a punching bag. As a candidate, Donald Trump called it a “disaster.” So did Bob King, the former president of the United Auto Workers. “For countless Americans, this agreement has failed,” Robert Lighthizer, the U.S. Trade Representative, said in a statement Wednesday morning, as he joined representatives from Canada and Mexico to renegotiate the trade deal. Among the complaints: NAFTA made it easier for companies to outsource jobs to Mexico, which led to lower wages for the American workers competing for the work that was left.

Not everyone agrees that NAFTA was bad for U.S. workers—some studies suggestthat manufacturing employment would have declined anyway, and that NAFTA and other trade deals helped U.S. companies become more profitable, which in turn helped U.S. workers. Still, negotiators from the three member countries are tasked with improving the deal. And they may not be able to do much in that regard as they meet to hash out a new version of the trade agreement, which they hope to reach an agreement on by the beginning of 2018. That’s in part because failure—at least from the point of view of American workers—is baked into the format of modern trade agreements. Trade agreements are no longer just about reducing quotas or tariffs on products imported by member countries. Instead, modern trade agreements are, as Dani Rodrik, a Harvard economist, argues in a forthcoming book, “designed largely with the needs of capital in mind,” meaning that they protect investors and companies and their interests overseas, and do little to ensure that workers and consumers are getting a fair deal.

Rather than just govern the tariffs on goods traded between countries, trade agreements today do much more. They protect intellectual property rights and limit product safety standards, and they establish legal protections for firms that locate abroad. In short, they make it easier for companies to sell goods overseas, Rodrik says. To the extent that American workers will benefit, the thinking goes, they will benefit when businesses’ success with exports trickles down. Trade agreements do little explicitly to improve working conditions, or wages, or workers’ bargaining power within countries. In reality, the effect is often the opposite: “NAFTA’s current rules allow companies to compete based on who can exploit workers or the environment more,” Susan Helper, the former chief economist of the U.S. Department of Commerce under the Obama administration, said, in a Congressional hearing about modernizing NAFTA in July.

Throughout the agreements, it is firms that are the main actors. For example, under today’s trade agreements, firms can challenge government policies that affect their investments under so-called “investor-state dispute settlement” (ISDS) mechanisms. Through these mechanisms, companies have won lawsuits against countries over environmental cleanup and criminal prosecutions, according to Helper, who is also an economics professor at Case Western Reserve University. But no such dispute resolution exists for worker groups or, for that matter, environmental-advocacy organizations. The only remedy for labor groups that think workers are being treated unfairly is to file a complaint with a national administration office, but Helper says these complaints lead to employers getting chastised by government offices, not any sort of requirement that labor practices change.

Even these complaints are rarely filed, according to James J. Brudney, a labor and employment law professor at Fordham University. Labor's grievances can, under NAFTA, lead to arbitration, but the process of getting to that stage is so difficult that only one labor complaint has reached arbitration in the history of trade deals in the Americas, and labor groups lost because they did not prove the poor labor conditions had affected trade. The number of labor complaints filed declined significantly after 1998, when labor groups realized that NAFTA's structure was not effective for responding to complaints, Brudney said.

This imbalance is part of the reason why some scholars including Rodrik and Helper suggest that NAFTA renegotiations focus more on workers. For example, Todd Tucker, a fellow at the left-leaning Roosevelt Institute, has proposed that countries agree to let labor take disputes to independent arbitrators, in a similar procedure to the ISDS mechanisms. "You have to have this as an explicit objective, at least of co-equal importance, to simply reducing the cost of doing business and investing across borders," Rodrik told me. "Ultimately you want to give workers and other segments a much greater voice in the way their economy is managed."

It's not just labor that should have more say in trade agreements, argues Tucker. Right now, for all their import, trade agreements are largely negotiated behind closed doors, and in the U.S., states and other local entities are not involved. Canada, by contrast, allows provincial governments to sign off on segments of trade deals that affect them specifically, Tucker said. When the European Union negotiates trade agreements, each national government gets veto power, and specific regions have veto power over their country's sign-off. Many progressive groups say trade negotiations in the U.S. should be more transparent, because state and local groups would benefit from knowing exactly what is being negotiated. "In an ideal world, this process would move in tandem with a domestic conversation," Rodrik told me. The AFL-CIO's trade and globalization policy specialist, Celeste Drake, has suggested sharing individual provisions and text with the public and with Congress.

Looping in more parties like this could also help inspire their support, as well as lead to ways of compensating those who will be left worse off by a deal. If certain states or domestic groups oppose a trade provision because it will hurt their constituents, negotiators would have more pressure on them to add a remedy to gain their support. Those remedies would ideally be more robust than the current programs, such as the federal government's Trade Adjustment Assistance initiative, that are supposed to be helping the people displaced by trade today.

Of course, there may be significant downsides to giving labor and other groups more power in trade agreements. Such concessions could make it more expensive for companies to do business in countries such as Mexico, which would in turn make them less competitive, argues Dan

Ikenson, the director of trade policy studies at the right-leaning Cato Institute. If companies can't compete with Asian and European businesses, they will "start to atrophy and die," Ikenson told me. And that will lead to lead to the loss of more, rather than fewer, U.S. jobs. In fact, Ikenson has found, in his research, that companies that outsource work to low-cost countries also add domestic jobs when they do so. In short, Ikenson argues, it's not the responsibility of trade agreements to create jobs. Instead, the U.S. should figure out how to retrain and reemploy people who can't compete with workers overseas, rather than trying to protect their jobs.

Still, conservatives like Ikenson and liberals like Helper agree that there are some parts of NAFTA that are too investor-friendly. They recommend reforming or eliminating the special courts for investors—the aforementioned ISDS mechanisms. Such mechanisms make it easier for firms to leave the United States, Helper argues, since they know they'll have to deal with an international arbitrator, rather than less-lenient foreign governments, when disputes arise.

NAFTA could also do more in regulating how companies pay their taxes. As Gabriel Zucman, an economist at the University of California Berkeley haswritten, multinational companies are able to avoid paying $200 billion in taxes each year by using tax havens and other accounting techniques. Tucker suggests that as a condition for joining new trade agreements, countries should be required to adopt "formulary apportionment systems," under which companies are taxed based on where their products are sold, rather than the jurisdiction where their profits are recorded. The financial institutions that refuse, especially those in tax havens, could be blocked from doing business, he suggests.

Of course, most of these objectives are far afield from the objectives of the current administration. The U.S. Trade Representative has already said that the administration will not make public any parts of the negotiations until they're finalized, for example. And governments are often hesitant to give up sovereignty on enforcing laws in domains such as labor because doing so overrules laws that have been created democratically.

These objectives would probably be difficult to achieve in a Democratic administration as well. Companies have long been allied with the government during trade processes, and unwinding that relationship would be difficult, if not impossible. According to Tucker, from the 1950s to the 1990s, only agricultural interests and manufacturing groups pushed for bigger trade deals with other countries. This wasn't enough support to overcome opposition to trade deals, so various administrations began to add rules that benefited certain industry groups to gain their support. President Nixon added industry trade advisory committees, which are groups of corporate representatives who get special access to the trade negotiator. This is how trade negotiations became about more than tariffs and quotas in the first place.

This all means that today's U.S. Trade Representative faces a huge obstacle in coming up with a trade agreement that will generate widespread support nationally, something that will undermine a president who ran on making trade a better deal for American workers. As the election of Trump showed, large groups of constituents across the country are upset with NAFTA and with trade in general. To make them happy, the best solution may to give workers' groups and local and state governments more of a voice. But doing so may alienate business interests, which were essential in getting these trade deals passed in the first place. Without large changes in how it's structured, NAFTA will likely remain a punching bag in much of the country. With changes, it could still remain one—it would just be different groups doing the punching.