

What's Next for NAFTA?

Department of Defense

Removal of the last transitional trade restrictions established by the North American Free Trade Agreement (NAFTA) presents a new challenge to the agreement's signatories—Canada, Mexico, and the United States. Because the architects of NAFTA deliberately avoided creating strong supranational institutions that could have deepened the economic relationship fostered by the agreement, the member countries will have to exercise their national autonomy, either individually or in concert, in order to take additional actions that advance regional economic integration. Actions that would build upon NAFTA are sometimes referred to as “NAFTA Plus.”

One possible approach to NAFTA Plus, analyzed by ERS and Canadian researchers, is for the member countries to move in the direction of a customs union, a free-trade area with a common set of external tariffs. A customs union would eliminate the possibility that differences in external tariffs would distort decisionmaking by the private sector. However, reaching consensus on these tariffs may be difficult. Each member country has preferential trade agreements other than

NAFTA, and there are some substantial differences in the most-favored-nation (MFN) tariffs applied by individual NAFTA countries. In conformance with the World Trade Organization, a country must apply its MFN tariffs to all trading partners that have MFN status with that country. Important exceptions to this rule include preferential trade agreements and special access for developing countries.

Common external tariffs would enable the NAFTA countries to eliminate the agreement's rules of origin. In a preferential trade agreement, rules of origin determine whether a product originated from the area covered by the agreement and thus qualifies for its preferential tariff, which in NAFTA's case is usually duty-free status. NAFTA's rules of origin are not a major impediment to regional agricultural trade since most of the goods traded are produced using inputs originating from the NAFTA countries. Nevertheless, compliance with these rules imposes an administrative cost on firms participating in NAFTA trade. Those firms must complete NAFTA Certificates of Origin and ensure that they seek preferential tariff treatment only for qualified products.

Since 2003, the NAFTA Working Group on Rules of Origin has crafted multiple incremental changes to the agreement's rules of origin that have been implemented by the NAFTA governments. A handful of these changes directly apply to agriculture. For instance, one provision allows the regional content of certain cranberry juice mixtures to be determined on the basis of transaction value or net cost, rather than volume. Whether these steps eventually lead to a North American customs union remains to be seen, however, since they do not involve the establishment of common external tariffs. \forall

Steven Zahniser, zahniser@ers.usda.gov
Karl Meilke, University of Guelph
James Rude, University of Alberta

This finding is drawn from . . .

“Is NAFTA Plus an Option in the North American Agrifood Sector?” by Karl D. Meilke, James Rude, and Steven Zahniser, in *The World Economy* 31(7):925-46, July 2008.

Some differences in the most favored nation tariffs of the NAFTA countries are quite large

| Product | Canada | United States | Mexico |
|--|----------------|----------------|--------|
| | <i>Percent</i> | | |
| Chickens, uncut (fresh or chilled) | 238.0* | 3.5 | 234.0 |
| Butter | 298.5* | 35.3* | 20.0 |
| Cheddar cheese | 245.5* | 24.0* | 125.0 |
| Durum wheat | 0.4** | 1.3 | 67.0 |
| Barley | 0.4** | 0.4 | 115.0 |
| Potatoes | 1.0 | 1.8 | 245.0 |
| Raspberries | Free | Less than 0.05 | 20.0 |
| Raw sugar (cane or beet, solid form, not containing added flavoring or coloring) | 9.3 | 91.5* | 73.5 |
| Strawberry jam | 12.5 | 2.2 | 51.0 |
| Peanuts (shelled) | Free | 131.8* | Free |

* = Over-quota tariff ** = In-quota tariff. Some tariffs were converted to ad valorem equivalents using unit import values and other trade data, as compiled by Global Trade Information Services, Inc.

Source: USDA, Economic Research Service, using 2008 data from Canada Border Services Agency, Mexico Secretariat of Economy, and U.S. International Trade Commission.