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TRADE

NAFTA nations: U.S. flouts rules

Mexico and Canada say the United States violates the terms of the North American Free Trade Agreement. The debate threatens to fray the trade pact and damage diplomatic relations.

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Bloomberg News

Canada and Mexico are escalating their allegations that the United States is flouting the terms of the North American Free Trade Agreement in order to protect domestic producers.

Canadians are dropping what Prime Minister Paul Martin called "the safe language of diplomacy" and spurning new negotiations on a dispute involving U.S. export limits on Canadian softwood lumber. Mexico is publicly supporting the Canadians in the lumber case as it pursues its own grievance over a long-running sugar trade dispute.

The spats threaten to fray NAFTA, the landmark 1994 accord that set up the world's largest trading bloc, and damage diplomatic relations with two of the United States' closest allies.

"We've got two really big cases with huge political ramifications" for the United States, said Gary Hufbauer, a fellow at the Institute for International Economics in Washington. "What's needed now is some kind of political settlement."

Much of the U.S. policy on these issues has been dictated by domestic industries fearful of competition from cheaper foreign goods, Hufbauer said. President Bush needs to intervene with domestic industry and "knock some heads," said Hufbauer, author of the forthcoming book *NAFTA Revisited*.

The grievances surfaced at a Sept. 30 trade summit in Vancouver between Mexican President Vicente Fox and Martin and boiled over in an Oct. 6 speech by Martin, who said the integrity of NAFTA is being compromised.

"Where rules are established and agreed upon, they should be followed," Martin told the Economic Club in New York.

Martin says the United States is avoiding complying with rulings that require it to drop duties on \$7.6 billion a year in lumber from Canada and return more than \$4 billion in levies collected. Canada tried to negotiate a solution to the lumber dispute two years ago; it is now ruling out any further talks.

"If this was poker, we won the pot, and now the U.S. wants to negotiate with us over how to divide it," Frank McKenna, Canada's ambassador to the U.S., said. "The time for negotiation has passed."

ALTERNATIVE MARKETS

Five days after Martin's speech, Canadian Revenue Minister John McCallum traveled to Beijing on a mission to find alternative export markets for Canadian oil and lumber. Canada, which ships 80 percent of its exports to the United States, now wants new trade partners and may increase tariffs on American products to force the United States to give in on the lumber dispute, McKenna said.

"We do have leverage, and we'll use it," he said.

Mexico has expressed similar frustration, saying it won't accede to a World Trade Organization ruling this month against its tax on high-fructose corn syrup until the United States agrees to drop restrictions on

Mexican sugar. Mexico has been trying to submit a dispute over sugar trade to NAFTA since before Bush took office, but has been unable to get the United States to agree to terms for the case to be heard.

Martin and Fox say the United States is effectively ignoring NAFTA rules that the United States itself demanded a decade ago, when it insisted on an independent tribunal to enforce the agreement. The United States counters that it has a different legal interpretation of the tribunal's rulings.

"The U.S. strongly disagrees with the allegation that we flout NAFTA," said Neena Moorjani, a spokeswoman for the U.S. Trade Representative's office. "While we have differing views with the Canadians with respect to the legal effects of these decisions, those differences are being litigated."

Working to the benefit of the United States is its importance as the world's biggest economy. The United States buys more than 90 percent of the oil that Mexico and Canada export and is a top market for products such as Mexican clothing and Canadian wheat and auto parts.

"There is only one way to retaliate, and that involves shooting yourself in the foot," said Michael Hart, a professor of trade policy at Carleton University in Ottawa, who helped Canada negotiate its free-trade agreement with the United States.

SIGNS OF BENDING

The U.S. may be starting to show some signs of bending: After a NAFTA panel ruled against the tariffs the United States imposed on Canadian wheat, an independent U.S. trade panel decided that the U.S. industry isn't hurt by those imports, clearing the way for the duties to be lifted.

The United States imposed tariffs on softwood lumber from Canada in 2002 after American producers complained that Canadian provinces give their companies below-market access to government forests. In August, a NAFTA panel ruled that the duties violate U.S. laws.

The United States argued that the ruling didn't apply because it was superseded by a new determination from the U.S. International Trade Commission. The duties would stay in place, and no money returned, the U. S. announced.

Mexico has been trying to negotiate a solution to the sugar dispute since 1998, when it first called for an independent trade panel. Sugar growers in the United States say giving Mexican growers unfettered access to the U.S. market could destroy their price-support system and put them out of business.