A State-Level View of NAFTA: Economic Implications and Policy Options

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This Article examines the economic implications of the North American Free Trade Agreement (NAFTA) and its recent renegotiation from the perspective of individual U.S. states. Individual states have very few options in the arena of international commerce, despite the fact that trade agreements like NAFTA make some states better off while simultaneously making others worse off. This Article provides a framework to understand how NAFTA redistributes wealth among U.S. states, as well as what options are available to states seeking to capitalize on new opportunities or mitigate harms from changes in trade policy. States face legal constraints from the Commerce and Supremacy Clauses of the U.S. Constitution, as well as international law – specifically, the World Trade Organization (WTO). There is also very little evidence to support the efficacy of those policies clearly within the legal rights of state and local governments. Instead, states may need to rely on their representatives in Congress to more forcefully represent their interests in international trade negotiations. These points are made salient by the recent renegotiation of NAFTA to produce the United States-Mexico-Canada Agreement (USMCA).

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I. INTRODUCTION

The Trump Administration has just recently concluded talks to renegotiate the North American Free Trade Agreement (NAFTA) with Canada and Mexico. As of this writing, the agreement still needs to be ratified by the governments of the member countries, but it is all but certain that the new agreement, called the United States-Mexico-Canada Agreement (USMCA), will come into force.[1] NAFTA has been the subject of contentious political debate at least since the 1992 presidential campaign, when Ross Perot coined the term "giant sucking sound" to describe the relocation of manufacturing from the United States to Mexico.[2] The renegotiation objectives released by the office of the U.S. Trade Representative (USTR) reflect similar concerns, and aligned with the rhetoric Trump employed on the campaign trail and after assuming office.[3] The President has expressed a great deal of skepticism about the value of deeper global integration, and his "America First" slogan seems to signal a greater willingness to raise barriers to trade, or at least demand greater concessions from trade partners in terms of opening to U.S. exports. Recent experience with steel and aluminum tariffs shows that Trump is willing to take an aggressive stance to pursue what he sees as U.S. national interests in trade negotiations.[4]

The focus on a single national interest ignores the fact that, while the trade agreements are negotiated at the federal level, the consequences will be felt at the level of states and counties. Some states and counties will be made better off by NAFTA or similar trade agreements, while others will be made worse off. At the same time, the Constitution and existing trade agreements constrain the ability of state and lower governments to engage in international commerce, including offering support for local industries that may be adversely affected by changes in trade policy. This Article will offer some insight into the disparate impacts NAFTA has had across different U.S. states. Additionally, this Article will review the legal constraints faced by state and local governments as they search for policies to manage the state-level consequences of USMCA and future trade negotiations.

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[1] *See* Jen Kirby, *USMCA, the New Trade Deal Between the US, Canada, and Mexico, Explained*, VOX (Oct. 2, 2018), https://www.vox.com/2018/10/2/17923638/usmca-trump-nafta-trade-agreement [https://perma.cc/S9TQ-VPP4].

[2] *See* Gary Hufbauer, *Ross Perot Was Wrong About NAFTA*, N.Y. TIMES (Nov. 25, 2013), https://www.nytimes.com/roomfordebate/2013/11/24/what-weve-learned-from-nafta/ross-perot-was-wrong-about-nafta [on file with *Ohio State Law Journal*].

[3] *See generally* U.S. TRADE REPRESENTATIVE, SUMMARY OF OBJECTIVES FOR THE NAFTA RENEGOTIATION (2017), https://ustr.gov/sites/default/files/files/Press/Releases/NAFTAObjectives.pdf [https://perma.cc/SZ2T-6S5R] [hereinafter USTR] (outlining specific objectives for the NAFTA renegotiation process).

[4] *See* Kevin Breuninger, *Canada Announces Retaliatory Tariffs on Steel and Aluminum*, CNBC (May 31, 2018), https://www.cnbc.com/2018/05/31/canada-announces-retaliatory-tariffs.html [https://perma.cc/LNQ5-72DM].

II. AN OVERVIEW OF THE OBJECTIVES AND RESULTS OF THE NAFTA RENEGOTIATION

Renegotiating NAFTA was a signature promise of President Trump's campaign.[5] It fit with his broader theme of skepticism toward free trade, as was also demonstrated by his withdrawal of the United States from the Trans Pacific Partnership (TPP).[6] President Trump was vague about his NAFTA renegotiation objectives while on the campaign trail, beyond promising he would promote the interests of American workers and firms.[7] He also stated several times that he was willing to withdraw the U.S. from NAFTA if he is not happy with the results of the negotiation.[8] Canada[9] and Mexico[10] made similar threats.

On July 17, the U.S. Trade Representative released a summary of their objectives for renegotiating NAFTA.[11] The document lists twenty-two major areas the USTR would focus on during the negotiations, ranging from intellectual property protections to labor and environmental standards.[12] Critics of the USMCA point out that the new agreement falls short of achieving the Administration's loftier objectives, and represents only a minor update of the existing agreement.[13] Some of the Administration's objectives were achieved. U.S. dairy farmers will have greater access to the Canadian market, and new rules were negotiated governing trade in digital goods.[14] The Administration was also successful in updating the "rules of origin" for auto manufacturing, which determine how much of the value of an automobile must be added within

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[5] Megan Cassella, *Trump Launches NAFTA Renegotiation*, POLITICO (May 18, 2017), http://www.politico.com/story/2017/05/18/trump-adminstration-formally-kicks-off-renegotiation-of-nafta-238552 [https://perma.cc/DLD4-3EWM].

[6] C. Fred Bergsten & Monica de Bolle, *Overview*, *in* A PATH FORWARD FOR NAFTA, PETERSON INST. FOR INT'L ECON. 5 (C. Fred Bergsten & Monica de Bolle eds., July 2017), https://piie.com/system/files/documents/piieb17-2.pdf [https://perma.cc/3B7V-KY2J].

[7] *See Presidential Candidate Donald Trump Rally in Grand Rapids, Michigan*, C-SPAN (Nov. 7, 2016), https://www.c-span.org/video/?418209-1/donald-trump-makes-final-campaign-stop-grand-rapids-michigan&start=1343 [https://perma.cc/6VUD-94ZD].

[8] *See If Trump Pulls Trigger on NAFTA Withdrawal, Mexico Will Walk Away*, CNBC (Aug. 30, 2017), https://www.cnbc.com/2017/08/30/if-trump-pulls-trigger-on-nafta-withdrawal-mexico-will-walk-away.html [https://perma.cc/VD9Y-65HS].

[9] *See* David Ljunggren & Andrea Hopkins, *Canada Suggests It Could Quit NAFTA Talks over Dispute Mechanism*, REUTERS (Aug. 14, 2017), https://www.reuters.com/article/us-usa-trade-nafta-canada/canada-suggests-it-could-quit-nafta-talks-over-dispute-mechanism-idUSKCN1AU1CK [https://perma.cc/959Y-QSPD].

[10] *See* Elisabeth Malkin, *Facing Trump, Mexicans Think the Unthinkable: Leaving NAFTA*, N.Y. TIMES (Jan. 24, 2017), https://www.nytimes.com/2017/01/24/world/americas/trump-mexico-nafta.html [on file with *Ohio State Law Journal*].

[11] USTR, *supra* note 3, at 4.

[12] *Id.* at 4–17.

[13] *See* John Brinkley, *USMCA Is Not the Magnificent Trade Deal Trump Says It Is*, FORBES (Oct. 8, 2018), https://www.forbes.com/sites/johnbrinkley/2018/10/08/usmca-is-not-the-magnificent-trade-deal-trump-says-it-is/ [https://perma.cc/4HE2-ZHCN].

[14] *See* Kirby, *supra* note 1.

member states to qualify for zero tariffs.[15] The new rules require that 75% of components be manufactured within USMCA member states in order to qualify, compared to 62.5% under NAFTA.[16]

The U.S. also achieved some of its objectives related to so-called "deep integration," or the harmonization of domestic regulations.[17] The emphasis on "deep integration" is somewhat surprising, since these were important elements of the TPP,[18] which President Trump has abandoned.[19] In the USMCA, the Administration successfully negotiated stronger protections for certain kinds of intellectual property.[20] There is another important provision related to labor standards in the auto industry. To qualify for zero tariffs under USMCA, at least 40% of the value of an automobile must be added using workers who earn at least $16 per hour.[21] This provision would come into force by 2023.[22] Critics argue that this new "minimum wage" standard, along with stricter rules of origin, may actually reduce employment in the U.S. auto sector by driving up costs.[23] Rather than abide by the new USMCA rules to qualify for zero percent tariffs, it may be cheaper to move production out of North America and import autos under the U.S. most-favored nation (MFN) tariff of 2.5%.[24]

The U.S. was unable to achieve several key objectives that would have given the President more flexibility to raise trade barriers to protect domestic industries.[25] Specifically, the USTR was unable to eliminate NAFTA's Chapter 19 dispute settlement mechanism and the global safeguard exclusion.[26] In the past, these provisions have prevented the U.S. from raising barriers to shield domestic industries from competition with Canadian and Mexican producers.[27] Critics argued that removing these provisions would have been the beginning of

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[15] *See id.*

[16] *Id.*

[17] USTR, *supra* note 3, at 12–13.

[18] *See* GARY HUFBAUER & EUIJIN JUNG, PETERSON INST. FOR INT'L ECON., NAFTA RENEGOTIATION: U.S. OFFENSIVE AND DEFENSIVE INTERESTS VIS-À-VIS CANADA 12 (2017), https://piie.com/publications/policy-briefs/nafta-renegotiation-us-offensive-and-defensive-interests-vis-vis-canada [https://perma.cc/T2Y3-FAQY].

[19] BERGSTEN, *supra* note 6, at 24.

[20] IAN F. FERGUSSON & M. ANGELES VILLARREAL, CONG. RESEARCH SERV., IF10997, PROPOSED U.S-MEXICO-CANADA (USMCA) TRADE AGREEMENT 2 (2018).

[21] Kirby, *supra* note 1.

[22] *Id.*

[23] *See* Jeffrey Schott, *For Mexico, Canada, and the United States, a Step Backwards on Trade and Investment*, PIIE: TRADE & INV. POL'Y WATCH (Oct. 2, 2018), https://piie.com/blogs/trade-investment-policy-watch/mexico-canada-and-united-states-step-backwards-trade-and [https://perma.cc/3TCC-RNX9].

[24] *Id.*

[25] *See* Chad Bown, *Trump's Renegotiation Could Take the "Free" Out of NAFTA's Trade*, PIIE: TRADE & INV. POL'Y WATCH (July 19, 2017), https://piie.com/blogs/trade-investment-policy-watch/trumps-renegotiation-could-take-free-out-naftas-trade [https://perma.cc/F3TW-6XFA].

[26] *Id.*

[27] *Id.*

the end of "free" trade under NAFTA.[28] It is important to note that the USMCA includes a sixteen year sunset clause, and requires review every six years.[29] If future Administrations adopt a similarly aggressive stance, these provisions will certainly be the focus of future USMCA negotiations.

A. *Chapter 19 Dispute Settlement*

Chapter 19 provides a process for binding arbitration over antidumping and countervailing duties (AD/CVD).[30] These measures are authorized under Title VII of the U.S. Tariff Act of 1930.[31] Under Title VII, the U.S. International Trade Commission (USITC) is tasked with investigating claims that domestic firms are subject to "material injury" (or the threat thereof) due to dumping or illegal subsidies by foreign governments.[32] If the USITC finds in favor of the domestic industry, U.S. Customs will impose special duties on imports from specific countries in order to bring these import prices closer to their "fair" value.[33] Since the conclusion of the Uruguay Round of WTO negotiations, the U.S. is required to conduct "sunset" reviews no later than thirty days before the five-year anniversary of the AV/CVDs being imposed.[34] To keep the duties in place, the USITC must determine that revoking the AV/CVD measures would again lead to "material injury" due to dumping or illegal subsidy.[35]

USITC findings of material injury can be appealed.[36] Non-NAFTA members can appeal these decisions to the U.S. Court of International Trade.[37] NAFTA members, on the other hand, can call for the establishment of a binational panel to review AD/CVD decisions.[38] Both affected nations are represented on the panel, and its decision is binding.[39] The Chapter 19 dispute settlement mechanism was enshrined in NAFTA partly in response to the U.S.'s frequent use of AD/CVDs in the 1980s.[40] It has since produced many judgments

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[28] *Id.*

[29] Kirby, *supra* note 1.

[30] *Understanding Antidumping & Countervailing Duty Investigations*, U.S. INT'L TRADE COMM'N, https://www.usitc.gov/press_room/usad.htm [https://perma.cc/3NEG-9KBV].

[31] *Id.*

[32] *Id.*

[33] *See id.*

[34] *Understanding Five-Year (Sunset) Reviews*, U.S. INT'L TRADE COMM'N, https://www.usitc.gov/press_room/us_sunset.htm (last visited Sept. 30, 2018) [https://perma.cc/63NU-8UKP].

[35] *Id.*

[36] North American Free Trade Agreement, Can.-Mex.-U.S., ch. 19, art. 1904, Dec. 17, 1992, 32 I.L.M. 289 (1993) [hereinafter NAFTA].

[37] *Id.*

[38] *Id.*

[39] *Id.*

[40] *See* Bown, *supra* note 25.

striking down U.S. AD/CVDs.[41] Experts believe it has also prevented the use of AD/CVD measures among NAFTA partners.[42] Despite the USTR's strong stance against it, Chapter 19 of NAFTA is now contained in Chapter 10 of the USMCA.[43]

B. *The Global Safeguard Exclusion*

The global safeguard exclusion is related to a different class of trade protections. Article XIX of the General Agreement on Tariffs and Trade (GATT) authorizes member states to temporarily raise trade barriers on specific products, so long as they are applied in a non-discriminatory way.[44] Section 201 of the Trade Act of 1974 provides the legal framework for these safeguards in the U.S.[45] The investigative process is similar to the one for AD/CVD cases, with two important exceptions. First, safeguards do not require a finding of unfair or illegal trade practices.[46] Second, the standard for "material harm" is higher in safeguard investigations compared to AD/CVD investigations.[47] Section 201 requires the injury (or threat thereof) to be "serious."[48] If the USITC finds there is serious injury to a domestic industry, they recommend a remedy to the President (usually some kind of trade barrier), who has final authority over the remedy.[49] Protections are permitted for an initial period of four years, with a possible extension up to eight total years.[50]

Although safeguards are supposed to be imposed in a non-discriminatory manner, the global safeguard exclusion carves out exemptions for Canada and Mexico from remedies recommended by the USITC.[51] Imports from Mexico and Canada are considered exempt from safeguards following a Section 201 investigation unless the USITC finds (1) imports from an individual NAFTA

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[41] *See* Cyndee Todgham Cherniak, *NAFTA Chapter 19 Bi-National Panel Review Process Used Rarely by Canada/US; BUT Remains Needed*, CANADA-U.S. BLOG (July 26, 2017), http://www.canada-usblog.com/2017/07/26/nafta-chapter-19-bi-national-panel-review-process-used-rarely-by-canadaus-but-needed/ [https://perma.cc/YM4Y-J92S].

[42] Bown, *supra* note 25.

[43] Gregory Spak et. al, *United States, Canada, and Mexico Announce New Trilateral Trade Agreement to Replace NAFTA*, LEXOLOGY (Oct. 2, 2018), https://www.lexology.com/library/detail.aspx?g=2abffd0b-b4e8-45ee-9fcc-33226ecb3ad6 [https://perma.cc/82BC-JGYK].

[44] *See Understanding Safeguard Investigations*, U.S. INT'L TRADE COMM'N, https://www.usitc.gov/press_room/us_safeguard.htm [https://perma.cc/UY83-37B3].

[45] *Id.*

[46] *Id.*

[47] *Id.*

[48] *Id.*

[49] *Id.*

[50] GLOBAL AFFAIRS CAN., U.S. TRADE REMEDY LAW: THE CANADIAN EXPERIENCE (2013), http://www.international.gc.ca/trade-agreements-accords-commerciaux/topics-domaines/disp-diff/section03.aspx?lang=eng [https://perma.cc/NN7D-Y4XP].

[51] *See id.*

country account for a "substantial" share of the imported goods targeted in the investigation, and (2) imports from NAFTA countries are important contributors to the "serious injury" found during the investigation.[52] For example, the USITC has recently determined that imports of certain types of photovoltaic cells are a cause of "serious injury" to domestic producers.[53] Canada sought an exemption from the safeguards as member of NAFTA. In their published decision, the majority of the USITC panel found that imports from Canada did not satisfy (1) and (2), and excluded them from the proposed remedies.[54]

Considering Mexico and Canada account for approximately twenty-five percent of total U.S. trade in goods and services,[55] the global safeguards exemption clearly limits the President's power to protect domestic industries. Given the President's skepticism toward free trade, it is not surprising that the USTR would call for this provision of NAFTA to be eliminated. However, the USMCA reproduces the global safeguard exclusion that was found in Chapter 8 of NAFTA.[56]

C. *NAFTA and the Trade Balance*

The Trump Administration has cited the U.S. trade deficit as a justification for its aggressive negotiating strategy.[57] However, this reasoning has drawn scrutiny from experts.[58] U.S. trade with Canada is roughly balanced.[59] The U.S. does maintain a trade deficit with Mexico, but Mexico maintains a trade deficit with the rest of the world.[60] It would be difficult to persuade either of these countries to make concessions that would increase their bilateral deficit with the U.S. It stands to reason that they would be unwilling to agree to the Trump Administration's demands for more flexible protectionism without achieving increased protection of their own industries.

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[52] *Id.*

[53] News Release No. 17-133, U.S. Int'l Trade Comm'n, Crystalline Silicon Photovoltaic Cells (Whether or Not Partially or Fully Assembled into Other Products) (Sept. 22, 2017), https://www.usitc.gov/press_room/news_release/2017/er0922ll832.htm [https://perma.cc/9S3V-66GE].

[54] *See* U.S. INT'L TRADE COMM'N, INV. NO. TA-201-075, CRYSTALLINE SILICON PHOTOVOLTAIC CELLS (WHETHER OR NOT FULLY ASSEMBLED INTO OTHER PRODUCTS) (2017), https://www.usitc.gov/press_room/documents/solar201_remedy_commissioner statements.pdf [https://perma.cc/N3ZK-T2W7].

[55] U.S. DEP'T OF COMMERCE: BUREAU OF ECON. ANALYSIS, U.S. INTERNATIONAL TRADE IN GOODS AND SERVICES (2016), https://www.bea.gov/newsreleases/international/trade/2017/trad1216.htm [https://perma.cc/BQF4-J2DN].

[56] GOV'T OF CAN., TRADE REMEDIES AND RELATED DISPUTE SETTLEMENT (CHAPTER 19) SUMMARY (Oct. 2018), http://international.gc.ca/trade-commerce/trade-agreements-accords-commerciaux/agr-acc/usmca-aeumc/dispute-differends.aspx?lang=eng [https://perma.cc/D3H2-R6RA].

[57] USTR, *supra* note 3, at 2.

[58] *See* BERGSTEN, *supra* note 6, at 15.

[59] *Id.* at 16.

[60] *Id.* at 16.

Critics also point out that the Administration's attempt to address the trade deficit through bilateral or narrowly multilateral negotiations is fundamentally misguided.[61] The trade balance is determined by domestic macroeconomic conditions, not trade agreements.[62] The U.S. maintains a trade deficit because its domestic savings (by households, firms, and government) are smaller than domestic investment.[63] Raising barriers to trade against NAFTA partners will be disruptive and costly in the short term and will not have any long-term effect on the trade balance. For instance, decreasing the U.S. bilateral trade deficit with Mexico, holding domestic savings and investment constant, will simply increase U.S. trade deficits with other countries as production shifts to other countries in order to circumvent the new barriers.

U.S. trade policy with Japan in the 1970s and 80s is an instructive example of the last point. Following negotiations with the U.S., Japan adopted voluntary export restraints (VERs) on goods sold to the U.S. as well as voluntary import expansions (VIEs) for U.S. goods sold in Japan.[64] While significant effects were seen within specific sectors, these policies had no net effect on the U.S. global balance of trade.[65] In light of the marginal changes in policy produced by the USMCA, one should expect no substantial changes in the U.S. trade deficit.

III. THE COSTS AND BENEFITS OF NAFTA

If NAFTA renegotiation will not ultimately affect the balance of trade, it is worth asking what the U.S. stands to gain or lose from these negotiations. Since the USMCA is not a major departure from NAFTA, the changes are likely to be subtle. To understand what is likely to come from the USMCA, it is important to identify what the net effect of NAFTA has been, as well as the regional and sectoral variation in those effects.

A. *Aggregate Effects*

Measuring the aggregate effects of NAFTA for the U.S. is a contentious subject, at least in popular media. On the campaign trail, President Trump made it clear that he thought NAFTA was the "worst trade deal" the U.S. had ever signed.[66] Critics of the deal point to losses in U.S. manufacturing employment

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[61] *Id.* at 17.

[62] *Id.* at 14–15.

[63] For a non-technical explanation, see SCOTT A. WOLLA, FED. RESERVE BANK OF ST. LOUIS, INTERNATIONAL TRADE: MAKING SENSE OF THE TRADE DEFICIT 3–4 (Nov. 2016), https://research.stlouisfed.org/publications/page1-econ/2016/11/01/international-trade/ [https://perma.cc/YHW5-B4SC].

[64] *See* BERGSTEN, *supra* note 6, at 18.

[65] *Id.*

[66] Julie Hirschfeld Davis & Alan Rappeport, *After Calling NAFTA 'Worst Trade Deal,' Trump Appears to Soften Stance*, N.Y. TIMES (Mar. 30, 2017), https://www.nytimes.com/2017/03/30/business/nafta-trade-deal-trump.html [on file with *Ohio State Law Journal*].

and the persistent U.S. trade deficit.[67] Then Presidential candidate Ross Perot famously coined the phrase "giant sucking sound" to describe the loss of U.S. manufacturing employment to Mexico as a result of NAFTA.[68] This heated political rhetoric reflects, in part, the fact that NAFTA was the first free trade agreement the U.S. signed with a developing country.[69] The criticisms tend to focus on the threat posed by competition with Mexico, while ignoring any effects from increased trade with Canada.[70]

These concerns are not without cause. NAFTA did contribute to lower employment in certain sectors in the U.S.[71] The magnitudes of those effects, however, is a subject of some controversy. Robert Scott published a study in 2011 attempting to estimate the net job loss due to increased trade with Mexico.[72] The analysis focused on the increased trade deficit with Mexico after 1994, which the author attributes to NAFTA.[73] He estimated that increased trade with Mexico due to NAFTA caused the loss of nearly 700,000 jobs in the U.S., with that largest effects felt in the manufacturing sector.[74] It is important to consider this study in the context of the claim made above: bilateral trade deals do not determine the size of the U.S. global trade deficit. Scott's study assumed that the net imports from Mexico would otherwise have been produced in the U.S. if NAFTA had not been signed. Since domestic savings were still less than domestic investment during this period, these goods would simply have been produced in some other country.[75]

Proponents do not deny that NAFTA was disruptive to the economic order in the U.S. It is well known that lower trade barriers will drive smaller, less efficient firms to bankruptcy while allowing larger, more efficient firms to expand.[76] The net result is an increase in productivity through this process of

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[67] *See* USTR, *supra* note 3, at 2.

[68] *See The 1992 Campaign: Transcript of 2d TV Debate Between Bush, Clinton and Perot*, N.Y. TIMES (Oct. 16, 1992), http://www.nytimes.com/1992/10/16/us/the-1992-campaign-transcript-of-2d-tv-debate-between-bush-clinton-and-perot.html [on file with *Ohio State Law Journal*].

[69] GARY CLYDE HUFBAUER ET AL., PETERSON INST. FOR INT'L ECON., NAFTA AT 20: MISLEADING CHARGES AND POSITIVE ACHIEVEMENTS 1 (2014), https://piie.com/sites/default/files/publications/pb/pb14-13.pdf [https://perma.cc/PNL9-VV47].

[70] *See id.* at 11, 16.

[71] ROBERT E. SCOTT, ECON. POLICY INST., NAFTA'S IMPACT ON THE STATES (2001), https://www.epi.org/publication/briefingpapers_nafta01_impactstates/#anchor116616 [https://perma.cc/9FBT-6B7B].

[72] ROBERT E. SCOTT, ECON. POLICY INST., HEADING SOUTH: U.S.-MEXICO TRADE AND JOB DISPLACEMENT AFTER NAFTA 7 (2011), https://www.epi.org/files/page/-/BriefingPaper308.pdf [https://perma.cc/BWX6-HRP4].

[73] *Id.*

[74] *Id.*

[75] *See* HUFBAUER, *supra*, note 69, at 5.

[76] *See* ANDREW BERNARD ET AL., INST. FOR FISCAL STUDIES, FALLING TRADE COSTS, HETEROGENEOUS FIRMS, AND INDUSTRY DYNAMICS 3, 6 (Apr. 2003), https://www.ifs.org.

"creative destruction," and as resources are realigned with a country's comparative advantage.[77] The disruptions caused by lower trade barriers also increase "churn" in labor markets as workers leave shrinking industries to join the ones that are expanding.[78] Unfortunately, it is not always obvious which jobs are "created" due to lower trade barriers, while it is very visible which jobs are lost.[79] Proponents argue that NAFTA's contribution to U.S. labor markets was not necessarily more jobs, but better jobs, as workers left shrinking import-competing sectors and higher-paying jobs were created elsewhere.[80]

The U.S. auto industry has been particularly successful at taking advantage of the new opportunities created through NAFTA.[81] They have successfully expanded their supply chains into Mexico and the Canada.[82] Since 1994, the gap between U.S. auto imports and exports has widened – reflecting the increasing importance of sourcing components from abroad.[83] This has also been reflected in a decline in U.S. employment in the auto sector.[84] However, real value added per worker rose by 41% U.S. in the two decades since NAFTA was signed.[85] Real hourly compensation for U.S. auto workers has also increased by approximately 19% over the same time period.[86] The auto industry is also at the center of the new rules of origin and "minimum wage" requirements in the USMCA.[87] However, critics argue that these provisions may end up significantly raising auto prices for U.S. consumers,[88] and actually encourage more auto imports from abroad rather than more production in the U.S.[89]

So, what is the true net effect of NAFTA? Answering this question requires a sophisticated theoretical framework and empirical methodology. It is not enough to simply compare levels of GDP or employment before and after NAFTA came into effect. We must take into account the complex economic relationships among NAFTA countries, between NAFTA and the rest of the

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uk/wps/wp0310.pdf [https://perma.cc/7C3S-XFYA] (finding that the general consensus is that "foreign competition both reduces the domestic mark share of import-competing firms and reallocates domestic market share from inefficient to efficient firms").

[77] *See id.* at 2.

[78] *See id.* at 19.

[79] *See* HUFBAUER, *supra* note 69, at 6.

[80] *Id*. at 7.

[81] *NAFTA, 20 Years Later: Do the Benefits Outweigh the Costs?* WHARTON, UNIV. OF PA. (Feb. 19, 2014), http://knowledge.wharton.upenn.edu/article/nafta-20-years-later-benefits-outweigh-costs/ [https://perma.cc/XJ8A-8V23].

[82] *Id.*

[83] *Id.*

[84] *Id.*

[85] HUFBAUER, *supra* note 69, at 9.

[86] *Id.* at 10.

[87] Kirby, *supra* note 1.

[88] *See* Jeffrey Schott, *A Reported NAFTA Auto Deal Would Backfire Against Consumers and Auto Makers Alike*, PIIE: TRADE & INV. POL'Y WATCH (Aug. 24, 2018), https://piie.com/blogs/trade-investment-policy-watch/reported-nafta-auto-deal-would-backfire-against-consumers-and [https://perma.cc/DQ7B-5RNK].

[89] Schott, *supra* note 23.

world, as well as among traded and non-traded sectors within these countries. It is instructive to compare the results of the study published by Anderson and van Wincoop in 2001[90] against the those published by Caliendo and Parro in 2015.[91] The earlier study found that NAFTA produced modest net gains for Canada and the U.S., while imposing losses on Mexico.[92] They also found that NAFTA imposed miniscule losses on the rest of the world, mostly due to trade diversion.[93] On the other hand, Caliendo and Parro found that NAFTA created modest gains for the U.S. (once again), modest losses for Canada, and fairly large gains for Mexico.[94]

The differences in findings reflects a difference in methodology: Caliendo and Parro accounted for the complex linkages among heterogeneous sectors that characterize a modern economy.[95] In other words, NAFTA affected different sectors of the U.S. economy differently. Since these sectors are interdependent, gains and losses in one sector have a ripple effect through the rest of the economy.[96] Caliendo and Parro found that failing to account for these "ripples" causes a substantial underestimation of the aggregate welfare effects from NAFTA.[97] Still, even after accounting for these "ripples," the net effect of NAFTA on the U.S. has been small.[98] The Congressional Budget Office estimates the effect of NAFTA on GDP growth to be "probably no more than . . . a few hundredths of one percent."[99] By the same token, USMCA will likely have no appreciable effects on overall U.S. GDP growth. However, emphasizing the aggregate effects covers up the highly uneven distribution of gains and losses across different industries and across different regions within the U.S.

B. *Decomposing the Gains and Losses from Trade*

Contrary to the sometimes heated political rhetoric, there seems to be a consensus in the economic literature that NAFTA was a modest net benefit to the United States. However, there were clear winners and losers within the U.S. as well as within Canada and Mexico.[100] To make sense of this heterogeneity,

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[90] JAMES E. ANDERSON & ERIC VAN WINCOOP, NAT'L BUREAU OF ECON., RESEARCH, BORDERS, TRADE AND WELFARE (2001), http://www.nber.org/papers/w8515 [https://perma.cc/BT9T-WJ2Y].

[91] Lorenzo Caliendo & Fernando Parro, *Estimates of the Trade and Welfare Effects of NAFTA*, 82 REV. ECON. STUD. 1 (2015).

[92] ANDERSON, *supra* note 90, at 29.

[93] *Id.* at 16–17.

[94] Caliendo & Parro, *supra* note 91, at 3.

[95] Caliendo & Parro, *supra* note 91, at 1.

[96] *See id.* at 23–34.

[97] *Id.* at 27–28.

[98] *Id.*

[99] CONG. BUDGET OFFICE, THE EFFECTS OF NAFTA ON U.S.-MEXICAN TRADE AND GDP xiv (May 2003).

[100] *See id.* at 6.

it is important to remember that the distribution of the gains from trade depend on the nature of a country's comparative advantage.[101] Some sectors will expand as they are able to reach new export markets or gain access to cheap intermediate goods.[102] Other sectors will shrink as they face of more intense head-to-head competition with cheaper imports.[103] This has implications for how the gains from trade are distributed between workers and owners of capital, and even among different types of workers.

When trying to understand the linkages between barriers to trade and the distribution of the gains from trade, economists often turn to the Stolper-Samuelson theorem.[104] Put simply, this theorem states that lower barriers to trade will make a country's relatively abundant factors of production better off, while making others worse off.[105] Viewed through this lens, it is not surprising that U.S. manufacturing workers were made worse off due to NAFTA: Mexico is relatively abundant in the types of workers employed in these manufacturing jobs compared to the U.S. The theorem also asserts that others in the U.S. will be made better off, even as manufacturing workers are made worse off.[106] Considering the differences between the U.S. and Mexico, this would likely include highly skilled workers and owners of capital.

Although they did not study NAFTA specifically, a study published in 2014 provides some evidence to support this point.[107] The authors estimated the effects of exposure to globalization on different types of workers in different industries.[108] They measure exposure to globalization in terms of industry export share, import penetration, and foreign affiliate employment (meant to capture the degree of offshoring).[109] They also distinguish between more and less "routine" occupations, which gives some indication of workers' skill levels.[110] Their findings demonstrate the wide dispersion of gains and losses within the U.S. from NAFTA and similar trade agreements.[111] First, they show that import penetration and offshoring to low wage countries (like Mexico)

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[101] BERNARD, *supra* note 76, at 3.

[102] *See id.* at 19.

[103] *Cf.* Gary Clyde Hufbauer et al., NAFTA AT 20: MISLEADING CHARGES AND POSITIVE ACHIEVEMENTS 5 (finding that "only a small fraction of the jobs lost are caused by imports in general or imports from Mexico").

[104] For a non-technical introduction, see *An Inconvenient Iota of Truth*, THE ECONOMIST (Aug. 6, 2016), https://www.economist.com/news/economics-brief/21703350-third-our-series-looks-stolper-samuelson-theorem-inconvenient-iota [https://perma.cc/J755-GR38].

[105] *Id.*

[106] *See id.*

[107] Avraham Ebenstein et al., *Estimating the Impact of Trade and Offshoring on American Workers Using the Current Population Surveys*, 96 REV. ECON. & STAT. 581 (2014).

[108] *Id*. at 581.

[109] *Id*. at 585.

[110] *Id*. at 586.

[111] *See id*. at 594.

tends to lower U.S. wages.[112] This effect is particularly strong for workers performing the most routine tasks.[113] They find similar effects on employment for these workers.[114] Interestingly, offshoring to low-wage countries actually increases wages for workers in the least routine (highest-skilled) occupations.[115] There is also a positive (but statistically insignificant) effect of import penetration on high-skilled workers wages.[116]

These results confirm the basic intuition of the Stolper-Samuelson theorem – lower barriers to trade with low-income countries allow U.S. firms to find less-expensive substitutes for low-skill U.S. workers. This reduces employment opportunities for these workers and reduces wages for low-skill workers who are able to keep their jobs. At the same time, high-skill workers are better off thanks to cheaper imported goods or intermediate components (in the case of offshoring), which are complementary to them in their occupations. To understand this, it is helpful to return to the example of the U.S. auto industry. Following NAFTA, total employment in the U.S. auto sector shrank, but there were large increases in value-added per worker and real compensation for those still employed.[117] This corresponds to a change in the kinds of tasks workers perform in U.S. auto plants. The workers who remain employed in the U.S. auto industry today do a very different kind of work than the average plant employee in 1993.[118] Rather than performing relatively simple tasks to manufacture components, workers engage in skill-intensive, non-routine tasks that cannot be easily outsourced or automated.[119]

The Stolper-Samuelson theorem is closely related to the Heckscher-Ohlin theorem, another classic result that predicts how lower barriers to trade will affect different industries within a country.[120] Put simply, when barriers to trade fall, industries that intensively use the country's abundant factor of production should expand while others should shrink.[121] Again, it would be a mistake to ascribe all changes in industry size after 1994 to NAFTA.[122] However, large changes in the volume of trade among NAFTA members has been documented

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[112] *Id*. at 590.

[113] Ebenstien, *supra* note 107, at 590.

[114] *Id.* at 582.

[115] *Id*. at 590.

[116] *Id*. at 591.

[117] HUFBAUER, *supra* note 69, at 9.

[118] *See, e.g.*, Jeff Bennett, *Why GM Hired 8,000 Programmers*, WALL ST. J. (Feb. 17, 2015), https://www.wsj.com/articles/gm-built-internal-skills-to-manage-internet-sales-push-1424200731[https://perma.cc/UK7V-3V73] (highlighting engineering tasks required of today's auto workers).

[119] *See generally id*. (explaining the transition of auto worker duties).

[120] For a non-technical introduction, see *Why Trade?*, NOBELPRIZE.ORG (Feb. 28, 2006), https://www.nobelprize.org/educational/economic-sciences/trade/ohlin.html [https://perma.cc/V3WE-XS9P].

[121] *See id.*

[122] *See supra* notes 71–79 and accompanying text.

in a few key sectors since the agreement was signed.[123] A study by the Congressional Research Service in 2003 highlighted the automotive industry along with chemicals and allied products, computer equipment, textiles and apparel, and microelectronics.[124] All of these sectors saw significant rapid growth in total trade volume as well as large increases in trade deficits between the U.S. and its NAFTA partners.[125]

NAFTA has also become very important for U.S. agriculture. Mexico and Canada are major export markets for U.S. agricultural products.[126] Approximately 28% of total U.S. maize production is exported to Mexico.[127] Mexico and Canada collectively account for nearly one-third of U.S. beef exports.[128] As with the auto industry, agricultural supply chains now stretch across the borders of NAFTA member states.[129] For example, U.S. producers imported nearly 5 million pigs from Canada in 2014.[130] These pigs were finished and slaughtered in the U.S., and a significant portion of the pork products were re-exported to Canada or Mexico.[131]

C. *Regional Variation*

Because industries and factors of production (i.e. capital, skilled vs. unskilled labor, natural resources, etc.) are not evenly distributed across the U.S., lowering barriers to trade will have different economic impacts in different parts of the country. A study published by Robert Scott in 2001[132] uses the same basic methodology as in Scott's 2011 study[133] to estimate the effect of NAFTA on employment in all fifty U.S. states. Again, the analysis makes two critical (and dubious) assumptions: 1) changes in the trade deficit after 1994 can be attributed to NAFTA, and 2) the excess of imported products over exports would otherwise have been produced in the U.S. without NAFTA.[134] Scott finds that California, Michigan, and New York experienced the largest total job losses due

[123] M. ANGELES VILLARREAL, CONG. RESEARCH SERV., RL31386, INDUSTRY TRADE EFFECTS RELATED TO NAFTA 5 (2003).

[124] *Id.*

[125] *Id.* at 5–6.

[126] *See* Cullen S. Hendrix, *Agriculture in the NAFTA Renegotiation*, PIIE: TRADE & INV. POL'Y WATCH (June 19, 2017), https://piie.com/blogs/trade-investment-policy-watch/agriculture-nafta-renegotiation [https://perma.cc/H677-PDVP].

[127] *Id.*

[128] *Id.*

[129] *Id.*

[130] *Id.*

[131] *Id.*

[132] *See generally* SCOTT, *supra* note 71 (providing an estimate for the employment effects of NAFTA in 2001).

[133] *See generally* SCOTT, *supra* note 72 (providing an estimate for the employment effects of NAFTA in 2011).

[134] SCOTT, *supra* note 71, at 7.

to NAFTA.[135] Alaska, Wyoming, and North Dakota experienced the smallest job losses.[136]

Again, it is difficult to link the trade balance to changes in trade policy or changes in the trade balance to changes in the level of employment. A 2016 study by Hakobyan and McLaren takes a different approach, studying how increased exposure to Mexican imports due to NAFTA has affected wages at the regional level.[137] They begin by calculating regional measures of exposures to Mexican import competition, measured at the level of a Consistent Public-Use Microdata Area or "*conspuma*."[138] Their measure of exposure aggregates *conspuma*-level information on the sizes of each industry, the level of the tariff on Mexican goods for that industry, and a measure of Mexico's comparative advantage in that industry.[139] The degree of concentration they find is remarkable; eight of the top ten most vulnerable *conspumas* were in North and South Carolina.[140] Unsurprisingly, they find that areas most exposed to Mexican imports experienced slower wage growth.[141] They also find that these effects are larger for workers with the lowest levels of education.[142]

Hakobyan and McLaren's study is limited by the fact that it focuses specifically on the negative effects due to increased import competition from Mexico. This paints a somewhat gloomy picture of NAFTA, with no apparent upside. It is important to remember that many firms (and their employees) benefit from imported intermediates sourced from both Canada and Mexico.[143] States also differ in the extent to which NAFTA has reshaped these supply chains.[144] Brookings recently published a study examining how reliant each state is on intermediate goods imported from Canada and Mexico.[145] Overall, nearly 50% of U.S. trade with NAFTA partners is in intermediates.[146] However, this figure varies tremendously from state to state. Montana sourced 92.6% of their imported intermediates from NAFTA countries in 2015.[147] Louisiana, on the other hand, relied on NAFTA partners for only 8.2% of their imported intermediates.[148] The rapid expansion of intermediates trade has been

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[135] SCOTT, *supra* note 72.

[136] *Id. at app. tbl. "Job Losses by State, 93-00."*

[137] Shushanik Hakobyan & John McLaren, *Looking for Local Labor Market Effects of NAFTA*, 98 REV. ECON. & STAT. 728, 728–41 (2016).

[138] *Id*.

[139] *Id*. at 730.

[140] *Id*. at 735.

[141] *Id*. at 741.

[142] Hakobyan, *supra* note 137, at 735.

[143] Joseph Parilla, *How US States Rely on the NAFTA Supply Chain*, BROOKINGS: THE AVENUE (Mar. 30, 2017), https://www.brookings.edu/blog/the-avenue/2017/03/30/how-u-s-states-rely-on-the-nafta-supply-chain/ [https://perma.cc/KQB5-L8LU].

[144] *Id.*

[145] *Id.*

[146] *Id.* at fig. 2.

[147] *Id.* at tbl. 1.

[148] *Id.*

accompanied by massive flows of Foreign Direct Investment (FDI) among NAFTA partners. Around 50% of total FDI in both Canada[149] and Mexico[150] comes from the United States.

NAFTA has also benefited some U.S. states through increased export opportunities. This has been especially important for U.S. agriculture and the states where these farms are located.[151] Farmers in the Midwest enjoy large export markets in Mexico and Canada for their corn and soybeans.[152] These farms are generally concentrated in the Midwest, spread out across Ohio, Indiana, Illinois, Iowa, Minnesota, and the Dakotas.[153] NAFTA has also created export opportunities for pork exporters, which are even more concentrated, largely in Iowa.[154] Regions with large clusters of dairy producers are likely to benefit from the increased access to Canadian markets negotiated under the USMCA.

No study has attempted to fully decompose the effects of NAFTA across states accounting for increased import competition, export opportunities, and offshoring. However, the 2014 study referenced above suggests that the benefits have gone to states that are populated with skilled workers and host firms that have expanded their supply chains into Mexico and Canada.[155] NAFTA has also probably benefited a number of Midwestern states as they found new markets for their agricultural exports. However, the fact that NAFTA has produced only minute aggregate gains for the U.S. implies that these gains are mostly balanced out by the costs imposed on other states, workers, and firms.[156]

The uneven regional distribution of winners and losers from NAFTA means that this policy is inherently a transfer of wealth among the states. Similarly, the USMCA will imply further transfers of wealth among U.S. states. Some states will benefit from increased export opportunities (e.g. dairy), while states that rely more heavily on the auto industry may suffer, if critics' fears about the new rules of origin and "minimum wage" provisions are realized.[157] Negotiations took place under the President's "trade promotion authority," which means

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[149] U.S. DEP'T OF STATE, 2014 INVESTMENT CLIMATE STATEMENT–CANADA 16 (2014), https://www.state.gov/documents/organization/226813.pdf [https://perma.cc/D9YX-7SPS].

[150] DEP'T OF STATE, 2013 INVESTMENT CLIMATE STATEMENT–MEXICO (2013), https://www.state.gov/e/eb/rls/othr/ics/2013/204693.htm [https://perma.cc/2WKN-Q4P3].

[151] Kim Soffen & Kevin Uhrmacher, *If NAFTA Sees Major Changes, Farmers May Pay the Price*, WASH. POST (June 5, 2017), https://www.washingtonpost.com/graphics/national/nafta-negotiation-farmers/?noredirect=on&utm_term=.9bdb9e145f44 [https://perma.cc/XC8P-3V7M].

[152] *Id.* at fig.2.

[153] *Id.*

[154] Donnelle Eller, *Trade War: Mexico Pork Tariff Threats Push Iowa Losses to $560 Million*, DES MOINES REG. (June 1, 2018), https://www.desmoinesregister.com/story/money/agriculture/2018/06/01/mexico-pork-tariff-trade-war-threats-iowa-producer-losses-trump-steel-canada-china-exports-ham/663212002/ [https://perma.cc/8BVW-SDN5].

[155] EBENSTEIN, *supra* note 107, at 589.

[156] CONG. BUDGET OFFICE, *supra* note 99, at xiv.

[157] Schott, *supra* note 23.

legislators in the House and Senate will only have the opportunity to vote the revised treaty up or down.[158] Such a limited role for Congress in the negotiation process means that states may have to rely on their own powers to adapt to whatever changes the USMCA might bring.

IV. TRADE POLICY AND STATE GOVERNMENT

The U.S. Constitution vests the power to conduct foreign affairs in the federal government.[159] The Supremacy Clause and Commerce Clause together make it clear that federal law will generally preempt state law in matters of international trade.[160] The Supreme Court has further clarified that state policies affecting international commerce will receive special scrutiny, even if they pertain to powers normally exercised by the states.[161] This gives states very few options for responding to the costs and benefits imposed on them by federal trade negotiations. Explicit protections like state-level tariffs and quotas are out of the question.

However, the courts have carved out some legal space for state and local governments to operate in this arena. First, states may be able to engage with international commerce when they have the express consent of Congress.[162] In this case, the state laws would not be subject to federal preemption because they are acting as "mere creatures of the state," assisting the federal government in its charge to manage foreign affairs.[163] Without the express consent of Congress, state or local laws that relate to international commerce must pass two tests: 1) the laws have a legitimate local purpose, and 2) the laws do not interfere with the federal government's ability to "speak with one voice" on international issues.[164] This sets a high bar. The actions of Congress or the President will preempt any state laws inconsistent those federal actions.[165] State laws may also be unconstitutional if the federal government merely demonstrates an intent to "occupy the field" covered by those state laws.[166] Presuming that managing the local impacts of international trade deals constitutes a legitimate local interest, states still must not interfere with the federal government's ability to conduct foreign policy.

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158 IAN F. FERGUSSON & CHRISTOPHER M. DAVIS, CONG. RESEARCH SERV., R43491 TRADE PROMOTION AUTHORITY (TPA): FREQUENTLY ASKED QUESTIONS 1 (2018).

159 U.S. CONST. art. 1, § 8, cl. 3.

160 *See, e.g.*, Michelin Tire Corp. v. Wages, 423 U.S. 276, 285 (1976) (describing the Federal Government's desire to speak with one voice when relating commercially with foreign nations).

161 Japan Lin Ltd. v. Cty. of L.A., 441 U.S. 434, 446 (1979).

162 Jessica V. Carter, *The Role of Local Government in Foreign Trade: The Case of Baltimore*, 15 MD. J. INT'L L. 169, 176–77 (1991).

163 *Id.* at 177.

164 Howard N. Fenton, III, *The Fallacy of Federalism in Foreign Affairs: State and Local Foreign Policy Trade Restrictions*, 13 NW. J. INT'L L. & BUS. 563, 571 (1993).

165 *Id.* at 572.

166 *Id.*

A. *Government Procurement*

Despite these limitations, state and local governments still have relatively broad latitude when it comes to procurement decisions. In *South-Central Timber Dev., Inc. v. Wunnicke*, the Supreme Court found that states can impose restrictions on procurement that would otherwise not be allowed if the states were acting as regulators.[167] This could allow the states to partially shield local firms from foreign competition. For example, state and municipal governments could give preferential treatment to bids from local firms in procurement decisions. The so-called "Massachusetts Burma Law" famously tested the limits of this power.[168] The Massachusetts state government attempted to penalize firms doing business with Myanmar (Burma) over human rights concerns.[169] The Supreme Court ultimately struck down the law, finding it went beyond Massachusetts acting as a "market participant."[170] Rather, the law required that the state monitor the activities of firms doing business with Myanmar.[171] The Court also pointed out that the law was crafted with the express intention of affecting the behavior of a foreign country, while the federal government had already imposed its own sanctions.[172]

Chapter 10 of NAFTA contains specific language covering government procurement.[173] The agreement targets non-defense related procurement covering nearly all federal agencies.[174] The general principle is that governments of NAFTA signatories must not discriminate against goods and services from other NAFTA countries.[175] NAFTA members also agree not to impose "offsets," which are conditions in procurement contracts that would require a foreign firm to take actions that would benefit local firms.[176] This might include local content requirements or licensing of technology.[177] However, state and local governments were not covered by the commitments in Chapter 10.[178] The USMCA reproduces the same commitments on government procurement for the U.S., but with updated monetary thresholds.[179] It would seem there are still no legal obstacles to state and local firms using procurement decisions to protect local firms, so long as they remain simply a market participant.

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[167] S. Cent. Timber Dev. Inc. v. Wunnicke, 467 U.S. 82, 93 (1984).

[168] *See States' Rights v. International Trade: The Massachusetts Burma Law*, 55 THE RECORD 554, 654 (2000).

[169] *Id.* at 560.

[170] *Id.* at 556.

[171] *Id.* at 558.

[172] *Id.*

[173] NAFTA, *supra* note 36, at Ch. 10.

[174] *Id*. at art. 1001.

[175] *Id*. at art. 1003.

[176] *Id*. at art. 1006.

[177] *Id.* at art. 1006.

[178] *Id.* at art. 1001.

[179] FERGUSSON, *supra* note 20.

Government procurement as a tool of economic development has been studied extensively in developing countries. The World Bank has argued that it is vitally important for low income countries.[180] Government procurement has also contributed to the development of important technologies in the developed world.[181] However, there is very little research on the effectiveness of state and local government procurement as a development strategy in high income countries. Some have also expressed concern that preferentially sourcing from local firms may lead to a reduction in the quality of goods and services governments are able to provide.[182] More research is necessary before one can conclude that procurement is an effective strategy for managing the local effects of changes in trade policy.

B. *Export Promotion*

Export promotion is a common strategy adopted by states seeking to participate in international commerce. In this case, states have received the express consent of Congress to engage with international commerce. The Export Trading Company Act of 1982 states "[t]hose activities of State and local governmental authorities which initiate, facilitate, or expand exports of goods and services can be an important source for expansion of total United States exports . . . . "[183] Congress also called for more coordination between local and federal agencies in export promotion with the Export Enhancement Act of 1992.[184]

All fifty states engage in some form of export promotion, with responsibilities spread across various government agencies.[185] Export promotion can take many forms, including outreach and training to give firms the information they need to start exporting.[186] This might include training on the logistics and regulatory hurdles to marketing their products in a foreign country. State governments can also play the role of "matchmaker" by

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[180] Philipp Krause & Lina Tutunji, *Three Reasons Procurement Is Essential for Development*, WORLD BANK: GOVERNANCE FOR DEV. (Nov. 6, 2014), http://blogs.worldbank.org/govergover/three-reasons-procurement-essential-development [https://perma.cc/H255-BQ6R].

[181] Ricardo Hausmann, *Government Procurement: Arsenic, or Gold?*, WORLD ECON. FORUM (Oct. 14, 2014), https://www.weforum.org/agenda/2014/10/ricardo-hausmann-government-procurement/ [https://perma.cc/29F3-3NJZ].

[182] Katherine Barrett & Richard Greene, *In Government Procurement, Buying Local Is Popular. But Is It Beneficial?*, GOVERNING (Mar. 2018), http://www.governing.com/topics/finance/gov-procurement-hometown-vendors-local-preference.html [https://perma.cc/F5US-7PYT].

[183] 15 U.S.C. § 4001(a)(9) (2012).

[184] U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-14-393, EXPORT PROMOTION: TRADE AGENCIES SHOULD ENHANCE COLLABORATION WITH STATE AND LOCAL PARTNERS 1 (2014).

[185] *Id.* at 6.

[186] *Id.* at 5.

organizing trade missions abroad.[187] State governors play an especially important role here as "economic ambassadors."[188] They can help local firms identify foreign markets for their goods, as well as connect them directly with partners in the foreign country. Finally, states can provide export financing as part of their export promotion strategy.[189] State agencies can provide loans to help businesses cover the costs of marketing and logistics associated with selling products internationally.[190] Export financing agencies can also provide accounts receivable financing, i.e. borrowing against accounts receivable to free up working capital while waiting for international transactions to clear.[191] All of these services are especially important to small businesses.

The effectiveness of these export promotion strategies is not well-established in the literature. Early studies of export promotion were generally qualitative and focused more on managers' perceptions of the effectiveness of the program.[192] It is particularly difficult to evaluate these programs because firms already engaged in international markets are more likely to self-select into the programs.[193] Therefore, it should be no surprise to find a positive relationship between participation in export promotion and engagement in international trade. It is more difficult to establish that export promotion programs cause firms to engage in international trade. A recent comprehensive review of the literature on export promotion yields limited support for the hypothesis that these programs boost state exports.[194] The success of the program seems contingent on the type of firm participating and the time span over which the program is studied.[195]

C. *Tax and Regulatory Incentives*

States may also engage in international commerce by offering tax and regulatory incentives to invite new businesses to invest in the area or to retain

[187] *Id.* at 9.

[188] *See* NAT'L GOVERNORS ASS'N, A GOVERNOR'S GUIDE TO TRADE AND GLOBAL COMPETITIVENESS 7 (2002), https://www.nga.org/files/live/sites/NGA/files/pdf/AM02TRADE.pdf.

[189] U.S. GOV'T ACCOUNTABILITY OFFICE, *supra* note 184, at 4.

[190] For a brief overview of state and local finance programs, see *Export Finance Programs*, EXPORT.GOV (Oct. 20, 2016), https://www.export.gov/article?id=Exploring-State-and-Local-Export-Finance-Programs [https://perma.cc/MGQ5-42HP].

[191] *Id.*

[192] Timothy J. Wilkinson & Lance Eliot Brouthers, *An Evaluation of State Sponsored Promotion Programs*, 47 J. BUS. RES. 229, 230 (2000).

[193] Joan Freixanet, *Export Promotion Programs: Their Impact on Companies' Internationalization Performance and Competitiveness*, 21 INT'L BUS. REV. 1065, 1078 (2012).

[194] *Id.*

[195] *Id.* at 1077.

businesses threatening to leave.[196] States will often compete for investment by offering lower individual and corporate income taxes, as well as lower sales and property taxes.[197] States might also offer tax credits for increasing local employment, investment, and research and development (R&D).[198] States could use these kinds of policies to promote local economic activity in the wake of the NAFTA renegotiation. However, the legal and economic justifications for such tax incentives are not particularly strong.

U.S. states have a long history of competing to attract businesses with tax reductions or favorable regulatory treatment.[199] Surprisingly, the economics literature has only recently been able to demonstrate that these incentives have a positive effect on businesses' location decisions.[200] It is less clear that these incentives have a net positive effect on the regions that offer them. While it has been demonstrated that tax incentives can attract R&D[201] and capital[202] to the locality offering them, these positive effects might be offset by a reduction in public services due to the decreased tax base.[203] Studies of local tax incentives have also shown that they may be a "zero-sum game" – the benefits to the state offering the incentive are matched by losses to surrounding states.[204]

Trade agreements also constrain states' abilities to use these kinds of incentives. This is illustrated by a recent case involving tax incentives provided by Washington state to aircraft manufacturer Boeing.[205] In 2013, the Washington State Legislature offered Boeing $8.7 billion in tax relief to keep production of the 777X in the state.[206] The European Union brought a case to the WTO Dispute Settlement Body alleging that these tax incentives constituted an illegal subsidy.[207] After an initial ruling in the EU's favor, the WTO Appellate Body rejected the EU's claim that Washington state had provided "prohibited" subsidies to Boeing.[208] However, the ruling leaves open the

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196 DANIEL J. WILSON, FRSBF ECONOMIC LETTER 2015-06, COMPETING FOR JOBS: LOCAL TAXES AND INCENTIVES (2015).

197 *Id.*

198 *Id.*

199 Robert S. Chirinko & Daniel J. Wilson, *Tax Competition Among U.S. States: Racing to the Bottom or Riding on a Seesaw?* (Fed. Reserve Bank of S.F., Working Paper No. 2017-05, 2017), https://www.frbsf.org/economic-research/files/wp08-03bk.pdf [https://perma.cc/9REM-DPPR].

200 Shawn Rohlin et al., *Tax Avoidance and Business Location in a State Border Model*, 83 J. URB. ECON. 34, 48–49 (2014).

201 Daniel J. Wilson, *Beggar Thy Neighbor? The In-State, Out-of-State, and Aggregate Effects of R&D Tax Credits*, 91 REV. ECON. & STAT. 431, 435 (2009).

202 Robert S. Chirinko & Daniel J. Wilson, *State Investment Tax Incentives: A Zero-Sum Game?*, 92 J. PUB. ECON. 2362, 2378 (2008).

203 *See* WILSON, *supra* note 196, at 2.

204 *Id.* at 2, 3.

205 Appellate Body Report, *United States—Conditional Tax Incentives for Large Civil Aircraft*, 5, WTO Doc. WT/DS487/AB/R (adopted July 21, 2017).

206 *Id.*

207 *Id.*

208 *Id.* at 34.

possibility that the tax incentives could be found to be "actionable subsidies," which was the basis of an earlier, successful dispute lodged by the EU against a similar tax incentive deal for Boeing.[209] If a state attempted to use similar incentives to adjust to a newly-renegotiated NAFTA, it could easily end up facing a similar challenge.

V. CONCLUSIONS

The Trump Administration's aggressive negotiating strategy is a departure from the norms established in previous Administrations.[210] In the past, trade agreements have been conducted as strategic exchanges of market access for mutual benefit. The current Administration's "America first" rhetoric seems to signal a change in negotiating strategy. This was also reflected in the USTR's objectives for renegotiating NAFTA. In this case, the USTR was not able to achieve negotiating objectives that would have allowed the President to raise substantial trade barriers with our NAFTA partners. Instead, the USMCA appears to be a narrow update of the existing NAFTA agreement. Like NAFTA, it is unlikely to have a large effect on overall U.S. GDP growth or unemployment, but the costs and benefits will be distributed unevenly across the states.

This Article has explored the legal constraints states will face as they attempt to respond to the changes USMCA will bring. In short, states' options are very limited. They face severe Constitutional constraints as well as constraints imposed by existing trade agreements. While they enjoy express Congressional approval for export promotion, there are limits on what they can do to protect local industry through procurement and tax policy. There is also very limited evidence that these measures can increase local economic growth.

States may need to rely on political forces, rather than policy, to weather the storm of USMCA and future trade negotiations. Many rural areas that voted for Trump in the 2016 election depend on export markets available to them through NAFTA. He will certainly need the support of those districts if he expects to run for reelection in 2020. This might have disciplined the Administration's approach to USMCA and, at the very least, prevented the Administration from walking away from the negotiations. The trade promotion authority insulates the renegotiation from conventional channels of political influence, but the states can also look for other solutions through their representatives in Congress. For example, states might lobby for an expansion of Trade Adjustment Assistance.[211]

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[209] Tim Hepher & Tom Miles, *WTO Reverses Boeing 777X Tax Credit Ruling in Blow to EU*, REUTERS (Sept. 4, 2017), https://www.reuters.com/article/us-wto-aircraft/wto-reverses-boeing-777x-tax-credit-ruling-in-blow-to-eu-idUSKCN1BF1PC [https://perma.cc/79KG-BTU7].

[210] *See* Cassella, *supra* note 5.

[211] *See Free Trade and Federalism*, NAT'L CONFERENCE OF STATE LEGISLATURES (2013), http://www.ncsl.org/ncsl-in-dc/standing-committees/labor-and-economic-develop

Uncertainty around trade deals like USMCA will probably be a major theme of this presidency. President Trump has taken similarly aggressive stances with other allies, with recent steel and aluminum tariffs providing notable examples.[212] It is difficult to predict which states will win and which states will lose in these negotiations. However, it is clear that states need to start thinking creatively about how they can protect themselves against abrupt changes in trade policy in the future.

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ment/free-trade-and-federalism.aspx [https://perma.cc/ZG2Z-5SWA].

[212] William Mauldin, *U.S. Tariffs Prompt Anger, Retaliation from Trade Allies*, WALL ST. J. (May 31, 2018), https://www.wsj.com/articles/u-s-slaps-steel-aluminum-tariffs-on-canada-mexico-european-union-1527774283 [https://perma.cc/62CM-YLUT].