

NEW HORIZONS IN U.S.-MEXICO RELATIONS

Recommendations for Policymakers

A Report of the U.S.-Mexico
Binational Council

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Finally, we are grateful to the Smith Richardson Foundation for the financial support for this endeavor and for its dedication to changing the U.S.-Mexico relationship for the better.

Executive Summary

The moment is right to achieve new momentum in U.S.-Mexico relations. Mexico has undergone an historic political transition with the election of Vicente Fox, and newly elected U.S. president George W. Bush is especially committed to good relations with Mexico. The mission of the U.S.-Mexico Binational Council is to contribute sound policy ideas to help the two governments set goals and sustain momentum. This Council report, therefore, is extensive, but not exhaustive, addressing the following areas: (1) general principles; (2) overall management of bilateral relations; (3) immigration policy; (4) trade; (5) investment and entrepreneurship; (6) energy policy; (7) monetary policy; (8) environmental and border issues; and (9) counternarcotics policy. The report is not a consensus document, and the ideas contained within cannot be attributed to any one member of the Council, although all of the members believe that the ideas contained in this report are worthy of consideration.

General Principles

- Nothing should be off limits for discussion--from joint law enforcement operations to open borders.
- The two presidents should decide whether they prefer a compartmentalized approach to issue management, which prevents contamination of the entire relationship when conflict emerges in a particular area, or a package approach that identifies trade-offs across the entire bilateral agenda.
- Leveling social disparities between Mexico and the United States is a high priority that should guide the formulation of policy. This might take the form of a substantial commitment from the United States and Canada to provide financial resources to Mexico as well as expanded trade and investment.
- The Canadian perspective on policy should be sought whenever appropriate, as well as the involvement of citizen's groups, business, and nongovernmental organizations.
- Targets for rapid action include (a) establishing hot-line links between President Bush and President Fox; (b) resolving remaining trade disputes; (c) funding Mexican micro-credit initiatives; (d) authorizing special advisers to discuss the parameters of North American cooperation; (e) expanding binational maritime intelligence-sharing and interdiction to three carefully targeted land zones; (f) creating a small binational committee of congressional leaders to explore options for legal immigration; and (g) implementing "virtual customs" for selected manufacturing sectors within one year.

Management of Bilateral Relations

- Expand hot-line telephone links to include the Oval Office of the White House and its Mexican counterpart, Los Pinos.
- Empower a key individual operating out of the White House to ensure that U.S. federal agencies sing from the same song sheet by (a) tasking the president's chief of staff or a deputy chief of staff with a Mexico "watching brief"; (b) creating a special assistant/senior director for North America in the National Security Council; (c) appointing a U.S. special envoy to Mexico.
- The United States should consider (a) creating a Border Affairs Principals Group within the NSC; (b) inviting the border states to send an observer to the annual Binational Commission meetings; (c) creating a State Department deputy assistant secretary (DAS) for border affairs.
- The Binational Commission should be improved by limiting the time devoted to lengthy reports by each cabinet representative and expanding the time carved out for long-range, strategic thinking.
- The Inter-Parliamentary Group should be formalized as a full-time, staffed entity.

Immigration

- Both governments must strive to level income disparities and visit the issue of open borders when wage levels between workers in the United States and Mexico narrow.
- Mexico should be treated as a special case rather than as part and parcel of overall U.S. global immigration policy.
- Members of Congress from both countries should hold special consultations to discuss immigration policy.
- The quotas for the number of U.S. professional visas granted under NAFTA are scheduled to be lifted by the year 2004, but an executive order could eliminate the quotas earlier.
- A temporary worker program should begin with workers in the agricultural sector, who constitute close to 50 percent of those apprehended at the border but only 15 percent of all illegal workers. The hospitality and hotel construction industries should have the option of contracting workers under an expansion of the current H-2A Visa Program. Businesses should guarantee fair working conditions and wages.
- Visa overstays could be addressed by (a) creating a worker and employer's registry in the U.S. Department of Labor and in the government of Mexico; (b) offering eligibility for resident alien status after working in the United States for six months of the year for five of seven years conditional upon visa compliance;

(c) using income withholding or escrow accounts in a temporary worker program.

- U.S. workers should be protected during times of economic slowdown by linking the number of visas to U.S. economic growth rates in identified sectors.
- Sensitivity to humanitarian issues, rescue procedures, and basic life-saving techniques should be part of the regular training that U.S. INS agents undergo.
- The United States has never fully staffed Border Patrol in spite of increased funding authorized by the Congress, an objective that finds support among many on the U.S. side of the border.
- Consider the proposal made by Congressman Harold Rogers (R-Ky.) to divide INS into two separate agencies: one for enforcing border regulations and one for administering the immigration and naturalization process.
- A temporary worker program should be accompanied by a serious Mexican commitment to enforcement along its national border, including its coastline and its frontiers with Belize and Guatemala.
- The U.S. government should consider declaring a moratorium on building new fences along the border.

Trade Policy

- Appoint special advisers with the authority to begin exploratory discussions regarding expanding North American cooperation, looking at options for both widening and deepening.
- Move quickly toward building a Free Trade Area of the Americas (FTAA).
- Establish a North American Customs Union, with a common external tariff.
- Promote customs efficiency at the border by exploring (a) establishing U.S. Customs Service facilities within major Mexican manufacturing areas; (b) adopting virtual customs procedures for companies that are not considered a risk for either trade fraud or drug trafficking; (c) implementing express lanes and expedited port passage credentials for precertified individuals and companies; (d) involving the private sector in the funding of border infrastructure such as expanded use of mobile X.-ray machines; (e) collecting sales tax electronically.
- Improve dispute resolution by (a) requiring the U.S. International Trade Commission to use transparency in setting technical criteria to determine dumping; (b) harmonizing competition and antitrust policies; (c) improving NAFTA arbitration panels by establishing automatic deadlines and procedures for naming arbiters and strengthening the role of nongovernmental organizations as facilitators of arbitration; and (d) improving labor and environmental standards without employing trade sanctions.

- Resolve pending trade disputes rapidly, including the sweetener dispute, agricultural quotas, and implementation of the NAFTA trucking agreement.
- Improve the compatibility of environmental protection and trade by (a) expanding the application of the successful voluntary ISO NAFTA environmental standards to small and mid-sized business; (b) compiling a bilingual database of environmental and other regulations; and (c) revising the mandate of the North American Commission for Environmental Cooperation (CEC) to permit discussion or resolution of environmental trade disputes.

Promotion of Investment and Entrepreneurship

- Direct U.S. investment in Mexico should be doubled over the next four years, with special emphasis on small and mid-sized businesses.
- The U.S. government, in consultation with Mexico, should increase funding for U.S. Agency for International Development support for micro-enterprise and micro-credit initiatives in high-immigration regions of Mexico.
- Both governments should draft standards of best practices in corporate governance and certify voluntary compliance under ISO-like procedures.
- The science and technology advisers to both presidents should bring both countries' electronic commerce standards into accord and disseminate Internet technology throughout education institutions in both countries.

Coordination of North American Energy Policy

- Current shortages and high prices of energy--including electricity, natural gas, and oil--should be addressed by production increases, facilitating direct foreign investment and liberalizing market structures in all three countries.
- The liberalization of Mexico's energy market might include encouraging foreign direct investment in upstream oil and gas exploration and production with innovative service contracts between private companies and Pemex. Companies that invest in drilling and production would be compensated with performance-based contract payments in kind or payments in cash based on the amount and market value of the hydrocarbons produced. Pemex would remain the sole owner and producer of the hydrocarbons.
- An alternative to service contracts are risk contracts, which would provide incentives for investment and would encourage companies to take a fresh look at the Mexican market.
- Developing new electricity capacity and promoting the ability to move electricity freely across the border is a high priority. Transmission lines all along the border region require upgrading, Mexico's Federal Electricity Commission's

bidding process requires streamlining and transparency to encourage investor interest.

Monetary Policy

- The issue of short-term capital mobility has been problematic. It is legitimate to explore a wide range of options for monetary policy, ranging from a common currency for North America to preserving the current free-floating system.
- Exchange-rate volatility and speculation could be inhibited *ex ante*, which is less expensive than *ex post*, by creating a North American stabilization fund in which each nation would contribute \$10 billion for a total fund of \$30 billion.
- The Treasury Departments and Central Banks of both countries should continue consultation in order to coordinate fiscal and monetary policies to the extent feasible and to seek convergence on key macroeconomic indicators.

Environmental Issues

- NAFTA institutions will need increased funding over the next 10 years to meet rapidly growing needs on the border and in Mexico's interior. Toward this end, the mandate of the North American Development Bank (NADB) should be broadened to include (a) funding infrastructure in the interior of Mexico; (b) increasing the NADB capital fund; (c) widening the range of projects it is permitted to fund; (d) increasing U.S. Environmental Protection Agency grants to the NADB.
- The North American Commission for Environmental Cooperation should be strengthened by (a) an increase of U.S. financial support; (b) compliance of Canadian provinces; (c) transparency *vis-à-vis* citizen's groups.
- Mexico's Environmental and Natural Resources Ministry (SEMARNAT) needs increased technical and financial resources from either the CEC or the United States to implement the NAFTA side accords.
- Power should be divested to the states and localities via presidential directives, for example, to authorize transboundary port authorities that can manage fees and float bonds.
- Limited water resources along the border require better management techniques, including (a) creating a binational task force to assess water supply over the next 50 years; (b) permitting the Border Environment Cooperation Commission (BECC) to assist in water conservation planning; (c) developing a water market; (d) complying with the allocation provisions of the 1944 U.S.-Mexican water treaty; (e) improving water conveyance and field water delivery systems; and (f) discouraging cultivation of water-intensive crops in this semiarid region.

- Transboundary air quality can be improved by (a) establishing International Air Quality Management Districts for the San Diego-Tijuana and Nogales-Nogales twin cities; (b) changing the U.S. Clean Air Act to enable U.S. firms operating along the Mexican border to apply for emission reduction credits elsewhere within their U.S. operations; (c) sharing baseline data on ambient air quality and point source emissions within common air sheds; (d) U.S. export promotion of firms specializing in automotive emissions testing and vapor recovery systems.
- Hazardous waste containment requires stepped-up construction of hazardous waste management facilities and technical assistance from the CEC or U.S. government.

Antinarcotics Policy

- Many Council members believe that it is time to end or substantially modify the certification process. The Bush administration could work with Congress to establish an antinarcotics protocol that would serve as a certification exemption. Bilateral negotiation and implementation of such a protocol, which would define benchmarks in cooperation, could be offered as an exemption to certification for Mexico and other interested countries.
- Practical measures to build confidence could include (a) creating a binational drug seizure committee to oversee drug seizure, warehousing, and destruction in both countries; (b) expanding the highly successful binational maritime intelligence-sharing and interdiction program to targeted land-based transit zones; (c) a joint fund to administer goods and funds captured in the drug war, which can be used for anti-drug programs in both countries; (d) stiffer U.S. penalties for arms trafficking; (e) granting permission for FBI interrogations within Mexico; (f) prompt extradition of drug dealers; (g) registration and regulation of all currency exchange operations in both Mexico and the United States.
- Political steps to build confidence include depoliticizing drug cooperation, ending Mexico “bashing,” redefining national sovereignty to recognize that drug trafficking does not respect borders.
- Intelligence sharing could increase pending (a) the creation of a small team of vetted appointees to share intelligence; (b) the adoption of common security standards for clearance; (c) the establishment of joint vetting procedures for individuals occupying a limited number of sensitive positions; (d) the creation of specialized, bilateral units to work on a case-by-case basis.
- It is essential that the United States offer any technical cooperation or resource assistance that the Mexican government might find useful in its efforts to professionalize the country’s legal and law enforcement institutions.

- The Council members were inclined toward a continued strong role for the Office of National Drug Control Policy and building on the foundations of the High-Level Contact Group, and were open as well to managing the issue through normal institutional channels, such as the Binational Commission.

Introduction

The members of the U.S.-Mexico Binational Council are pleased to present this menu of policy ideas for President George W. Bush and President Vicente Fox and the Congresses of Mexico and the United States. The Council opted not to pursue consensus from the outset, recognizing that boldness often is sacrificed in the pursuit of consensus. Thus, the ideas in this report do not necessarily enjoy the support of all the Council members and cannot be attributed to any individual member. Rather, the Council has chosen to present a broad range of policy options, leaving the task of developing consensus to the two new governments. Although not every member of the Council agreed with every idea in the report, all concurred that these proposals deserve consideration.

U.S.-Mexico Binational Council members Alfonso Romo (Pulsar) and Lorenzo Zambrano (CEMEX) determined that it would be most appropriate to withdraw from contributing in any way to discussion of North American energy policy coordination, as they have served as members of the administrative council of *Petróleos Mexicanos*. They did not participate in the substantive discussions that led to the chapter on North American energy integration, and they abstained from commenting on the final version of the chapter.

The recommendations in this report are the product of an eighteen-month deliberative effort sponsored by the Center for Strategic and International Studies (CSIS) and the University of Texas at Austin in the United States, and by the Center of Research for Development (CIDAC) and the Autonomous Technological Institute of Mexico (ITAM) in Mexico. A series of eight meetings was held, during which specialists, scholars, and policy practitioners from both countries met to share their expertise and ideas. Recommendations generated in the working sessions were then presented to the members of the Council for evaluation, approval, and additional substantive input. This report does not pretend to be exhaustive; the Council intends to continue to contribute to the policy debate in the years to come. It is the Council's hope that its members will serve as permanent, informal goodwill ambassadors and points of communication between our two nations.

A preliminary draft of this report was provided to the White House and to Mexico's Los Pinos in preparation for the first meeting between Presidents Bush and Fox on February 16, 2001, in Guanajuato, Mexico, providing both administrations with the opportunity to move forward on some of the recommendations outlined in the report. Given the integral importance of the legislatures of both the United States and Mexico to advancing the bilateral agenda, CSIS and ITAM were honored to have been asked by their respective Congresses to present a draft of the U.S.-Mexico Binational Council report at the 40th annual Inter-Parliamentary Group Meeting in May 2001.

General Principles

The election of new presidents in both Mexico and the United States offers a unique opportunity to explore the parameters of the possible. The first principle that should guide the two presidents is that nothing should be off-limits for discussion—from joint law enforcement operations to open borders.

Second, President George W. Bush and President Vicente Fox should decide on an overarching strategy for managing bilateral relations. All previous administrations have delinked and compartmentalized the numerous issues on the agenda in order to prevent contaminating the entire relationship when conflict emerges in any particular area. However, the two administrations may wish to consider whether a package approach—one that identifies trade-off opportunities across the entire bilateral agenda—offers greater promise.

Third, both countries should seek the Canadian perspective on the evolution of policy, as well as look for opportunities to involve citizens' groups, businesses, and nongovernmental organizations.

Fourth, all members of the Council agreed that leveling social disparity between the two countries should be a principal policy objective. The greatest challenge facing Mexico today is the need to fight poverty, and the United States has a stake in boosting Mexican social development, given that many of the problems plaguing bilateral relations have their origin in the gap between living standards in the two countries. Many members of the Council advocated a significant commitment from the United States and Canada to provide financial resources for Mexico's efforts in dealing with poverty reduction, the environment, and infrastructure improvement.

Finally, the two new governments should spark momentum in bilateral relations by identifying obvious targets for rapid progress. Among these targets should be the following:

- Swift resolution of remaining trade disputes;
- Establishment of hot-line links between President Bush and President Fox and between other sensitive cabinet posts;
- A joint commitment to fund Mexican microcredit initiatives;
- Appointment of special advisers empowered to begin exploratory discussions in an effort to broaden and deepen the parameters of North American cooperation;
- Expansion of the successful binational maritime intelligence-sharing and interdiction program to three carefully targeted land-based transit zones;

- Creation of a small binational committee of congressional leaders to explore options for legal immigration; and
- Agreement on implementing “virtual customs” procedures for carefully selected manufacturing sectors and border-crossing points within one year.

Management of Bilateral Relations

Relations between Mexico and the United States could be enhanced considerably by improving and expanding direct contact between the governments of the two nations. A variety of approaches can achieve this goal.

Hot-Line Contact

The hot-line telephone link between former secretary of state Madeline Albright and former foreign minister Rosario Green helped both foreign policy chiefs to defuse fast-breaking tensions. The concept might be expanded to include the Oval Office of the White House and Los Pinos, thereby sending an emphatic message about the priority of bilateral affairs. Hot-line links could be established in other sensitive areas of bilateral relations as well, in particular, between the offices of the two attorneys general and the secretaries of the treasury.

U.S. "Enforcer"

President Bush should address the inefficiencies and conflicting goals of the sprawling federal bureaucracy by empowering a key individual to ensure that U.S. federal agencies are singing from the same song sheet and avoid interagency quarrels that send mixed signals to Mexico. That individual should operate out of the White House and be assured privileged access to the president. Serious consideration also should be given to empowering this individual to oversee the U.S.-Canada relationship. Options include the following:

- **THE PRESIDENT'S CHIEF OF STAFF OR DEPUTY CHIEF OF STAFF.** The president should task one of these individuals with a Mexico "watching brief." Cabinet officers and their senior staff would know that this person could arbitrate conflicting agendas or if necessary could convey concerns directly to the president. The same functions would also apply with respect to Canada.
- **A SPECIAL ASSISTANT/SENIOR DIRECTOR FOR NORTH AMERICA ON THE NATIONAL SECURITY COUNCIL.** By splitting off Mexico and Canada from the special assistant/senior director for Western Hemisphere Affairs, the new incumbent would have the time to follow trilateral developments and border affairs more closely.
- **A SPECIAL ENVOY TO MEXICO, WITH A COUNTERPART ENVOY TO CANADA.** The valuable performance of Thomas "Mack" McLarty as special envoy to the

Americas during much of the Clinton administration can inspire consideration of a similar position to work with Mexico.

Permanent Structuring of the U.S.-Mexico Inter-Parliamentary Group

The U.S-Mexico Inter-Parliamentary Group (IPG), which has been meeting once a year since its founding in 1961, has been an effective vehicle for relationship building among members of Congress from both nations. The two Congresses play an important role in bilateral issues such as drugs, immigration, border infrastructure, and energy policy and therefore should engage in more consultation on legislation that has bilateral implications. The IPG has been plagued in the past by ad hoc participation by U.S. members of Congress, in part, in response to the relative weakness of the Mexican legislative branch—attributed to its uneven partisan distribution and the perpetual turnover of Mexican legislators due to the prohibition of consecutive reelection. Thus, the IPG has not realized its full potential as a forum for binational policymaking. The current structure of the IPG has not kept pace with the maturing of the Mexican Congress which is now more independent and plays a greater role in policymaking. The IPG should enhance communication and collaboration between the legislative branches of each country on a year-round basis.

We suggest the following improvements:

- Serious consideration should be given to relocating the IPG meetings to Washington, D.C., and to Mexico City in the hope that it would be easier for members of Congress to participate.
- The continuity of the dialogue should be enhanced by the addition of two meetings, one in September and one in January, in which single issues would be given more in-depth treatment. Each delegation would choose the theme of discussion for one of the meetings.
- The IPG cochair should solicit the participation of the committee chairmen and ranking members of each subcommittee.
- In the U.S. Congress, the senior foreign policy advisers from the offices of the Majority Leader and Minority Leader in the Senate and the Majority Whip and Minority Whip in the House should attend at least the annual IPG meeting. Within the Mexican Congress, each party's senior staff member from the Parliamentary Coordinating Office should attend.
- The IPG should devise an action plan at each annual meeting that includes a time line for completion, laying out a series of legislative or internal IPG objectives.

Border Management

Border issues affect millions of Mexicans and Americans along the 2,000-mile frontier; and high-profile problems, such as drug trade and migration, can affect millions more beyond the border.

The last decade has witnessed an explosion of organizations and mechanisms to address these problems. Both governments have committed to goals enumerated in the Border XXI plan, which was born out of the 1983 Agreement for the Protection and Improvement of the Environment in the Border Area (La Paz Agreement) and is a cooperative effort to protect, improve, and conserve the environment of the border region. The two federal governments meet regularly to review the adequacy of bridge and border crossings, inviting state and local governments to participate. The border liaison mechanisms (BLMs) located at major crossings have become important venues for consular offices, federal agencies, and local law enforcement to resolve problems locally without deferring to each country's respective capital. The North American Development Bank (NADB) is addressing pollution and infrastructure issues. Semiannual meetings of border governors and border attorneys general have strengthened state-to-state links. In the U.S. Congress, the Border Caucus supports funding for these initiatives and occasionally blunts the excesses of "Mexico bashing" by its congressional colleagues. The Mexican Chamber of Deputies, with a more formal committee structure, has similar interests.

These border-related institutions serve to enhance dialogue and advance solutions to bilateral border problems; they do not, however, coordinate effectively with each other or with their federal governments. Moreover, Mexico has named a border czar to enhance its own border policies, and clearly would like to see the appointment of an interlocutor for border affairs in the United States. Similar efforts under the Clinton administration included the proposal of a "border czar," by the drug czar's office at the Office of National Drug Control Policy (ONDCP) and the Southwest Border Initiative, overseen by former attorney general Janet Reno. However, turf battles hindered success, and the focus has been exclusively on law enforcement. To improve cross-fertilization and thus strengthen border efforts, the new U.S. administration should consider the following:

A State Department Deputy Assistant Secretary (DAS) for Border Affairs

A State Department deputy assistant secretary (DAS) for border affairs could be created. The head of the State Department's Border Affairs Unit is a senior officer within the Office of Mexican Affairs. The incumbent must coordinate with a broad cross-section of federal agencies, state governments, the White House, and Congress and must deal with similar organizations in Mexico. Clout counts, and a better title would help. Such a step would require some reordering of DAS-level portfolios in the Bureau of Western Hemisphere Affairs (which now includes Canada).

Border Affairs Principals Group

A Border Affairs Principals Group within the National Security Council (NSC), similar to groups that meet on major foreign policy issues, could review major border developments. A Principals Group, chaired by the national security adviser and including the White House Intergovernmental Affairs Office, would put all agencies on an equal footing.

Border Governors

The frequency of exchanges between the border governors and the federal government should be increased. Personal contact between authorities on either side of the border is essential. Right now, only the State Department's Border Affairs unit represents the administration at the border governors and border attorneys general meetings. The White House's Intergovernmental Affairs Office should also attend. Each border state also should be invited to send an observer to the annual Binational Commission meeting (BNC).

U.S.-Mexico Binational Commission

The Binational Commission (BNC) has been the crown jewel of the bilateral relationship since its creation in 1981. Many constructive and practical ideas have emerged over the years. However, the BNC has grown in terms of both the number of agencies participating and the number of officials attending. There are 15 working groups and several subgroups involving almost all cabinet-level departments and agencies. A reduction in the number of working groups and some tinkering with the format of the BNC would be in order to give the senior participants more time to focus on the overall state of the relationship.

- The time devoted to lengthy reports by each cabinet representative should be shortened. Each BNC working group already prepares a written report on its results; the reports do not need to be read in the plenary session. Instead, the cabinet principals, each accompanied by only one staff member, could meet in relevant clusters to review the achievements of the working groups and designate one or two officials from each side to make a final oral report to the plenary.
- There needs to be better opportunity for an overall review of bilateral political relations. The Bilateral Working Group is currently charged with that task, but it ends up focusing primarily on technical border problems. Although the senior State Department and Mexican Foreign Ministry (SRE) officials who chair this meeting do meet to review the overall status of the relationship, they should carve out time to focus on a more political report for their respective cabinet secretaries.
- The BNC has little opportunity for strategic thinking because of the focus on "deliverables." It might be useful to task several working groups with long-range strategic planning about issues such as border transportation or the environment. A dialogue between the two governments six months before the BNC meeting could identify topics and task their relevant agencies with identifying the parameters of such an effort.

Immigration

Demographic experts agree that the immigration equation today is fundamentally different from what it was during the 1980s and the early 1990s, when profound economic distress in Mexico led to dramatic increases in immigration levels. Today, changing demographics and positive economic scenarios in both countries suggest that the moment is propitious for a new approach to immigration policy, although this panorama would change with an economic downturn in the United States.

Population growth in the United States is now below the labor replacement level, creating unprecedented low unemployment rates and a real need for foreign workers in certain sectors of the U.S. economy. The attitude of U.S. unions, moreover, has become receptive toward immigration, calling for an amnesty of illegal aliens currently in the United States and an end to sanctions against employers who knowingly hire these aliens. Federal Reserve chairman Alan Greenspan has recognized the role of immigration in lessening inflationary pressures in the United States. Immigration is modifying the dynamics of ethnic politics, ending the days when U.S. politicians played upon fear of immigration for electoral advantage.

In Mexico, job creation over the past four years has grown at approximately 700,000–800,000 jobs a year, close to the overall growth of the economically active population (EAP), with formal manufacturing jobs growing at 9 percent a year. Rather than the skyrocketing immigration rates of the 1980s, the United States is experiencing stable flows of around 300,000 legal and illegal permanent Mexican migrants yearly. Mexico's population authorities estimate an approximate growth of the economically active population at 900,000 a year for at least the next 5 years and probably beyond 10 years. There is some reduction expected in the 15–40 year-old age cohort in Mexico in 10 years, which could suggest a decline in immigration.

Immigration policy has not caught up with new realities and is torn between economic integration on the one hand and immigration restriction on the other. This has resulted in over 300 deaths a year, as Mexican immigrants risk their lives to enter the United States illegally, at isolated, desert portions of the border. It also has resulted in disruptions of local U.S. communities due to disorderly population flows. It is against this backdrop of enhanced economic integration, an increasing U.S. need for immigrants, and growing U.S. enforcement efforts that the Council offers the following thoughts and options.

Migration and Temporary Worker Programs

In general, the members of the Council agreed that orderly, legal immigration is preferable to disorderly, illegal immigration and can provide benefits for both governments as well as for their citizens. Therefore, several fundamental principles should guide all considerations regarding immigration policy.

Free Movement of Labor

Vicente Fox has set free movement of labor within 25–35 years as a long-term goal. The idea tends to raise eyebrows in Washington, D.C., where the U.S. Congress has been unable to agree even on limited programs. The relationship between the United States and Mexico will never reach its full constructive potential until incomes and career opportunities in Mexico rise sufficiently to lessen the economic disparities between the two countries. Therefore, both governments must agree in principle to do everything possible to reduce those disparities and to revisit the issue of open borders as soon as the differences in wage levels between workers in the two countries narrow. Also, in the absence of full labor mobility, it should be recognized that capital will continue to migrate to Mexico to take advantage of a cheaper labor force, while the United States will continue to face the high administrative costs of enforcing controls across the border.

Mexico as a Special Case

In setting immigration policy, the United States tends to treat Mexico as part and parcel of overall global immigration, not as a neighboring country with a common border. Joined by geography, Mexico and the United States share a long history and, under NAFTA, an economic relationship that might serve as an umbrella to justify expanded policies for the exchange of labor. The economic realities of the relationship have instilled a sense of urgency to negotiate a bilateral migration agreement.

Congressional Policymaking

Because the U.S. Congress determines the country's immigration policy, it may be useful to members of the legislatures from both countries to hold special consultative meetings to discuss immigration policy under the aegis of the IPG.

Executive Orders

Both governments should explore immigration policies that can be implemented by executive order. For example, in the United States, the quotas for the number of professional visas granted as part of NAFTA are scheduled to be lifted by the year 2004, but an executive order could eliminate the quotas earlier.

Benefits of a Temporary Worker Program

The benefits of an ambitious program of allowing temporary workers to enter the United States in a legal and regulated fashion include the following:

- Returning order to the U.S.-Mexican border;

- Protecting the human rights and safety of those who are currently trying to cross the border illegally;
- Meeting the labor needs of a growing U.S. economy; and
- Strengthening labor rights for all workers who are part of the U.S. economy by reducing the ability of employers to exploit underground employment.

Many Council members from the United States believe that a temporary worker program should be accompanied by improved U.S. vigilance over illegal immigration and a serious Mexican commitment to enforcement along its national border, including its coastline and its frontiers with Belize and Guatemala. A temporary worker program also should guarantee that temporary workers do not compete with or degrade the wage standards of U.S. national workers. The Council recommends that particular attention be paid to the following issues when setting immigration policy:

- **TEMPORARY AGRICULTURAL WORKERS.** Any temporary worker program should begin with workers in the agricultural sector, who constitute close to 50 percent of those apprehended at the border but only 15 percent of all illegal workers. Regulating these workers would immediately relieve pressure on border enforcement.
- **TEMPORARY WORKERS IN SERVICE INDUSTRIES.** There is a critical shortage of labor in seasonal services, such as in Arizona's travel and tourism sector. Companies engaged in the hospitality and hotel construction industries should have the option of contracting workers for specific projects or for specified services at their hotels, a principle that might apply under an expansion of the current H-2A Visa Program (a temporary worker program). The concept should include guarantees of fair labor conditions.
- **A REGIONAL APPROACH.** The border should not be treated as a homogeneous area. Pilot programs could be tailored to regional specifications, which has been done in Arizona and Sonora, the fastest-growing integrated cross-border region. There, a reciprocal agreement has been designed to expand the enforcement perimeter from 25 to 75 miles for defined categories, such as business travel, in recognition of expanded trade. There is room for additional creativity in variables such as fees and length of stay.
- **A SECTOR APPROACH.** The United States should conduct an inventory of job needs and identify with precision those sectors unable to meet their needs in the domestic job market. Precise economic sectors with clearly defined temporary labor requirements could be identified, and visas targeted to those sectors, as has occurred with certain agricultural activities in states such as Georgia.
- **VISA OVERSTAYS.** The U.S. government should design such programs in cooperation with Mexican government officials in order to ensure the program's success and to prevent visa overstays. Several tools can be employed to ensure that Mexican temporary workers and U.S. employers abide by the rules.

- *Worker registry.* A registry should be created in which employers would report their activities to the U.S. Department of Labor and Mexican visa applicants would register with the government of Mexico. One successful model to emulate might be the seasonal agricultural worker program that Canada has established with Mexico, which currently involves approximately 10,000 workers. The Mexican government actively participates in the Canadian program by maintaining a registry of workers and sending them to Canada.
- *Eligibility for resident alien status.* Incentives to abide by the rules could include eligibility for temporary workers to apply for resident alien status (commonly referred to as a “green card”) after working in the United States for six months of the year for five of seven years.
- *Income withholding/escrow accounts.* Including a savings withholding component in a temporary worker program would improve visa compliance, provide an incentive to return to Mexico, and lessen the high costs that migrants currently incur when they send home their wages via commercial delivery and wire services. One model that should be considered is the program between Canada and some Caribbean nations, in which the employer/employee contract includes a 25 percent holdback, which is remitted to the government agent within each pay period. In the case of foreign governments, a small percentage of the 25 percent is not returned to the worker and is used to defray administrative costs. These funds can also be used to repay any outstanding loans the worker might owe his or her employer. Workers would only be able to gain access to such funds following their return to their home country. It therefore serves as an incentive not to relocate permanently. Some Council members were concerned that such a withholding scheme is a confiscatory intrusion on workers' salaries and could create disincentives for participating in a visa program.
- **POSSIBLE DRAWBACKS.** In evaluating the feasibility of the proposed temporary worker program, a number of issues must be taken into account.
 - *Protecting U.S. workers during times of economic slowdown.* Mexican workers generally are not competitive with U.S. workers in sectors like agriculture, even during periods of U.S. economic slowdown. Any expansion of temporary worker programs to the service and construction industries, however, may want to consider linking a variable number of visas to U.S. economic growth rates in identified sectors. Moreover, the wage levels of previous immigrant cohorts may be affected, depressing earnings in certain skill categories.
 - *Size of the program.* The reality of the numbers of people involved needs to be considered. Each year, there are an estimated 150,000 to 170,000 net unauthorized additions to the permanent U.S. Mexican population residing in the United States. The number of visas offered would have to be quite high in order to have a significant impact on deterring migrants from crossing the border illegally. Some Council members suggested that these

estimates are too high and that there is no evidence that the yearly increases would be cumulative.

- *Labor rights.* Businesses that use contract labor should guarantee fair working conditions and wages. Applying the same standards equally to both domestic and immigrant workers would eliminate any cost advantage in hiring immigrants because of less stringent standards. Consequently, the legal protection and safety resulting from legalization of temporary workers not only strengthens the rights of immigrant workers but also increases the competitiveness of domestic labor, by reducing the incentive to exploit cheaper and unregulated labor.

Humanitarian Issues

Making legalization of Mexican immigrants the norm may help to promote their safety by rerouting them away from desert and ranching areas to legal ports of entry. The decision of thousands of Mexicans to risk their lives by crossing the border illegally has resulted in a dismaying increase in deaths not only from drowning and desert dehydration but also from violent encounters with border ranchers eager to protect their property rights, particularly the destruction of their cattle and fences and drainage of their water. In addition, sensitivity to humanitarian issues, rescue procedures, and basic life-saving techniques should be emphasized as being as important a part of the regular training that U.S. Immigration and Naturalization Service (INS) agents undergo as is their primary task of securing the U.S. border with Mexico. Immigrants should have no reason to fear harassment, physical harm, or discrimination.

Migration Amnesty

Opinions differed on whether or not it is time to grant another general amnesty to Mexican immigrants currently residing in the United States. Council members who were opposed to amnesty argued that it tends to perpetuate future flows of illegal immigration. Opponents also point out that amnesty undermines the rule of law and is inherently unfair to the individuals who are seeking entry through legal means. Those supporting this proposal pointed out that granting amnesty means immediate access to minimum wage and other labor rights for previously unprotected populations.

Enforcing an Orderly Border

Reliable enforcement of U.S. border regulations, a reduction in illegal immigration, and a commitment on the part of Mexican authorities to assure orderly population movement are essential components of any immigration policy that contemplates expansion of legal temporary migration. The Council encourages the two governments to experiment with innovative models of border enforcement that compliment the so-called Green Line Model, which emphasizes a policy of containment. A number of options follow.

Full Funding and Staff for the U.S. Border Patrol

The containment model has not yet succeeded in reducing the number of illegal border crossings. This method requires an estimated minimum of 15,000 agents to control land-based crossings. The United States has never fully staffed the Border Patrol to test the effectiveness of the model. In spite of increased funding authorized by the U.S. Congress, the INS has failed to meet its recruitment goals for the U.S. Border Patrol, an objective that finds support among many on the U.S. side of the border

Cooperation in Fighting Organized Crime

Both governments should experiment with improving binational police intelligence sharing and cooperation at the state and local level to attack the organized trafficking of human beings and drugs. Minor adaptations to innovations in police procedures can have a major impact on crime, as was demonstrated by the Arizona and Sonora initiative, in which a joint police effort improved the law enforcement capabilities in both localities.

Structure of the INS

The Bush administration should seriously consider the proposal by Representative Harold Rogers (R-Ky.) to divide the INS into two separate agencies: one for enforcing border regulations and one for administering the immigration and naturalization process. Some Mexican Council members expressed serious reservations about having border enforcement be the responsibility of an organization whose mandate is strictly based on law enforcement.

Impeding the Flow From Mexico

The Fox administration has denied the constitutional argument that the federal government cannot take an active role in preventing movement of Mexicans across the border region. At a minimum, Mexico can step up its enforcement efforts against organized criminal rings that traffic in migrants and better monitor well-known staging areas on the Mexican side of the border. Some Council members believe, however, that a democracy should not control the exit of its citizens.

Employer Sanctions

The enforcement of sanctions on employers who knowingly hire illegal workers—in accordance with the Immigration Reform and Control Act of 1986—has never been fully implemented. It is inconsistent to place greater emphasis on enforcement along the border while placing less emphasis on internal enforcement within the U.S. workplace. Enhanced enforcement of workplace sanctions can be useful in combination with an effort to legalize temporary workers.

Securing All Borders

The two administrations should immediately, in collaboration with Canada, begin consultation on the development of agreed policies and practices for the securing of

their respective borders. These policies should aim to eliminate all illegal immigration into North America. Currently, almost half of the undocumented aliens in the United States are estimated to come from places other than Mexico. Mexican labor markets cannot gain the hoped-for strength if undocumented migrants flood into, and across, Mexico from elsewhere in Latin America, the Caribbean, Asia, and the Middle East. The same holds true for undocumented migration into Canada. Thus, there is common interest in eliminating pass-through immigration from both Mexico and Canada. In addition to the border region, the Mexican, Canadian, and U.S. governments should investigate the possibility of expanding cooperative enforcement efforts in the airports of the three countries.

Moratorium on Construction of New Barriers

Some Mexican members of the Council expressed their hope that the U.S. government would consider declaring a moratorium on building new fences along the border while a binational review of immigration policy is under way.

Immigration and Economic Development

The causes for Mexican migration are varying, according to a study conducted by the National Population Commission (CONAPO) in 1999. The only lasting solution to the problem of illegal Mexican immigration into the United States, however, is to strengthen Mexico's economy and the employment opportunities within the country. A high priority should be placed on achieving rapid Mexican economic growth over the course of several decades to promote labor absorption in Mexico. But growth alone is not enough. The way in which growth occurs matters as well. What is needed is redistribution of gains made from Mexican economic development and a restructuring of regional labor markets.

Mexico's Labor Market

Mexico's labor market has a distinct north-south bias, which must be restructured. To achieve this goal, the Mexican government should take steps in following areas:

- **EMPLOYMENT RECRUITMENT.** Employment recruitment within Mexico should be improved. Jobs go unfilled in regional cities like Guadalajara, as local residents look northward for employment rather than homeward. Better advertising of job opportunities in Mexico by both government and the private sector should be explored as one of the possible solutions.
- **TRANSPORTATION INFRASTRUCTURE.** As much effort should be devoted to developing the country's internal east-west transportation infrastructure as has been done along the north-south transportation corridors. The NAFTA highway also should be improved. Specifically, the Lagos-San Luis Potosi portion needs to be four-lanes wide to provide a faster response to U.S. market needs.
- **TARGETED INVESTMENT AND EMPLOYMENT STRATEGIES.** Investment and employment strategies (along the lines of those suggested in chapter 6, Invest-

ment and Entrepreneurship) should be developed for states that have high outmigration numbers.

- **EDUCATION.** Mexico is currently facing a short supply of high-skilled workers, which is a key constraint facing large companies contemplating investing in Mexico. Resources devoted to education and training of the Mexican labor force should, by themselves, induce more capital inflows into Mexico and faster economic growth. President Bush is especially interested in setting clear educational standards for U.S. schools, an effort that could be expanded to all of North America, especially in harmonizing professional accreditation and licensing in the sciences and technical training. Educational policy should be designed to take into account Mexico's manufacturing needs.

Trade Policy

Steps after NAFTA

There are two schools of thought regarding the future of NAFTA. The first emphasizes widening or expanding free trade to other countries in Latin America in order to create a Free Trade Area of the Americas (FTAA). The second focuses on deepening NAFTA along the lines of the European Union, including intensifying the integration process along new, nontrade dimensions. These two models need not be mutually exclusive, and Council participants were interested in combining different elements from both models, as detailed in the following recommendations.

NAFTA Deepening

The two new presidents should appoint special advisers with the authority to begin exploratory discussions regarding the potential for expanding North American cooperation. Vicente Fox has advocated the deepening of NAFTA as a policy goal and has referred to the European Union model as a possibility in this regard, including the creation of a social development fund and open borders. It is not yet clear whether the European model or the deepening of NAFTA are of interest to Mexico's NAFTA partners. Some U.S. participants on the Council expressed reservations about deepening NAFTA along EU lines, given the tendency of Brussels institutions to exert a heavy regulatory hand on business, intrusive labor policies, and expensive social programs. All agreed, however, that NAFTA is a positive step in the direction of increasing economic, social, and cultural integration among the North American countries and remained open to new ideas for North American cooperation.

A Free Trade Area of the Americas

Most U.S. participants on the Council strongly supported the formation of an FTAA. They called on President Bush to seek the rapid renewal of trade promotion authority (TPA) to negotiate free trade agreements and on the U.S. Congress to grant that authority. Some Mexican participants expressed ambivalence, suggesting that Mexico would lose its NAFTA preferences both in the U.S. market and with other countries with which it has bilateral free trade agreements. Moreover, the rules of origin enshrined in NAFTA are not appropriate for application to other Latin American countries. Other Mexican participants, however, expressed confidence in Mexico's ability to successfully take advantage of liberalized hemispheric trade.

A North American Customs Union

A natural next step that follows from NAFTA would be to establish a common external tariff vis-à-vis the rest of the world. This option could raise thorny questions about how Mexico and the United States would handle their existing non-NAFTA free trade agreement commitments. The transformation of NAFTA into a customs union would change the rules of the game for the FTAA, as the whole of North America would have to negotiate as a block. Current FTAA negotiations are not consistent with the scheme of a customs union.

Customs Efficiency to Facilitate Passage at the Border

Borders add hidden but substantial costs to trade. For example, the European Union estimates that the cost of having borders constitutes about 2 percent to 3 percent of a given country's gross domestic product. The slowness of customs at the U.S.-Mexican border is a bottleneck that adds significant costs—in time as well as money—and therefore represents a de facto nontariff barrier. Several approaches can be adopted to facilitate commercial flows along the border without compromising drug interdiction or customs collection, as the proposals below make clear. In fact, separating the legitimate commercial trucking flow from higher-risk traffic would improve both the customs and the drug inspection processes.

In-Country Customs

U.S. Customs Service facilities should be established within major Mexican manufacturing clusters, such as Guadalajara, Monterrey, and Mexico City. These facilities would bond and seal containers after on-site inspection, and the containers could not be opened until they arrive at their U.S. destination.

“Virtual Customs” Procedures

Processing customs electronically is a viable option for companies that have a well-established reputation and are not considered a risk for either trade fraud or drug trafficking. The automobile industries in the United States and Canada already have automatic procedures in place for processing customs electronically, and the United States could duplicate this system at its borders with Mexico.

Standards of Best Practices in Corporate Security

For over 15 years, the U.S. Customs Service's Carrier Initiative Program (CIP) has been working in cooperation with the private sector to combat the transport of illegal drugs into the United States by way of air, sea, and land. A private sector initiative, begun in 1996, is the Business Anti-Smuggling Coalition (BASC), a Customs-supported alliance. Because a contributing factor to bottlenecks at the U.S.-Mexico border is the time involved in searching land carriers for drugs or contraband, programs such as the CIP or the BASC not only work to augment antinarcotics efforts, but also are useful in facilitating movement at the border. Mexico, which recently inaugurated its first Mexican BASC chapter in Monterrey in

March 2001, should consider providing incentives for companies that participate in the BASC, thus encouraging more Mexican companies to capitalize on the expedited inspection procedures applied to BASC-certified companies.

Border Infrastructure and Expedited Port-of-Entry Passage

Credentials could be issued to precertified individuals and companies, allowing them to pass through an express lane without inspection. The Sentri system currently in place in San Diego and Tijuana should be expanded to include other border crossings. The modernization and growth in number of all ports of entry should be accelerated. Expanded use of mobile X-ray machines at the border, for example, can facilitate legitimate commercial trade. Businesses could be persuaded to participate in funding improvements to the infrastructure, because of the savings realized through efficiency at the border would reduce the cost of doing business. This is not without precedent; in Juarez, for example, truckers and *maquilas* pay a “contribution” to fund bridges, and the private sector helped fund the Sentri system of bar-coded decals for precertified passage between Tijuana and San Diego.

Sales Tax

Sales taxes could be collected electronically at a later time, rather than at the border at the time of passage.

Dispute Resolution

With expanded trade comes an increase in the number of disputes and a need to find innovative ways of dealing with them. Dispute resolution—be it between the two governments or within the private sector—should be improved along the lines noted below.

Antidumping and a Common Competition Policy

Because Mexican businesses feel strongly that U.S. antidumping policy has been used as a nontrade barrier, the International Trade Commission must demonstrate transparency in setting the technical criteria used to determine the definition of dumping. The ultimate goal of the working groups created under NAFTA (Article 1504) is to eliminate dumping laws and to introduce a common competition policy, to avoid the protectionist use of dumping in the region. The United States, Mexico, and Canada should work to establish uniformity or, at a minimum, consistency in their competition policies.

Labor and Environmental Standards

Even though all Council participants agreed that it is important to improve labor and environmental standards in both countries, none believed that trade sanctions are a constructive way of enforcing these standards.

Arbitration

NAFTA panels will work more efficiently by establishing deadlines and automatic procedures for naming arbiters. For example, efforts to resolve the trucking and sugar industry disputes were grossly delayed because of failure to name panel members. Moreover, not all disputes require arbitration under NAFTA. The two governments, along with Canada, could strengthen alternatives by taking the following steps:

- Strengthen the role of third-party nongovernmental organizations as hosts to and facilitators of arbitration.
- Increase awareness of the availability of such mechanisms.
- Create a clearinghouse of U.S. arbitration associations.

Pending Trade Disputes and Barriers to Trade

A strong push on the part of the two new administrations to resolve lingering trade disputes would lend momentum to the NAFTA paradigm. Current trade disputes result in negative publicity that is disproportionate to their limited economic significance. Taking the following steps could help to eliminate these problems.

NAFTA Trucking Provisions

Now that an arbitration panel has ruled in favor of Mexico, the U.S. government should immediately implement trucking provisions that are currently a part of NAFTA, providing the requisite augmentation of the staff required to monitor uniform compliance with safety and environmental standards.

The Sweetener Dispute

Both governments should try to resolve rapidly the NAFTA side agreements on sugar trade, which provided for U.S. fructose to be permitted into Mexico without restriction, supposedly in exchange for the entry of Mexico's exportable surplus sugar into the United States without quotas.

Agricultural Quotas

The U.S. government should eliminate import restrictions on products (such as tomatoes, oranges, and avocados) that deny American consumers access to low-cost, high-quality Mexican produce. The cultivation of these agricultural products in the United States is dependent on employment of Mexican labor, thus contributing to the migration of Mexican workers.

Environmental Trade Disputes

The tuna-dolphin controversy points to the need for a forum in which trade issues with environmental components can be discussed prior to coming before a World Trade Organization (WTO) panel. The mandate of the North American Commis-

sion for Environmental Cooperation (CEC) should be revised to permit discussion or resolution of environmental trade disputes using scientific data.

Database of Regulations

Both the U.S. Department of Commerce and Mexico's newly created Ministry of the Economy should compile a bilingual database of environmental and other regulations, which vary state by state in the United States and, in Mexico, can create obstacles to investment.

Environmental Standards for Industry

The governments of both nations should expand the highly successful voluntary ISO NAFTA environmental standards to business associations that serve small and mid-sized industries.

Promotion of Investment and Entrepreneurship

Increased U.S. investment in Mexico would be beneficial to both countries. The Bush and Fox administrations should seek to double U.S. foreign direct investment, with special emphasis on U.S. small and mid-sized businesses. As a complement to purely private investment, a substantial commitment to support microcredit and microenterprise initiatives on the part of the U.S. federal government—managed principally through the U.S. Agency for International Development (USAID)—would be consistent with the entrepreneurial values of both nations, would contribute to promoting social development in Mexico, and may slow immigration by generating employment opportunities in Mexico.

This recommendation reinforces the NAFTA commitment and is a significant shift from past policy. Mexico previously rejected U.S. foreign aid out of concern for the conditionality that might accompany such assistance, while the United States emphasized trade, not aid. Some Mexican members of the Council continue to harbor concerns about the implications to Mexican sovereignty of oversight of USAID or other U.S. government spending programs in Mexico by the U.S. Congress and the U.S. General Accounting Office (GAO). Others—from Mexico as well as the United States—asserted that the most enduring development strategy is expanded trade and investment, not aid. Below are steps in the area of investment and entrepreneurship that would help achieve the objective of leveling social disparities.

Microcredit and Microenterprise Funding

Mexico has an interest in capitalizing on the entrepreneurial energy of its society, especially among the poor, while the United States is interested in seeing entrepreneurship and credit opportunities expand in the poorer sectors of Mexican society, whose inhabitants are most likely to migrate. Currently, Mexico constitutes a very small portion of USAID's \$150-million global microenterprise program. Therefore, the U.S. government should make an effort to substantially increase funding for USAID programs supporting microenterprise and microcredit initiatives in high outmigration regions of Mexico. These programs should be developed in consultation with the Mexican government and in coordination with World Bank and InterAmerican Development Bank initiatives.

- **TARGETED FUNDING.** Microcredit and microenterprise funding should be targeted to promote the start-up of suppliers for pre-existing industries already

operating out of Mexico. This will make possible the supply of inputs in-country.

Small and Mid-Sized U.S. Businesses

A greater effort should be made to expand direct U.S. investment in Mexico by small and mid-sized businesses, with the Small Business Administration (SBA) and the U.S. Department of Commerce taking the lead in this effort. Council members representing the U.S. business sector believed that an Overseas Private Investment Corporation (OPIC) agreement with Mexico would facilitate small and mid-sized business investment, although large companies should acquire their insurance privately. Mexican participants expressed reservations about OPIC because of concern regarding the legal right to collect debts to a U.S. government agency.

Corporate Governance

Both governments should draft standards of best practices in corporate governance and encourage the formation of an entity that would certify voluntary compliance, similar to ISO procedures. A NAFTA standard of corporate governance would increase investors' confidence. The market can enforce the standards, which should include the promotion of transparent accounting practices and protection for the rights of minority stockholders.

The Digital Divide

The emerging technological and telecommunications gap between the two countries must be narrowed. Council members expressed concern about the potential consequences of the digital divide, ranging from deepening social inequalities to a general loss of efficiency in Mexico's public and private sectors as well as inability for Mexico to conduct international business. The science and technology advisers of both new presidents should convene experts from the private sector to design a program that would bring both countries' electronic commerce standards into accord and would disseminate Internet technology throughout educational institutions in both Mexico and the United States. Some Council members feel that Mexico's efforts at bridging the digital divide would be facilitated if they were to sign the Information Technology Agreement (ITA), an agreement under the WTO eliminating import duties on information technology products. Mexico would thereby join the United States, Europe, Japan, India, China, and over 40 other IT nations.

Coordination of North American Energy Policy

Adequate supplies of oil, natural gas, and electricity are essential to the economic well-being of the North American market. It is necessary to integrate more fully the North American energy market to take advantage of the complementary capabilities of all three countries. This is a mutual interest of the three countries, as illustrated by the current scarcity and high price of natural gas, which is hurting Mexican and Canadian industry; the current scarcity and high price of electricity, which is hurting California, and the high price of oil, which is hurting the global economy. The recommendations in this chapter address critical issues in the four areas of oil, natural gas, petrochemicals and electricity.

An Energy Overview of Mexico

It is widely recognized among many Mexican and international energy experts that if current supply and demand trends continue, Mexico risks an energy crisis of its own in five to seven years. The Fox administration ranks energy policy as among the top issues on its agenda. The Mexican Constitution assigns the state-owned Petróleos Mexicanos (Pemex) a monopoly over production of oil and gas, refining, and firsthand sales, making this sector highly sensitive politically. Pemex is the single most important entity in the Mexican economy, contributing 37 percent of the federal government's revenue in 2001.

Mexico may well be able to attract new investment within its existing legal framework, meaning that the State would retain its current tight control of Pemex and the Federal Electricity Commission (CFE). It should be remembered, however, that investors are not neutral to the different schemes being considered to attract private investment and prefer greater liberalization to maximize investment flows and efficiency gains. To date, Mexico's energy policy has focused on expansion of the natural gas market and reducing reliance on fuel oil. Since reforms were implemented in 1995, the private sector has been able to build, operate, and own (BOO) facilities for the distribution, storage and transportation of natural gas. The private sector may participate in electrical power generation, although the transmission and distribution of electricity remains in the hands of the government by constitutional mandate.

Upstream Oil and Natural Gas

In a state-owned sector, the greatest challenges are transparency and financing. Accordingly, Pemex has suffered a shortage of investment capital over the years which, when combined with restrictions on direct private investment, has resulted in the dramatic under-utilization of Mexico's energy potential and lagging production of natural gas and oil. How could Mexico attract private investment capital in an operating environment where transparency in business practices does not meet the expectations of the private sector?

Mexico is a net importer of refined products, petrochemicals, and, now, natural gas. For the next five years Pemex will face three major challenges: (1) demand forecasts for natural gas that far exceed current production levels, (2) uncertainty over the ultimate effectiveness of some projects under Mexico's special exploration and production program, and (3) lack of government budgetary support for the needed investments in refining, natural gas gathering and processing, and petrochemicals. As a result of these challenges, some members of the Council recommend further opening of upstream activities.

Mexico serves predominantly as an export market for U.S. natural gas. Although Mexico is rich in natural gas resources, most are located in southeastern Mexico, far from the primary consuming areas in the north and central regions of the country; and Mexico lacks the capital or the infrastructure to move the gas from the southern producing regions to the north. Increasing Mexico's natural gas production for domestic consumption and eventual export is a reasonable midterm goal, especially in a more liberal investment climate—an objective of the Strategic Gas Program (PEG) recently announced by the director general of Pemex, Raul Muñoz. Given current restrictions, however, it will likely be more expedient, at least for the near term, to satisfy increasing Mexican demand for natural gas in part with imports from the United States. In the oil sector, as well, the production capacity could be considerably improved. In fact, Mexico may face oil supply problems after 2015 without new exploration and technology for increasing reserves. Nonetheless, options are available for Mexico to begin to remedy the situation by increasing private sector investment in a manner that is consonant with Mexico's constitutional restrictions and by liberalizing legal and regulatory frameworks. Specifically, more upstream authority should be given to the Energy Regulatory Commission (CRE), a measure considered to be within the realm of possibility during the Fox sexenio.

- **BURGOS BASIN.** In anticipation of the increased demand for industrial use and electric power generation in northern Mexico, several projects have been proposed to increase the capacity to flow gas from the United States to Mexico; if completed, the current U.S. export capacity to Mexico would more than double. Export capacity from Mexico to the United States has not increased over the past several years. With the exception of Pemex's intention to export part of any increased production from the Burgos Basin in northeastern Mexico to the United States, no new projects have been proposed. Because of the favorable location of the Burgos Basin, Pemex plans to spend \$12 billion over the next eight years to increase Burgos production from 500 million cubic feet per day to

1.4 billion cubic feet per day in 2001. The Council recommends that innovative contracts utilizing performance clauses be applied to encourage private investment to complement Pemex plans to access nonassociated, dry gas resources of the Burgos Basin in northeastern Mexico.

- **MARGINAL OIL FIELD PROGRAM.** Pemex does not have the resources to fully exploit its entire portfolio. A variation of Venezuela's marginal oil field program in which drilling is open to partnership between Pemex and the private sector in marginal oil fields could be one way to begin private investment.
- **RATIO OF LIQUID-TO-GAS VOLUME.** Mexico could establish a ratio of liquid-to-gas volume measured in wellhead production below which gas would be presumed to be “dry” gas subject to separate conditions for private investment.
- **ELIMINATION OF GAS FLARING, WHEN FEASIBLE.** Natural gas found with crude oil is known as associated natural gas. Often because there is not a market for the natural gas, or because of the cost of disassociation, the natural gas is simply burned off. The burning not only pollutes the atmosphere, but is a waste of a natural asset. Alternatives to gas flaring, when feasible, are the creation of markets for the use of natural gas as a substitute fuel or as a raw material for petrochemicals.
- **SEPARATION OF MEXICAN NATURAL GAS PRICES FROM THE SPOT PRICE OF SOUTH TEXAS GAS.** Tying Mexico's natural gas prices to the spot price of south Texas gas has unsettled the market. Long-term contract prices or proxies to long-term contract prices could be applied using derivatives such as futures and hedges to New York Mercantile Exchange prices. This measure would preserve the connection to the North American market while dampening short-term price volatility. In reaction to recent high gas prices, Pemex has fixed natural gas prices at U.S.\$3.60 MMBtu for three years. Although this essentially ends the policy of price-tying for the time being, it presents the new problem of selling Pemex gas at below market value, which adversely affects the prospects for profitability and, thus, private sector investment.

Innovative Contracts for Exploration and Production

Service Contracts

Competition should be encouraged to the degree possible in upstream oil exploration and production by expanding the use of performance clauses in service contracts between private companies and Pemex (as provided in NAFTA Annex 602.4). Companies that invest in drilling and production are compensated with performance-based payments in cash or in kind, based on the amount and market value of the hydrocarbons produced. Pemex would remain the sole owner and producer of the hydrocarbons but would have a contractual relationship to investing companies. Such a strategy would place investors and Mexico in a competitive position vis-à-vis the hydrocarbon policies of many other countries.

- **NORWAY MODEL.** A possible model from which lessons can be drawn is the case of Norway, in which concession holders are permitted to operate simultaneously with the government's state oil company. This model may offer enough transparency for private sector participation in Mexico.
- **BROADENED SERVICE CONTRACTS.** Pemex could also benefit from broadening the scope of service contracts to include greater prospect evaluation studies, including data gathering and interpretation. Private exploration service companies could play a role in this particular area of upstream activity.

Risk Contracts

Some members of the Council feel the Mexican government should consider the possibility of entering into risk contracts instead of the widely used service contracts. Risk contracts provide incentives for investment and would encourage companies to take a fresh look at the Mexican market.

Natural Gas Infrastructure

As a result of the fixed price of Pemex natural gas, the profit margin for competitors has been reduced. Private sector investment is highly unlikely under current natural gas market conditions in Mexico. The shortage in the supply of natural gas and transportation capacity available from Pemex is a serious bottleneck to investments in electricity and petrochemicals. The number of investors interested in Mexico's private pipeline opportunities has dwindled due to Pemex's unusual degree of power over transportation, storage, marketing, service pricing, interconnections, and operations. Investment could be encouraged by taking the following steps:

- **IMPROVE PIPELINE RELIABILITY.** Much gas is lost from leaking pipelines. More funding should be invested in modernizing gas pipelines. Since the transportation and distribution of gas was opened to privatization in 1993, many new projects have been initiated, and the trend should continue in that direction.
- **PRIVATE CAPITAL OPPORTUNITIES.** Identify and take advantage of any possibilities to increase the opportunity for private capital to improve gas deliverability and transmission capacity, such as through construction projects of generating plants and water treatment facilities.
- **PEMEX MARKETING RESTRICTIONS.** Pemex should be persuaded to not market to the end user. A competitive gas supply market should be created as an alternative with customers benefiting from gas-on-gas supply competition.
- **UNBUNDLE PEMEX PIPELINE NETWORK.** Pemex's existing pipeline network should, at minimum, be unbundled into separate companies offering transportation service with transparency of pricing; open-access, nondiscriminatory transportation rates; and unregulated secondary markets for assignable and salable transportation rights.
- **OPEN SALT-CAVERN GAS STORAGE TO PRIVATE INVESTMENT.** Salt-cavern gas storage fields for injection and withdrawal of privately owned gas should be

opened to private investment. Pemex should offer depleted gas fields for private use for gas storage.

Petrochemicals

Mexico imports 45 percent of its petrochemical needs, unusual for an oil-producing country. Basic petrochemicals consist of ethane, propane, methane, and naphtha. Pemex has a monopoly on these products and their delivery, but it does not have the capability to meet the demand for these basic commodities.

Promote Private Investment in Pemex

While there are no legal constraints to building a greenfield petrochemical project in Mexico, the Council finds that there are two major obstacles:

- the lack of competitive supply of feedstocks (which fall under the Pemex monopoly), both in price and in volume.
- the inability of investing companies to resell the basic petrochemicals that would be generated by the process to Pemex at market value.

Feedstocks

Pemex should offer basic feedstocks to all purchasers at internationally competitive prices. Purchasers should be able to obtain imported feedstocks, if necessary, without duties or penalties, providing competitive incentives for Pemex to offer feedstock at prices at or below international levels.

Increase Private Investment in Refining

Similar to the situation with petrochemicals, Mexico exports crude oil but imports refined products due to lack of investment in refinery infrastructure. In downstream activities of Mexico's petroleum industry, Pemex faces some major refining investment needs and the possibility of retail competition. As outlined in February 2001, Pemex Refining currently forecasts that overall investment requirements for 2001-2010 will be about U.S.\$18 billion.

Privately owned refineries should be permitted to be built and to obtain crude oil from Pemex at prices no higher than Pemex gets from exporters of crude oil. The refining sector should be opened up to private investment and competitive sales of refined products. Recognizing, however, that there could be strong political rejection of this move, an alternative could be an "integrated project" in which Mexico would open space to international oil companies for upstream activities in Mexican territory, using acceptable formats such as service contracts. In exchange, Mexico would get either equity or other forms of participation in refining and downstream in the United States within the framework of long-term agreements.

Alternatives to In-Country Private Sector Participation

To boost its refining capability, Mexico should increase joint ventures in refining beyond its borders, such as the project in Deerpark, Texas. This would allow for private sector participation in Mexico's oil industry within the current legal framework.

Potential Opportunities in Retail

Pending a decision by the Supreme Court of Mexico on an ongoing investigation by the Federal Competition Commission (CFC) regarding the potential illegality of the lack of competition in nonregulated markets, motor oil blenders and marketers may have access to Pemex's service station chain. This is one area in which the private sector should be looking to invest.

Electricity Sector

Both Mexico and the United States are facing the prospect of current and future electricity shortages, making the production of new capacity a high priority for both countries. Current reserve margins in Mexico are estimated to be between 5 to 6 percent, and the dramatic shortage of capacity in California suggest that all three countries of North America should encourage greater private participation to increase capacity. If electricity supply does not keep up with the growing demand, it will ultimately slow economic development.

Development of transparent rules and regulations and removal of subsidies would facilitate private investment in the electricity sector and enable Mexico to meet the projected 26,281 MW of new capacity (nearly 60 percent of current capacity) needed by 2009. The injection of private capital to fund new capacity in Mexico and the U.S. will allow government resources to be used for social priorities such as education, housing, and health care.

A transparent North American market with rates that reflect actual costs will lead industry and consumers to become more efficient and conservation oriented. New, more-efficient capacity using advancements such as clean coal technologies, will allow older less-efficient capacity to be retired and improve air quality.

Mexico is competing with every other country in the world for a finite amount of private sector investment resources. To the extent that other countries have an open-access electricity sector and clear opportunities for investment, they will receive more investment. The largest impediment to private investment in Mexico's electricity sector is the market structure itself. Private companies are limited to participating in the CFE's bidding process, "inside-the-fence" bids, and evaluating or developing small power production and cogeneration projects. Full-scale market reform is essential for Mexico to ensure that its growing capacity needs are met. However, benefits may be partially realized by improving the investment opportunities currently available in the electricity sector even if full market reform is not implemented. The following approaches could accomplish this goal.

- **OPEN MARKET.** As do virtually all other countries in Latin and Central America, Mexico should consider a comprehensive transition to a competitive, open electricity market that lifts restrictions on ownership. In other countries, competitive markets have lowered prices to consumers, and new investment has flooded in.
- **ELIMINATION OF ELECTRICITY PRICE SUBSIDIES.** The Mexican electricity sector has functioned without transparent regulations or accurate price signals which would reflect the true cost of generation, transmission, and distribution. Consumers who receive subsidies have no incentive to use electricity efficiently and private sector projects must compete with subsidized electricity provided by the CFE. The intention to lift subsidies recently announced by Mexico's Secretary of Energy is an important step toward market reform.
- **CFE BIDDING PROCESS.** The nature of the CFE bidding process limits their appeal to potential investors. The CFE bidding guidelines require extraordinary amounts of technical documentation, making the bids costly to prepare and taking away critical flexibility for the private sector companies to develop and operate the projects with the award-winning designs that distinguish the Independent Power Producers (IPP) industry elsewhere. The Council recommends that the technical aspects of the bidding process should be simplified and limited to a demonstration of technical competence .
- **DISQUALIFICATIONS.** There are a disturbing number of bidders who have been disqualified for "errors." In many instances, these errors have been nonmaterial, and correcting them would not have involved changing the price of electricity offered to CFE. Mexican consumers do not benefit when qualified bidders are turned away because of administrative matters. The CFE could define a period of time for bidders to correct technical or administrative errors that do not affect the price, a practice common in other government-run bids. This approach does not mean that bidders would be allowed to change their bid price but, rather, that a period of time (ranging from 12 hours to 5 days) would be established to correct discrepancies in the bid documents.
- **MAXIMUM PRICE POINT.** The CFE reserves the right to reject any or all of the bids offered in the event that the CFE believes the price is too high. Usually, when an entity wishes to reserve the right to reject offers received in a bid, a maximum price point is established prior to the bid. This bid price is either maintained confidentially or is announced as the maximum acceptable price. CFE bids are too expensive and time consuming and therefore cannot maintain the private sector's interest when the CFE can unilaterally decide, after reviewing the proposals, that the prices are not acceptable. The CFE should establish a maximum leveled price and distribute it with the bidding guidelines.
- **SELF-SUPPLY PROJECTS.** The current Mexican Constitution and the electricity energy law passed in 1975 and amended in 1992 allow large industrial consumers of electricity to produce their own electricity. Because of the regulatory restrictions on ownership, companies have to create cumbersome and expensive corporate structures to enable them to provide electricity. Artificial barriers

to ownership should be removed because it is constitutionally acceptable for an industrial company to own its own generating capacity, and therefore, it makes sense to allow private generating companies to own these facilities as well. It also makes sense to increase the amount of electricity that these projects are permitted to sell into the wider market.

- **TRANSMISSION AND CROSS-BORDER SUPPLY.** Imports and exports of electricity to and from neighboring countries are allowable under the current regulatory structure, so long as the imports are for self-supply projects and the exports are produced by small power-production or cogeneration projects (limited to less than 30 megawatts [MW]). It is difficult for U.S. producers to sell power into Mexico given the requirement that all sales be made to the CFE, and such negotiations can be lengthy. In addition, an IPP permit can be obtained for production of electricity for export to other countries. Similarly, a Mexican industrial company may wish to wheel its self-generated power production, produced at one facility, to another of its facilities located in a different state. Without open access to the transmission system and a tariff structure for wheeling charges, these types of projects will be more difficult to develop.

Another priority matter is the ability to move electricity freely across the border, which faces serious constraints given the aging transmission limit capacity in both countries. There are many interconnection points where there could be more exchange, but millions of dollars are needed to upgrade the lines or build new lines on both sides of the border. California transmission lines need upgrading, for example, yet its utility companies are bankrupt, raising the question of who will invest in this infrastructure. The Mexican side functions under constitutional restraints to private investment in transmission, although some projects end up with private companies paying for transmission line upgrades in exchange for reduced fees using those transmission lines.

- **CLEAR CONNECTION GUIDELINES.** There should be clear guidelines governing the process for interconnecting with CFE's bulk transmission system. These guidelines need to ensure nondiscriminatory access by which IPP projects are evaluated on the same basis as CFE generation. In addition, open access to the transmission system would entail implementing a wheeling and interconnection tariff structure that is clear, publicly available, and equal for all users of the CFE grid system.
- **TRANSMISSION AS A SEPARATE BUSINESS.** Separating ownership of generation and transmission assets ensures a level playing field for all generators. By making transmission a separate business, which is usually run as a regulated, government-owned business, it is possible to establish wheeling and interconnection tariffs that are the same for all generators.

Monetary Policy

The Current Situation

Events in Mexico and in the world raise issues about exchange rate policies. While enormous progress has been made in promoting long-term, fixed capital flows, the issue of short-term mobility has been far more problematic. It is legitimate to explore a variety of options in monetary policy, ranging from a common currency for North America to preserving the current free-floating system. The council members had mixed views regarding the options, which are summarized below.

Current Policies

It is extremely important for the Fox administration to continue to hold the line on Mexico's anti-inflationary fiscal and monetary policies. Without these strict policies, and in light of events over the last 25 years, Mexico would find it impossible to maintain the kind of stability in exchange rates that it has enjoyed since adopting a flexible system.

Arguments for and against Dollarization

In light of the successful float currently in place, some council members feel that dollarization is not desirable, at least not at this time. Fixed exchange rate systems were discredited following the sharp depreciation of the peso at the end of 1994. Mexico had had a system under which the peso was pegged to the dollar and maintained in a crawling band by active market intervention. In the course of 1994, Mexico used up most of its foreign reserves to maintain the dollar peg, which significantly contributed to the crisis. To replace this policy, the Mexican government adopted a flexible exchange-rate structure, in which the peso was allowed to float. The float has been relatively clean to date; market intervention has been quite modest, and when it took place, it was designed to prevent overshooting the peso-dollar rate on any given day. Since Mexico adopted a free-float system, the peso has been remarkably stable in real terms. For example, in 1996 the market rate was 7.6 pesos to the U.S. dollar, compared with 9.5 pesos per dollar during the past two years—a change that reflects the difference in inflation between the two countries. The stability in the exchange rate is a direct result of conservative fiscal and monetary policy on the part of the Mexican government.

Opposing Arguments

Those opposed to dollarization argue that it not only would deprive Mexico of an independent monetary policy but also could not guarantee that the country's cycli-

cal position would be consonant with that of the United States (in other words, the policy could not assure that the necessary countercyclical measures would be identical). The inability to implement a compensatory monetary flexibility would harm Mexican workers during times of recession, especially in the absence of full North American labor mobility.

Supporting Arguments

Many Mexican industrialists and individuals involved in trade favor complete dollarization of the Mexican economy—totally discarding the peso and using the dollar for the country's currency. Recurrent financial crises over three decades have created an environment of permanent uncertainty in Mexico, they argue, even when the government pursues proper policies. Breaking the cycle would take years to accomplish. To support their position, advocates cite the European Union, where national currencies are being phased out for countries that are in the process of economic and monetary union. The strongest arguments in favor of dollarization are that it will ensure currency stability, stimulate development of a mortgage system, enhance access to U.S. capital markets, and accelerate convergence with U.S. inflation and interest rates. There are various ways Mexico could move toward dollarization:

- **FREE COMPETITION OF CURRENCIES.** By permitting all currencies to compete freely in the domestic and international payments system, a de facto dollarization process would result.
- **U.S. DOLLAR AS LEGAL TENDER.** Making the dollar legal tender is the most straightforward way to achieve dollarization. An agreement with the U.S. Federal Reserve Board would have to be negotiated carefully in order to ensure liquidity. There is wide agreement that a currency board would not eliminate uncertainty and could create balance of payments and banking system hazards. An agreement with the U.S. Federal Reserve Board could include:
 - loan guarantees for Mexico's M4 at the outset so as to cover peso liabilities, in order to guarantee Mexico the necessary number of dollars for full currency conversion;
 - compensation mechanisms for recession in Mexico, with consultative arrangements to supervise the Mexican region as the Federal Reserve Board does in various U.S. regions; and
 - compensation for lost currency seignorage, that is, the earnings that must be given up as a result of the loss of interest on dollar holdings.

Preparedness for Exchange-Rate Volatility

Considering the past volatility of the peso, it would be prudent for the Mexican government to study what measures would be available in case the volatility in exchange rates returns, and what arrangements would be necessary to move toward the possibility of dollarization.

North American Stabilization Fund

Another solution would be the creation of a North American stabilization fund to which each nation would contribute \$10 billion for a total fund of \$30 billion. The function of the fund would be to inhibit speculation *ex ante*, which is far less expensive than *ex post*. A trilateral board would manage the fund and could also serve as the starting point for a more formal macroeconomic coordination mechanism. Participation in this fund would presuppose an agreement to seek convergence on basic economic indicators, including inflation, the ratio of debt to gross domestic product (GDP), the size of the fiscal deficit in relation to GDP, and real interest rates.

Harmonization of Financial Regulation

The harmonization of financial regulation is an important area for NAFTA attention, given that significant differences exist in the prudential regulation and bank supervision practices in Mexico and the United States. This leads to inefficiencies in the way bankers assess the value of banks and companies, which may well discourage the free mobility of capital inflows.

Overall Policy Coordination

The Treasury Departments and central banks of Mexico and the United States should continue consultation with one another in order to coordinate both countries' fiscal and monetary policies to the maximum extent feasible and to provide ample warning of any anticipated disruptive changes, such as variation in the U.S. federal funds rate.

Environmental Issues

NAFTA institutions will need increased funding over the next 10 years to meet rapidly growing needs on the border and in Mexico's interior. The current estimate for identified projects aimed at improving the environmental infrastructure at the border is \$3.1 billion, which should sustain the region until 2009. Land degradation, water pollution, and crop contamination continue on a significant scale. Established NAFTA institutions could be used and augmented in an effort to protect the environment along the border and within Mexico's interior.

The North American Development Bank and the Border Environmental Cooperation Commission

The NADB was established in 1993 to help finance projects dealing with local water supplies, wastewater treatment, and solid waste disposal along the border between the two countries. The BECC certifies projects for NADB funding and provides technical assistance to local communities via \$20 million in funds provided by the U.S. Environmental Protection Agency (EPA) through its Project Development Assistance Program.

The NADB is not lending much money because its loan rates have been unaffordable for many border communities, which lack a revenue stream both to pay off the loans and to provide operating costs for the infrastructure projects built with the funds. Moreover, by federal law Mexican communities are prohibited from seeking infrastructure debt financing outside of Mexico's domestic market, and they cannot issue debt or establish user fees. Certain provisions have been made to allow Mexican communities to use NADB funding, but these measures have met with only limited success. In contrast, U.S. communities have alternatives, including state revolving funds, municipal bonds, or other grants. These existing institutions could function more effectively if both governments take steps along the lines recommended below.

NADB's Mandate

NADB's responsibilities should be broadened, permitting it to serve as a mechanism for funding infrastructure improvements in communities in the interior of Mexico. Today, NADB deals only with financing such projects for Mexican and U.S. communities along the common border.

Increase in Capital Funds for NADB

Both governments should commit to an orderly annual expansion of NADB's capital funds in order to reach a negotiated common goal between the two countries.

Scope of NADB Projects

NADB should be authorized to widen the range of projects it is permitted to fund, including financially viable efforts (improvements to rail and port infrastructure, for example), which will provide the revenue flow needed to enable the bank to expand lower-cost funding to the often unprofitable types of infrastructure projects, such as water projects.

EPA Grants to NADB

EPA financing for border projects should be increased. The Border Governors Conference recently requested that the U.S. House Appropriations Committee provide \$100 million for the Border Environment Infrastructure Fund for fiscal year 2001. That is the amount that the North American Development Bank says that it needs each year for a period of 10 years for planned infrastructure projects.

Funds for Solid Waste Disposal

Additional funds should be allocated to create a technical assistance program to be offered by the BECC—which is currently paying substantial attention to water and wastewater issues—so that the BECC also can deal with the problem of solid waste disposal.

The North American Commission for Environmental Cooperation

The work of the North American Commission for Environmental Cooperation (CEC)—which consists of the environmental ministers of the U.S., Mexican, and Canadian governments—has conducted worthy projects dealing with conservation and pollution prevention in the three neighboring countries. The CEC should be strengthened by adopting measures in the following areas.

CEC Funding

The United States and Canada should increase its overall financial commitment to the CEC's secretariat and its working program, even without a larger financial commitment from Mexico. A stronger CEC could allocate funds to environmental programs and organizations in Mexico, including promotion of citizens' watchdog groups. If Canada, Mexico, and the United States want the CEC to deal with only a handful of transboundary priorities, the CEC's budget will be modest. However, to take on larger priorities, such as implementing an agreement dealing with persistent organic pollutants, the commission will need a budget increase.

Canadian Participation

Canada should secure the commitment of all its provinces to the North American Agreement for Environmental Cooperation. Because provincial governments have a certain degree of autonomy, they are not automatically subject to the accord. Only three of Canada's ten provinces have approved the NAAEC.

CEC Responsiveness

The CEC should continue to encourage transparency by listening to the complaints of each country's citizens about their government's environmental performance.

Funding Governmental Capacity to Protect the Environment

The implementation of NAFTA and its environmental side accord has pushed Mexico and its Environmental and Natural Resources Ministry (SEMARNAT) to a level of environmental performance for which it is both underfunded and unprepared. SEMARNAT needs assistance in developing both its institutional and its technical ability to implement domestic environmental programs and international cooperative efforts. Therefore, additional funding should be provided and augmented by technical assistance from the United States via the CEC, along the lines proposed below.

Binational Advisory Committees

Independent consulting committees from both countries—including nongovernmental organizations—should work together to establish clear-cut environmental goals. These committees should also set goals and time frames for providing technical assistance to Mexican federal authorities.

Harmonization of Indicators

The two countries should work to improve and harmonize environmental indicators in the existing databases on environmental indicators for both countries. This measure will make clear country-to-country comparisons possible.

State and Local Authority

The federal governments of both nations should look for creative opportunities to divest power to the states and localities. A presidential directive can make it possible, for example, to authorize transboundary port authorities to manage fees and float bonds, similar to the functions performed by the Port Authority of New York and New Jersey.

State and Local Taxation

Mexico's federal government should enhance the authority of local and state governments to assess and collect taxes for infrastructure development and to incur debt to finance such projects.

Technical Assistance to the States

Federal U.S. funding should include technical assistance for environmental programs that are jointly undertaken by individual states in Mexico and in the United States.

Nonprofit Sector Contributions

Regional nonprofit organizations have been helpful in the binational environmental relationship, including the updating of Mexico's emissions inventory system and increased application and implementation of current environmental laws. Enhanced U.S. and international funding can be provided to activities of nonprofit organizations that are aimed at solving environmental problems in the border region.

Water Supply

The primary limitation to development in the border region is lack of water. Water shortages plague both sides of the border, and the shortages affect not only agriculture but also water quality and the quality of life in this semi-arid region.

Wastewater treatment is the most crucial need, and it is of particular concern on the Mexican side of the border, although a substantial need also exists in Texas. Shortages are so severe that the U.S.-Mexico twin cities of Reynosa in Tamaulipas and McAllen in Texas have publicly voiced concern about attracting new maquiladora investment because of the insufficient water supply and infrastructure for industrial use. In San Diego-Tijuana water is being imported and in El Paso-Ciudad Juárez, underground water supplies may be depleted by 2030.

Most of the border states have not been as proactive in water conservation as California has. In 1996, California voters approved Proposition 204, the Safe, Clean, Reliable Water Supply Act, which issued \$995 million in general obligation bonds to finance water and environmental restoration programs. The following issues should be considered in an attempt to solve the problem of water supply.

Binational Water Planning

Binational water planning should be intensified, and not just for the border region. Both Mexico and the United States have individual planning efforts under way to conserve water on each side of the border. Although officials of Texas, New Mexico, Arizona, and California meet informally with Mexican federal officials on this issue, Mexican state governments lack the power of U.S. states to implement water conservation plans. One way to ensure that the state and federal governments on both sides of the border participate equally in the planning process is to establish a

federal binational mechanism for water supply planning that spans the entire border region. This mechanism would include participation by state and local governments as well as by interested citizens. A binational task force should be formed to assess the expected water supply level at the border over the next 50 years, as well as to conduct studies of water availability and demand for both national economies over the next two decades. Participants should include representatives of both countries' federal governments, state governments, and citizens' groups.

BECC Involvement

The BECC was established specifically to certify water, wastewater treatment, and solid waste disposal projects for funding by the North American Development Bank, and it provides some project development and project design assistance to local communities. But the role of the BECC in overall water conservation planning is limited. The scope of the Border Environment Cooperation Commission could be widened to include new types of technical assistance to local communities, beyond those projects financed by the NADB.

Irrigation Systems

The irrigation systems in both countries need to be optimized by improving conveyance systems and field water delivery systems. The water-intensive practice of field flooding, used both in the United States and Mexico, should be replaced when possible with drip irrigation methods. In both Texas and Mexico, fees can be established for water conveyance improvements. Alternatively, Texas can authorize state bonds for water projects aimed at conserving existing supplies. However, this option does not exist for Mexican states, which do not have constitutional authority to issue such bonds.

Create a Water Market

Federal and state governments on both sides of the border should investigate the possibility of establishing water markets in which water rights owned by irrigation districts or in some cases by individual farmers can be routinely auctioned or publicly sold by some other method to municipal or other users. The establishment of such markets could result in the transfer of water to users with the greatest need, and appropriately priced water could result in more efficient water use.

Promote Crop and Climate Compatibility

Certain types of crop production should be discouraged through proactive government programs. Texas, California, and some Mexican states are producing crops that are not well suited to farming in semi-arid regions. One prime example of this is sugarcane production, which is increasing in Texas.

Monitoring of Water Distribution

All nations should strive for compliance with the allocation provisions of the 1944 U.S.-Mexican Water Treaty. The treaty could be more fairly enforced with improved

monitoring of water flows and levels, for which Mexico needs a system of water meters to monitor the distribution of water for irrigation purposes.

Transboundary Air Quality

The U.S. and Mexican governments face transboundary air pollution issues that are sometimes exacerbated by differing air quality standards and enforcement capabilities on either side of the border. For example, Mexican ambient and point source air quality standards are not as stringent as U.S. standards. Several approaches can remedy this situation.

International Air Quality Management Districts

Federal, state, and local agencies on both sides of the border could establish international air quality management districts for basinwide planning, monitoring, and management of air quality in bordering cities, as was successfully done at the twin cities of Ciudad Juárez and El Paso. This concept should serve as a blueprint for cooperation for two other border regions with significant deterioration of air quality—such as the areas around the San Diego-Tijuana border and the Nogales (Sonora)-Nogales (Arizona) border.

The U.S. Clean Air Act

To make the common air shed program more effective, the U.S. government should consider changes to the Clean Air Act that would enable U.S. firms operating on the Mexican side of the border to apply for emission reduction credits elsewhere within their U.S. operations. The system should take into account emission reductions in a common binational air shed.

Data Comparisons

In a region where air quality standards vary on each side of the border, an open dialogue can be facilitated by first comparing baseline data on ambient air quality and point source emissions within a common air shed. Such data comparisons are one of the goals of the Commission for Environmental Cooperation's annual report, *Taking Stock*, which details emissions and waste transfers by region throughout North America. As Mexico undergoes the process of revising its air emissions inventory, greater transparency on air quality issues could help facilitate both regional planning and opportunities for source reduction and pollution prevention.

Corporate Incentives

One measure that would be helpful to Mexican government officials as well as U.S. firms would be a U.S. export promotion effort for firms specializing in automotive emissions testing equipment and vapor recovery systems. Mexico is moving toward an increased use of natural gas as a cleaner burning fuel, and firms producing natu-

ral gas-fired boilers and related conversion technologies should have good market opportunities in Mexico.

Hazardous Waste

Mexico generates about 8 million metric tons of hazardous waste each year (excluding the mining sector). The Mexican government estimates that only about 11 percent of this waste is properly disposed of, with the remaining illegally dumped on land, in bodies of water, or in the municipal sewer system, by far the most common option. The Hazardous Waste Tracking System (Haztraks) accounts for shipments of hazardous waste across the border and alerts local, state, and federal officials on both sides of the border to potential violations. However, Mexico still does not have reliable data on the total generation of hazardous waste by the *maquiladora* industry, pointing to a serious long-term problem in the safe handling of these industrial wastes.

The *maquiladora* industry is the chief generator of hazardous waste in the U.S.-Mexico border region. Under Mexican law, *maquiladora* waste must be returned to the country of origin (usually the United States). But as the *maquiladora* program is phased out in 2001, and more companies register as Mexican national firms, the requirements for exporting wastes from American firms back to the United States will disappear. As this happens, Mexico's already overburdened waste management infrastructure will be further encumbered, posing enforcement problems for Mexican authorities.

In addition, Mexico has developed a number of abandoned and health-threatening hazardous waste sites over the years. Out of 166 such sites, about six are located at the border. Mexico has only one hazardous waste disposal facility, and it is located outside the border region. This affects the ability of firms outside the *maquiladora* program to comply with hazardous waste laws.

Construction of Facilities

Mexico should follow through with its 1996 plan to locate sites for and promote construction of hazardous waste management facilities throughout the country. Mexico can identify and negotiate with international firms that possess expertise to build such facilities and invite those firms to participate in the planning process.

Technical Instruction

The U.S. government or the North American Commission for Environmental Cooperation can provide greater technical assistance to Mexico in the area of waste management.

Antinarcotics Policy

Both American and Mexican members of the Council believe that it is time to end or substantially modify the certification process, particularly in reference to Mexico, with which the United States has a special relationship. Mexican opinion was unified in considering U.S. certification to be unilateral, offensive, and corrosive to the spirit of mutual respect that is necessary to advance cooperation. Although U.S. members' opinions were divided, all agreed that the U.S. Congress and the two new presidents should make a concerted effort to seek reciprocal measures that build confidence and goodwill.

Alternatives to the Certification Process

The modification of the certification law proposed and passed unanimously by the Senate Foreign Relations Committee on April 5, 2001 (S.219) is a positive measure in this spirit, holding that foreign nations will be judged on adherence to international treaties or other commitments. The measure, offered as a three-year trial, would require that the president single out only the worst offenders; it would shift the premise from one of guilty until proven innocent to innocent until proven guilty; and it would continue to make the worst offenders ineligible for U.S. aid. The bill is but one solution among many proposed; its passage has yet to be secured, and its efficacy has yet to be tested. The Council therefore suggests that additional propositions remain open to discussion.

One especially promising proposition would be to establish an antinarcotics protocol and certification exemption policy for all countries currently subject to the certification process. Negotiating formal bilateral agreements or protocols—much as the Mexico and the United States have done with NAFTA—could define bilateral benchmarks in areas of cooperation such as extradition and cooperative law enforcement operations. Upon successful negotiation and implementation of such a protocol, whose criteria could be defined by each government, the country involved would automatically be exempt from certification. This protocol could be offered as an option to each country. This proposal shares important elements with an initiative sponsored by Congressman Jim Kolbe (H.R. 753) and Senator Kay Bailey Hutchinson (S. 353), and it has the virtue of building performance targets and accountability into bilateral antidrug efforts.

Practical Steps for Building Confidence and Managing the Issue

Intensifying bilateral counternarcotics efforts would help to create the confidence necessary for the U.S. Congress to seek either a Mexican exemption or permanent modification of the certification law. To demonstrate the political will of both gov-

ernments to work together, practical measures, such as those recommended below, need to be taken on the operational level.

- **BINATIONAL COMMITTEE FOR DRUG SEIZURE AND DESTRUCTION.** This committee would be responsible for overseeing the seizure, warehousing, and destruction of drugs. This should be a permanent committee in which decisions are made by consensus. The committee activities should include formalizing U.S.-Mexico post-seizure analysis teams, which, in the United States, play a significant role in gathering valuable information.
- **EXPANSION OF EXISTING PROGRAMS.** The binational maritime intelligence-sharing and interdiction program has been highly successful and should be expanded to include carefully targeted land-based transit zones. Air interdiction should be strengthened by the adoption of a communications plan for aerial interdictions operations similar to the recently implemented plan for maritime communications.
- **JOINT ASSETS SEIZURE PROGRAM.** A joint fund should be established to administer goods and funds captured in the drug war, which can then be used for antidrug programs in both countries. The U.S. and Mexican governments are preparing a Memorandum of Understanding for reciprocal asset sharing that should result in more seized assets going for antinarcotic programs.
- **STIFFER PENALTIES.** The United States should impose stiffer penalties for arms trafficking and should cooperate with Mexico to improve and augment existing tracking programs. The cooperation with Mexico is already under way and has resulted in a higher percentage of illegal arms reported to the Bureau of Alcohol, Tobacco, and Firearms (ATF) being traced. It is not clear how much effect, if any, this has had on illegal trafficking of firearms into Mexico, or whether the cases that can be traced have a higher rate of prosecution. Some sort of feedback mechanism to assess effectiveness should be built into the system if Mexico wishes the United States to intensify the program.
- **LEGAL INTERROGATIONS BY U.S. AUTHORITIES.** A legal mechanism to permit FBI interrogations within Mexico should be created. Mexican participants expressed concern that such interrogations are not possible within the Mexican judicial system and that it would be more appropriate to increase temporary extraditions with the sole purpose of speeding up ongoing judicial processes in both countries.
- **PROMPT EXTRADITION.** Mexican drug lords frequently appeal extradition requests and severely delay the arraignment process. It is legally impossible to appeal a bilateral agreement in Mexican courts of law, and thus both new governments should negotiate a bilateral agreement in the area of expedited extradition to prevent drug lords from engaging in lengthy appeals.
- **INFORMATION SHARING.** Information sharing should not be limited to narrowly defined narcotics issues. Many homicides and car theft cases are related to drug issues and the exchange of information in these areas could provide more details on the laundering of money and criminal organizations. In these cases,

information often is handled by local authorities, which makes the exchange of information almost impossible.

- **DEPOLITICIZING ANTINARCOTICS COOPERATION.** Ending Mexico “bashing” should be a high priority in bilateral antinarcotics efforts. The president and the attorney general of the United States should insist on disciplined behavior from U.S. law enforcement agencies; for example, politically inspired leaks that vent the frustrations of law enforcement agents end up on the front pages of major U.S. newspapers, politicizing and undermining both countries' efforts to end drug trafficking.
- **AN END TO THE BLAME GAME.** Finger pointing does not advance antidrug efforts. The United States should assume responsibility for the corrosive effect that consumer demand for drugs has upon Mexico, and Mexico should assume responsibility for curtailing supply.
- **REDEFINITION OF SOVEREIGNTY.** Just as Mexico is often frustrated by U.S. placement of blame on Mexico for the drug problem, many in the United States are frustrated by Mexico's tendency to sharply delineate the boundaries of bilateral antinarcotics cooperation in the name of defending national sovereignty. Drug trafficking does not respect borders or traditional concepts of national sovereignty.

Intelligence Sharing and Confidence

Mexican members of the Council complained about U.S. reluctance to share intelligence but acknowledged that the Mexican police are ready targets for the corrupting influences of drug traffickers. The following options would serve to remedy this situation.

- **DIPLOMATIC COOPERATION.** A small team of vetted and anonymous diplomats from the U.S. Department of State and Mexico's Foreign Ministry or individual presidential appointees could be formed for the purpose of sharing intelligence (as distinct from law enforcement information). Law enforcement agencies in both countries should be challenged to propose a system that would be viable and meet their needs for protecting sources.
- **EVALUATION OF INDIVIDUALS.** Both countries could build the confidence needed for sharing intelligence by adopting common security clearance standards. This policy could be broad-based across-the board cooperation or narrowed to individuals occupying limited, sensitive positions.
- **SPECIALIZED INVESTIGATIVE UNITS.** Instituting bilateral highly specialized units would help achieve a balance of the skills and approaches needed to gather the intelligence required for combating drug trafficking effectively. These should be small secure groups consisting of about 15 members, who would work on a case-by-case basis. They should have some guarantee of continuity to ensure professional cohesion and insulation from the influence of clique politics.

Mexico's Judicial Institutions

The strengthening of Mexico's police force and court system are internal matters, but Mexican members of the Council stressed that the success of bilateral counter-narcotics efforts depends on building better Mexican legal institutions. It is essential that the United States offer any technical cooperation or resource assistance that the Mexican government might find useful in its efforts to professionalize the country's legal institutions.

- **MEXICAN LAW ENFORCEMENT INSTITUTIONS.** President Fox should work to enhance the professionalization and continuity of Mexican law enforcement institutions, whose members must receive adequate salaries and be afforded a professional future that is insulated from political patronage and personal politics.
- **FUNDING FOR INSTITUTION BUILDING.** Funding should be increased to coincide with bilaterally agreed-upon goals. Previous efforts have included USAID's program to train judges; funding by the U.S. Department of Health and Human Services and the Office of National Drug Control Policy to help Mexico curb drug demand among its citizens; the U.S. Treasury Department's funding for Mexico's money-laundering unit; and the U.S. Department of State's financing of binational judicial conferences and provision of seed money for institutions such as the Drug Control Planning Center (CENDRO).
- **POLICE TRAINING.** The FBI and other U.S. agencies should continue and also expand the training programs offered to Mexican police forces. Training should be directed toward specific objectives, such as training for undercover work or how to manage an effective witness protection program. The effectiveness of U.S. training could be gauged by implementing a tracking system that monitors the careers of trained officials.

Institutional Organization and Strategies

The Bush administration will have to decide what antinarcotics strategy it will pursue and what institutions it will rely on to implement that policy. The authority of the ONDCP has fluctuated during the agency's relatively brief existence, depending on the personality of the director and the willingness of the White House to permit the office to assume a leadership role.

Many in the Council were inclined toward a strong role for the ONDCP. Specially created mechanisms such as the High-Level Contact Group for Drug Control, the Senior Law Enforcement Plenary, and the Binational Expert Group on Demand Reduction have been effective tools for opening communication and coordinating policy. Many Council members were in favor also of building on the foundations of the HLCG, while trying to make the agenda more dynamic and action-oriented.

Other Council members, however, recognizing the significance of the election of the Fox government and the renewed spirit of goodwill between the two governments, believe that antinarcotics policy might best be managed through normal institutional channels, such as the Binational Commission.

Conclusion

We are poised on the verge of an exciting new era in U.S.-Mexican relations. Old paradigms are being challenged on both sides of the border, and new paradigms are being explored. In order to realize the full potential of this historic opportunity for change, the bilateral relationship must remain a priority and receive sustained attention in a permanent fashion from both governments. We welcome the creativity displayed at the first meeting of Presidents Vicente Fox and George W. Bush. Indeed, the proposals contained in this report address in detail the interest of the two leaders in developing new ideas for policies dealing with immigration, drug, border, trade, and energy issues. This Council stands ready to provide substantive support and participation in the policy debates that will occur in the months and years ahead. May the hopes and dreams of citizens on both sides of the border be fulfilled and brought into harmony.

Managing the Bilateral Relationship

Working Group Meeting, October 29, 1999
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Working Group Meeting, January 14, 2000
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Bilateral Counternarcotic Efforts and Judicial Reform

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Migration Dimensions to the U.S.-Mexican Trade Relationship

Working Group Meeting, September 29, 2000
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