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A Comparison of EU-NAFTA Integration Regimes: From a Trade Bloc to an Institutional Development Model

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Introduction

The beginning of the 1990s ushered in a decade of economic and political reforms for poor, backwards countries around the world. Developmentalists looked on excitedly as autocratic regimes and outdated economic systems were dismantled, especially in the regions of Latin America and Eastern Europe. Both emerging from poor governance and hyper inflated, inefficient economies, remarkable reforms in these countries provided exciting opportunities to better understand the domestic processes involved in economic, political and institutional development. For example, both Argentina and Poland used "shock therapy" economics to create market economies, implementing rapid liberalization and privatizations to institutionalize economic reforms. However, instead of providing two examples of effective democratization and economic reform, only one country could provide such an example by the end of the decade. Poland's emergence as an economically vibrant democracy contrasts starkly with Argentina's default in 2001 and stagnant growth rates. Given Argentina's more democratic roots, the disparate outcomes in institutional development between these two countries have stimulated vivid debate about the factors which could have led to such a counterintuitive result.

In explaining this puzzle, it is not obvious that domestic politics in reforming 3rd world countries are the sole determinants of reform success or failure. International geopolitical factors must also be accounted for, as the 1990s have introduced new questions about the role of international actors in promoting democratic and economic reforms. No longer subject to the constraints of the Cold War, advanced western countries had a better position from which they could aid and encourage reforming countries. Indeed, international actors have been instrumental in bringing about economic reforms to create market economies throughout both regions. Institutions such as the World Bank, IMF, EBRD, and LABD have been key players in this effort. Despite their efforts however, they have not been able to systematically bring about institutional reforms and change to ensure the stability and functionality of these new markets. How, then can the cases of Poland and Argentina inform developmentalists about methods of creating and facilitating institutional reforms and stability? An important variable in the Poland/Argentina comparison is their membership in very different geopolitical blocs. Poland's acceptance to the EU and Argentina's membership in MERCOSUR has meant that they have been integrated into regional political and economic systems in significantly different ways. However, even with this observation considerable ambiguity still surrounds the precise role of international actors in each country's reform process. This paper will argue that the differences in institutional development in Latin American and Eastern European countries can be explained by the different types of conditionality and compliance mechanisms employed by their respective regional hegemons. These mechanisms of conditionality and compliance are most common and necessary when regional players form political and economic integrational regimes where there is a clear discrepancy across member states in terms of stability, prosperity and competitiveness. This can be conceptualized in terms of "big brothers" and "little brothers." The big brothers represent advanced 1st world countries entering into regional agreements with poor, backwards countries whose economic and political systems are vastly behind those of their partners. Given this framework, the EU integration regime and the NAFTA integration regime have been chosen as the subjects for comparison used in this paper. Both regimes place similar expectations for economic reforms on little brothers but differ significantly in the amount of political commitment and conditionality employed. Consequently, the accession of Eastern European countries to the European Union and the NAFTA agreement provide excellent cases through which to understand institutional development.

Outline/overview

This paper will begin by reviewing the literature on institutional development in 3rd world countries. These theories point in a very specific direction regarding the predicted reform paths and results of little brothers subjected to a regional integration regime. While strong economic and political incentives undeniably lay the foundations for necessary economic and political reforms, the catalyst for a little brother's institutional reform is the extent to which their big brother imposes conditions upon them and ensures the satisfaction of these conditions. The importance of conditionality and compliance thus transforms integration regimes into development regimes whose robustness depends upon the extent to which big brothers incorporate and dedicate precious resources to these two crucial elements.

The second section will look at institutional trends observed among Hungary, Slovakia, Slovenia, Poland, the Czech Republic compared to Mexico, Argentina and Brazil to support the hypothesis that international geopolitical factors have had a lasting effect on institutional development in these two regions. The third section discusses the NAFTA agreement and the EU accession process in depth, offering an explanation and understanding of these different effects through the varying use of conditionality and compliance in the design of their integration agreements. Finally, a discussion of the development of phytosanitary institutions under each integration regime provides an elucidating case study to further demonstrate the ways in which integration regimes can become institutional development programs.

Section I: Theory/Literature Review

Theory I: The economic incentives theory

The literature on institutional development offers two main schools of thought about the effect of international integration regimes on domestic reforms. The first of these is functionalist/neofunctionalist theory. This theory is based on the idea that institutions are created and developed when economic elites pressure the state to do so. These economic elites are created by the opportunities presented when countries liberalize their capital and current accounts. In order to maximize the gains offered by liberalization and integration, these elites will lobby for the creation of institutions to further coordinate and increase integration.[1] Garett provides an example of this by explaining that important economic actors, notably multinational corporations, will not remain in a country if a local market does not have the institutions needed to protect property rights or enforce the rule of law

[1] M&M

which are vital to the functioning and efficiency of business. This incentivizes states to develop institutions in order to increase trade competitiveness and secure the FDI opportunities presented by liberalization.[2] This idea is supported by the concept of policy anchoring. Policy anchoring is the idea that trade agreements provided strong enough economic to ensure that politicians will comply with treaty rules in order to provide consistency and predictability in their actions.[3] In a 2003 report, the World Bank points out that liberalization and trade integration provide a set of rules and understandings between countries for their mutual benefit which is expected to "trigger reforms on other fronts as well." Indeed, the idea that policy anchorage would make it easier for politicians to push through unpopular but necessary institutional reforms was one of the primary motivators of the North American Free Trade Agreement between the United States, Canada and Mexico.

Despite the popularity of this "economic school of thought," functionalist and neofunctionalist accounts leave the type, process and extent of institutional development unclear. On the one hand, if these ideas about the role of economic incentives play themselves out, it could lead to what is called the "race to the bottom;" on the other hand, it could also lead to the "market-making state." In the first scenario, the state is seen as a danger to the new economic groups who are supposed to lobby for the desired institutional changes. Wiengast refers to this problem as the "self-preserving state." As economic elites gain independence from the state through economic liberalization, the state tries to weaken them and resist their demands for reform. The solution to this threat is to downsize the reach and power of the government; the minimizing pressures placed on the public economy consequently leads to a "race to the bottom" with an ever-shrinking state, making institutional development increasingly difficult and unlikely.

Doner et. al provide an alternative prediction about liberalization and the architecture of the state after functionalism has worked its magic; in Doner's view, institutional development the result of a "developmental state" which ultimately arises when political elites recognize that tense domestic political conditions can be solved

[2] Garett
[3] Tovias and Ugur

through developing institutions which reorient domestic exporters' strategic trade positioning within a liberal economic framework. While this account shifts the emphasis from private actors to planning and implementation by political elites, this account of institutional development leaves external actors in a standby position at best. Advanced countries trying to help recreate the developmental state described by Doner would have to more often than not watch and wait on the sidelines rather than actively engage poorer countries to put in place institutional reforms.

The second underlying problem with all of these theories is that they are ultimately unrealistic. Both state and market actors can be predatory; whereas supporters of functionalism/neofunctionalism only warn about the tendency for the state to block reforms, newly created economic elites can also pose obstacles to reform efforts. Moreover, scholars such as Lazlo Bruzt point out that the "developmental state" and the "market preserving state" are outdated concepts from the 19th century. The alternative picture of the modern state which Bruzt proposes looks radically different from the minimalist picture painted by advocates of functionalist/neofunctionalist accounts. Rather than a minimalist apparatus whose sole purpose is to protect property rights and the rule of law, the modern state contains a panorama of institutions in a wide array of social and economic sectors. Government and its institutions have the ability and obligation to redistribute resources and prevent economic actors from allocating resources to themselves through the exploitation of unfair advantages. However, in addition to subjecting societal actors to multiple accountability mechanisms, the state is also subject to horizontal and vertical accountability from civil society groups, business groups, and the general population. The resulting combination of heterarchical context and a strong regulative capacity should thus be the ultimate ending point of institutional development efforts.

The political incentives theory

Attempting to address this flaw in functionalist/neofunctionalist theory, a second school of thought has been created to emphasize the importance of political incentives in enabling institutional change. Kopstein's study on the effect of geography on economic and political reform in post-communist Eastern Europe provides strong evidence in favor of this notion. His study finds that geopolitical factors, notably a country's openness and freedom score and spatial proximity with the West, are statistically significant indicators of how likely states are to reform. Given the importance of location and external context on domestic reform, Levitsky and Way study 12 different countries across continents to specify under what conditions international pressures on poor countries are most effective. They argue that a combination of economic, social and political ties to the West mediate the effect of diplomatic pressure, conditionality and military pressure on domestic reforms. According to their research it is the combination and strong presence of both economic and political leverage which provides the most fruitful results. In their comparison, Slovakia is singled out as the country most responsive to Western leverage. It is most successful in implementing democratic reforms precisely due to its significant linkages and intense subjection to political leverage from international Western actors. Their choice of runner-up points in an even more interesting direction however. Mexico is identified as the runner up because although it had significant linkages to the West it was not subject to as much political leverage as Slovakia. This result does not negate the economic incentives theory totally- to the contrary, Mexico fares better than countries with high political leverage and low economic and social linkages. However, Mexico's second-place status also suggests that high economic and social linkages created through integration regimes are not enough to motivate institutional change.

The apparent importance of political incentives through the use of pressure, carrots and conditionality also raises questions about the exact nature of this "leverage." Levitsky and Way generally define leverage as diplomatic pressure and military pressure. But what exactly does the international partner pressure for, and how do they know? There is heated debate about whether or not democracy comes before economics or economics before democracy, or if they should occur simultaneously. The exact type and depth of democracy demanded of reforming countries is not specified by this theory. Secondly, there is no discussion of how the international partners know whether or not their demands have been met. The importance of satisfying political demands can be understood through the success and failure rates of international economic reform programs; contrary to the effects predicted by policy anchoring, non-compliance with IMF deals actually increased from about 50% to about 72% from the 1970s to the 1990s.[4]

However, scholars such as Milada Vachudova do not take these statistics as evidence that conditionality is ineffective in creating development. To the contrary, Vachudova emphasizes the importance of the use and sequencing of conditionality on institutional outcomes. In this theory, the economic "winners of partial reform" present the first major obstacle to institutional reform. The only way to overcome their resistance is to establish a competitive democratic system with political turnover. This serves as a precondition to the satisfaction of all subsequent institutional reform conditions. Of course, in order for this pre-condition and the subsequent conditions to be met, the perceived benefits of satisfying the conditions must be considerable. This is what Vachudova calls "passive leverage," a concept which refers back to the idea of strong political leverage and incentives. Additionally, once a politically competitive system is established, extensive specifications outlining the type, nature and look of institutional reform must be imposed upon the "little brother" and actively monitored and enforced. Vachudova refers to this as "active leverage." Exactly how does one monitor in a way which ensures compliance? Critics such as William Egerly who expose the international community's overall inability to bring about effective change in 3rd world governance structures argue that after specifying conditions, the big brother does not always stick around to ensure that conditions are met.[5] This can be referred to as the "big brother commitment problem." Secondly, how will they avoid multiple agent problems and ensure enough accountability in domestic politicians to ensure compliance? This is the "little brother accountability problem." Vachudova provides 3 answers to these monitoring and compliance problems. The first of these, asymmetric interdependence, refers to the incentives poor countries have to do what the big brother specifies because the big brother is bigger, better and offers them a political prize. Secondly, meritocracy during the monitoring process is key because political elites are more likely to go ahead with costly and painful reforms if they perceive they are being evaluated fairly. Finally, the enforcement of extensive conditions is critical. However, enforcement and compliance

[4] Tovias and Ugur
[5] Egerly

deserve a more in-depth discussion of their own because they do not rely solely upon political incentives in order to function. Rather, enforcement and compliance involve monitoring, learning and a considerable level of commitment.

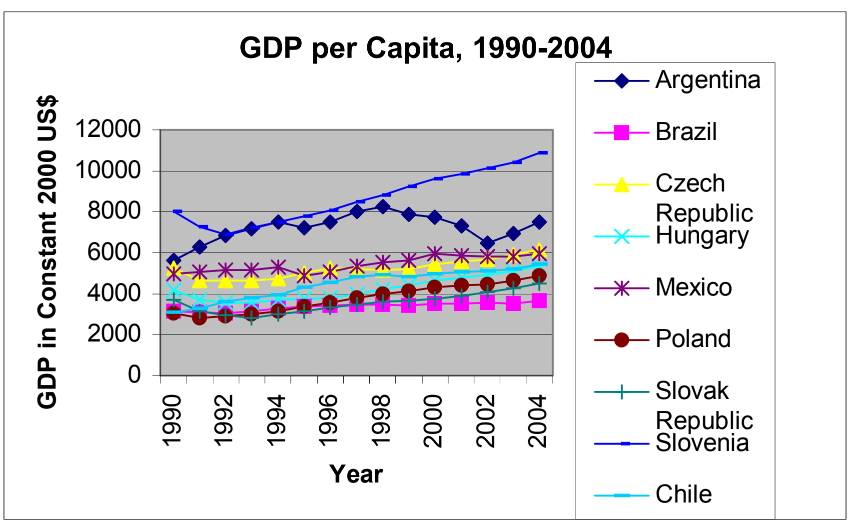
The monitoring necessary to ensure compliance with institutional development is an inherently innovative reformational and learning process. Moreover, the amount of innovation and learning for institutional reform is even greater than usual because it requires getting poor countries out of a long-term political-economic equilibrium trap. This undermines the stability of relations between the monitored and the monitor because innovations threaten the control of their subordinate agents. Charles Sabel and Jonathan Zeitlin argue that the breakdown of monitorability can only be attained by making monitoring and learning undistinguishable. Monitoring institutions must turn transactions into discussions, suggesting a continuity and fluidity of monitoring efforts. By jointly setting and evaluating the attainment of goals, the gap between an agreement and its execution is narrowed. This self-joint-monitoring scenario also reduces the multiple agent problems and accountability loops that are typically created by situations where the monitors impose standards requiring innovation upon the agent. By creating an ongoing discussion about goals and efforts to reach those goals, the monitor is able to learn enough about the agent to reasonably identify which agents to hold accountable, revise criteria to make them more reasonable, and create measurable evaluation metrics. As Wade Jacoby shows in his study of Eastern European institutional reforms, this also brings the principal close enough to the agent to distinguish when non-compliance originates from a lack of resources or technical expertise and when it originates from a lack of political motivation.

The combination of the political incentives theory and the need for strong conditionality, compliance standards and a monitoring-learning mechanism suggests that in order to bring about institutional development some sort of supranational institution must be created. Such an institution would set and revise criteria as well as monitor and provide financial and technical resources to ensure compliance. Given that this supranational institution would need to incorporate Bruzt's idea of the modern state as a final goal, the amount of effort and resources advanced country big brothers would have to channel to this effort are considerable. This also puts greater stress on existing political energies and institutions in the advanced country-partners. However, the upside to this theory is that the incorporation of conditionality and compliance into a regional agreement can transform the regime into an institutional development model.

Section II: The Lasting Impact of Geopolitics on Institutional Development

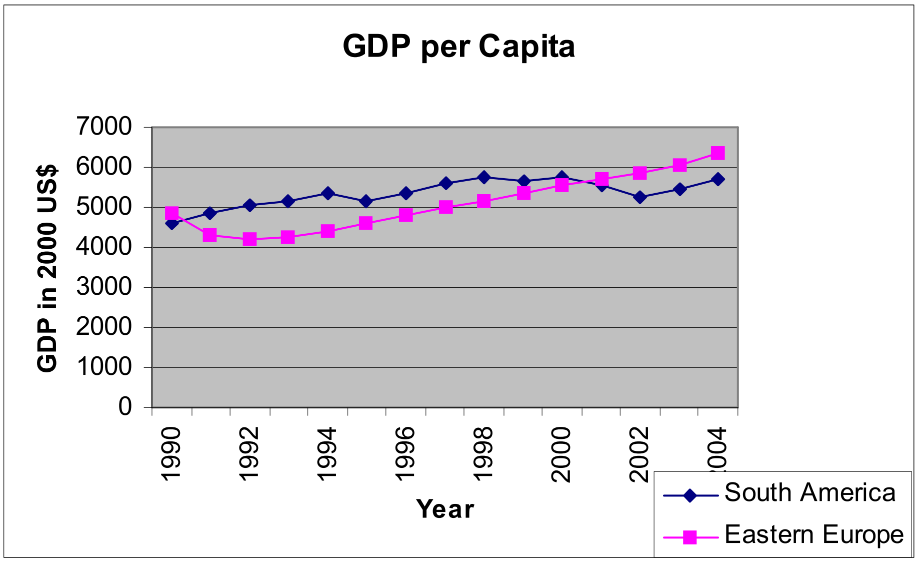
Despite the varying theories which look at the role of international actors in poor country development, there are still a large number of skeptics as to the effectiveness of international efforts. Most of this skepticism is rooted in the idea that reforms take place on a local level and as such are unaffected and uninfluenced by international and external factors. While this observation holds some truth, the conclusions it draws are misguided. Economic development, as well as institutional development, have been remarkably influenced by international geopolitical factors in Eastern Europe and Latin America. This impact is best seen through the consistent out performance of post communist countries on a variety of institutional and economic measures. Since the 1990s, Eastern European economic have improved much more than those of Latin America:

GDP



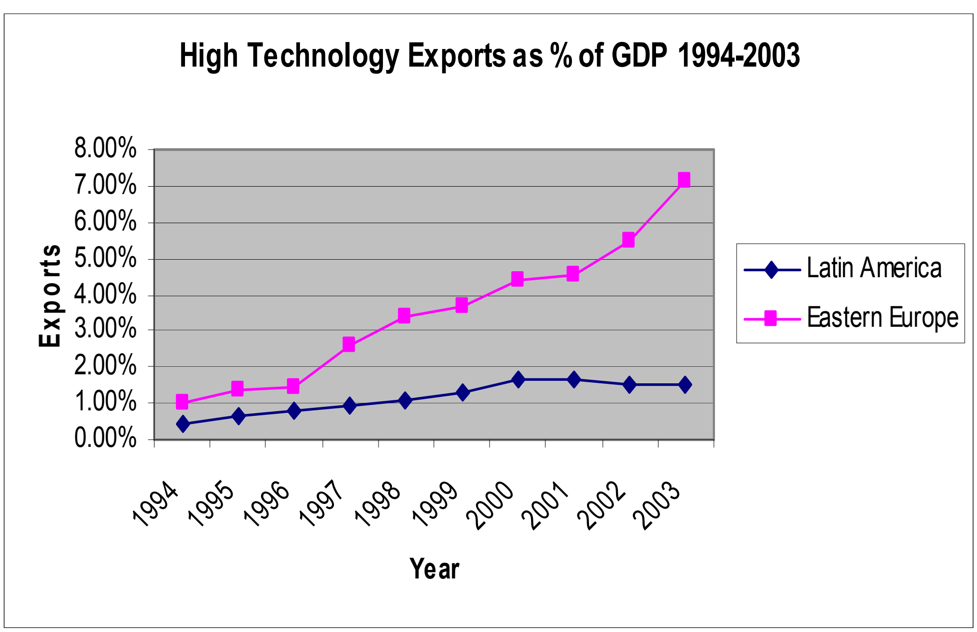
Source: World Development Indicators online

While Slovenia's growth has been the most impressive, Poland, Hungary, the Czech Republic and Slovakia have also improved consistently over the 1990-2004 period. Brazil's growth seems close to flat, with Argentina and Mexico's GDP/Capita exhibiting fairly volatile fluctuations. Moreover, it cannot be argued that these effects are solely due to income effects from differing starting points, as Argentina and Mexico started out with higher GDP per capita than four of the five Eastern European countries. Brazil started on par with three of the four Eastern European countries. This trend can be seen clearly on a regional basis as well: figure 2 shows that as a region, Eastern Europe is becoming wealthier than Latin America since the 1990s.



*Eastern Europe includes Slovakia, Slovenia, Poland, Hungary and the Czech Republic. Latin America includes Mexico, Chile, Brazil and Argentina. Source: WDI online

Another way of measuring successful economic performance is to look at the percentage of high technology exports, which contrasts even more starkly with Latin America than GDP.

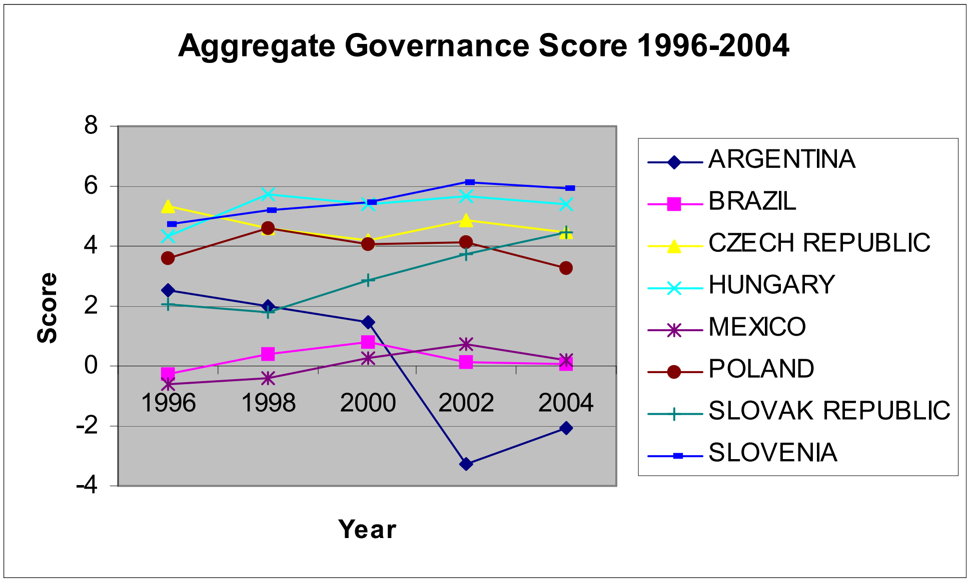


*Eastern Europe includes Slovakia, Slovenia, Poland, Hungary and the Czech Republic. Latin America includes Mexico, Chile, Brazil and Argentina. Source: WDI online

These graphs show that economic success is influenced by geopolitical factors. However, these emerging regional trends extend beyond economic factors and apply to political indicators as well. One indicator of effective politics on a general country-level is the Freedom in the World survey of Freedom House. The scores for political rights are meant to assess people's ability to participate freely in the political process, including elections and holding politicians accountable through elections. Civil liberties rankings are meant to indicate the extent to which there exists free expression, freedom of organization and association, as well as rule of law and personal autonomy from state interference. Both categories have a ranking of 1-7, with 7 being the least degree of freedom possible. On the freedom house rankings for 2006, Argentina, Mexico and Chile all rank "2" on a scale of 1-7 for political rights and civil liberties, whereas all of the CEE 5: Czech Republic, Hungary, Poland, Slovenia, Slovakia rank 1 for both categories. Brazil ranks 2 for political liberties and 3 for civil liberties. Again, Eastern Europe beats Latin America.[6]

Institutional trends across regions show themselves to be even stronger than political ones. World Bank data from Kaufmann, Kraay and Mastruzzi measuring institutional quality demonstrate high performance in terms of institutional rankings in Eastern Europe and poor performance in Latin America in comparison. An aggregate governance score consisting of metrics on rule of law, corruption, voice and accountability, government effectiveness and regulatory quality shows that Latin American countries have stayed below par at best and deteriorated at worst over the 8 year period from 1996-2004.

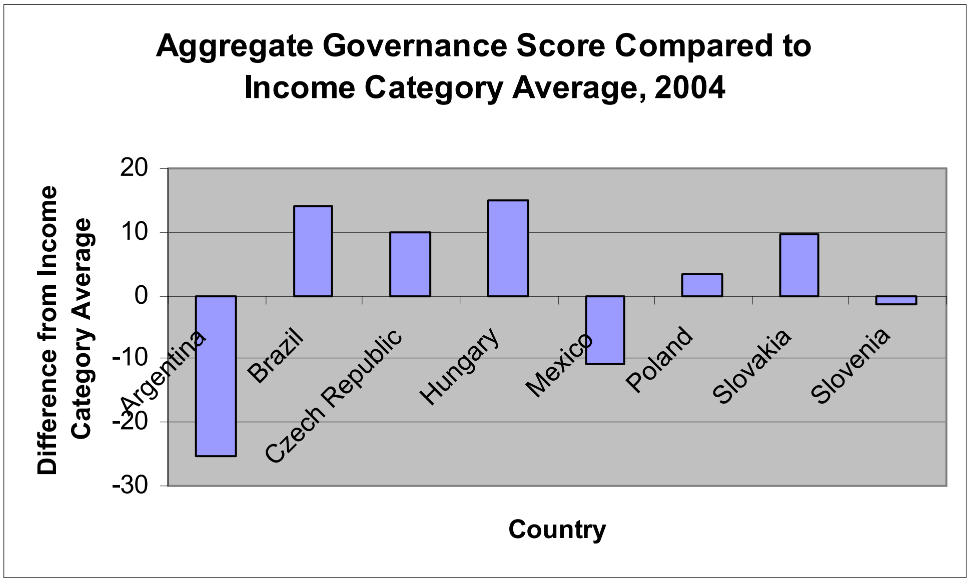
[6] http://www.freedomhouse.org/uploads/Chart33File36.pdf



Kaufmann, Kray and Mastruzzi 2005 (data retrieved from http://www.worldbank.org/wbi/governance/govdata/index.html)

While Poland and the Czech Republic have shown a slight deterioration in overall ranking, none of the Eastern European countries have shown a drastic decrease, with consistent increases in the other three instances. Moreover, it is interesting to look at Slovakia and Argentina, who start off with relatively similar rankings in 1996 and finish with enormously disparate rankings by 2004.

However, one must also control for income effects when looking at governance scores, as one could argue that the variation in performance across regions is the result of different levels of wealth and resources in each country. Even after controlling for GDP however, the picture remains the same: Eastern European countries tend to outperform their income category, while Latin American countries under perform.



* Brazil belongs to low-income category, Slovenia to high income category. All the rest belong to upper-middle income category.

Regional trend data support these two analyses: if one looks at the World Bank data on a regional comparison basis, Argentina, Mexico and Brazil do well relative to their regional category. Given that the CEE-5 consistently outperform both these three countries and their own income average, this means that the CEE-5 region performs fantastically well compared to Latin America on a regional basis.

One last and final comparison drives home the point that international, geopolitical factors have had a lasting impact on institutional development in poor countries. The table below provided from Mosely, Uno and May's study of labor rights violations and protections shows the typical picture of Eastern European success compared to Latin American disappointment.

Figure 1: Average Labor Rights Scores, by Region

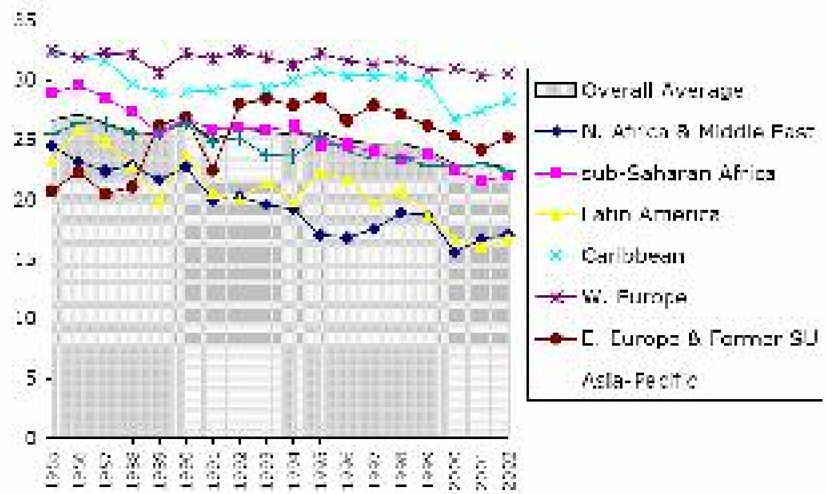
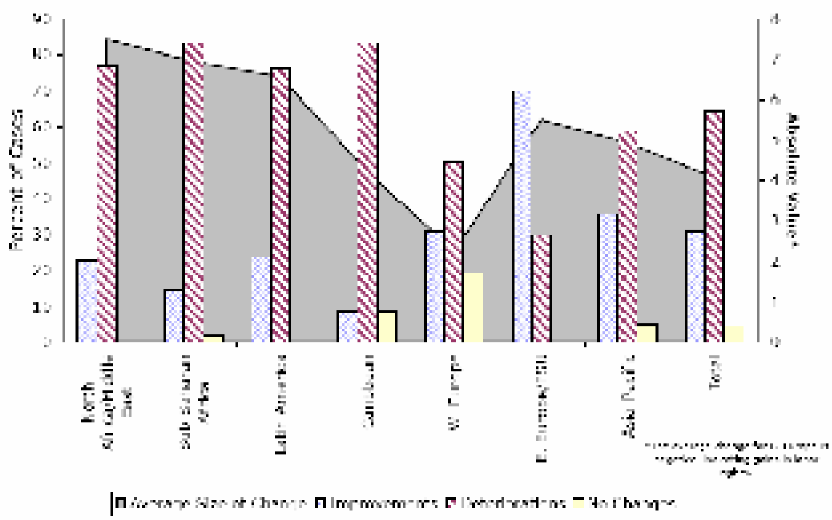


Figure 2: Changes in Labor Rights Scores, 1985-2002



It is interesting to note that while the authors do not find that neither stocks or flows of FDI, international trade levels nor external debt are significant predictors of labor rights' violations, the graphs show a clear distinction between the performance of Latin American countries and Eastern European countries. Additionally, they found that in addition to internal factors, a "regional variable" exhibited a significant correlation between averages of violations among neighbors or economic peers. The authors suggest that this indicates the presence of a mechanism of "competitive diffusion" and an influence of "what others are doing." In this analysis, it is the competition for the FDI rather than the existence of the FDI itself which motivates countries to "race each other to the bottom" by laxing their labor standards. External, international influences and factors are therefore important in this economic policy area as well.

Some critics say that this comparison is unfair because Eastern European countries started out at a better place than Latin America because of their communist legacies. While these countries were under communist rule long enough to inherit sate bureaucracies, this did not mean that state predation would be easy to unlearn or that the concept of consumer protection would be easy for Eastern European governments to understand and embrace. This is demonstrated by the less than stellar performance of these countries on survey questions distributed by BEEPS in 2002. Table 1 shows the responses of business owners to questions about their confidence in the government's capacity to uphold their property rights and contracts, rule fairly on court cases and interpret regulations impartially. Overall, relatively positive rankings (tend to agree or better, frequently or better), while hovering between 50-60% can go as low as around 30%. This means that in 2002, despite the communist legacy and the bureaucracy that would supposedly have turned itself around into a lean mean, regulatory machine was not quite transformed yet. Moreover, Kaufmann's data also show that Latin American countries performed more poorly than Eastern European countries even when they started out at the same or comparable place as Latin American countries. This means that Eastern Europe must have benefited from international aid in a way which Latin America has not in order to achieve successful institutional improvements.

Section III: Understanding Diverging Institutional Performance in Latin America and Eastern Europe: the NAFTA and the EU

The next section is dedicated to understanding the consistent differences across Latin American and Eastern European institutional development. As the first trade integration regime to combine underdeveloped and advanced country partners, the North American Free Trade Agreement provides a Latin American case for study. As the first five poor European countries to enter the European Union in 2004, Slovakia, Slovenia, Poland, Hungary and the Czech Republic (these will be referred to collectively as the CEE-5) provide the Eastern European cases for comparison. While an overview of the types of economic and political incentives in each region's integration regime shows a varying degree of intensity across the two cases, it becomes apparent that these differences alone cannot explain the difference in institutional performance. Institutional development theories help elucidate this difference, with an additional in-depth focus on the use of compliance and conditionality mechanisms providing the missing link to understanding the factors at play.

To start off, it is easiest to understand the different types of economic and political incentives provided to poor country partners in the NAFTA and EU integration regimes with the following comparison:

Integration blocs are a group that agrees to do one, several or all of the following:

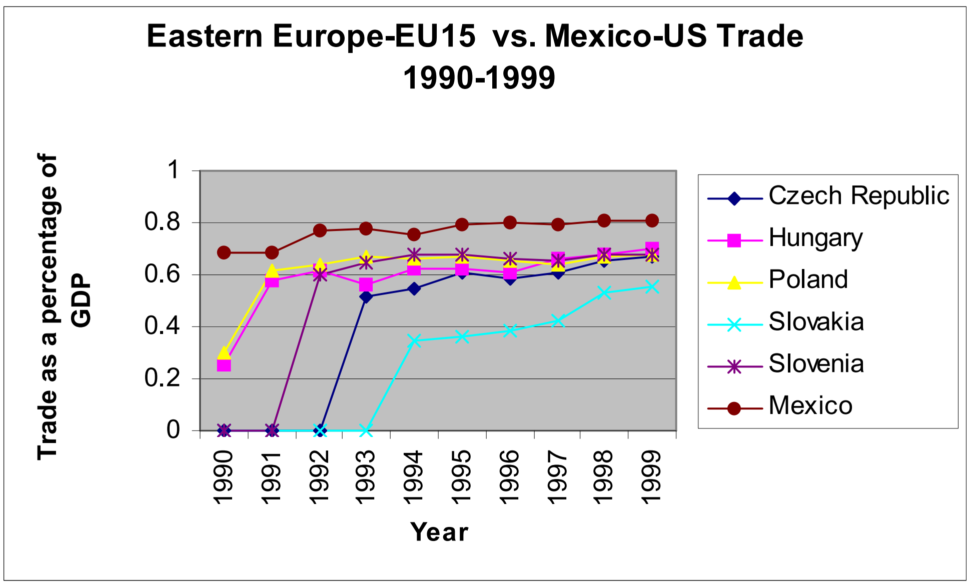
1) Remove internal trade barriers
2) Coordinate external trade barriers to constitute a customs union
3) Allow for the free movement of capital
4) Allow for the free movement of labor
5) Coordinate indirect tax policy
6) Coordinate regulatory and competition policies
7) Introduce a common currency
8) Coordinate macroeconomic policies
9) Coordinate foreign and defense policies

The EU meets criteria 1-8

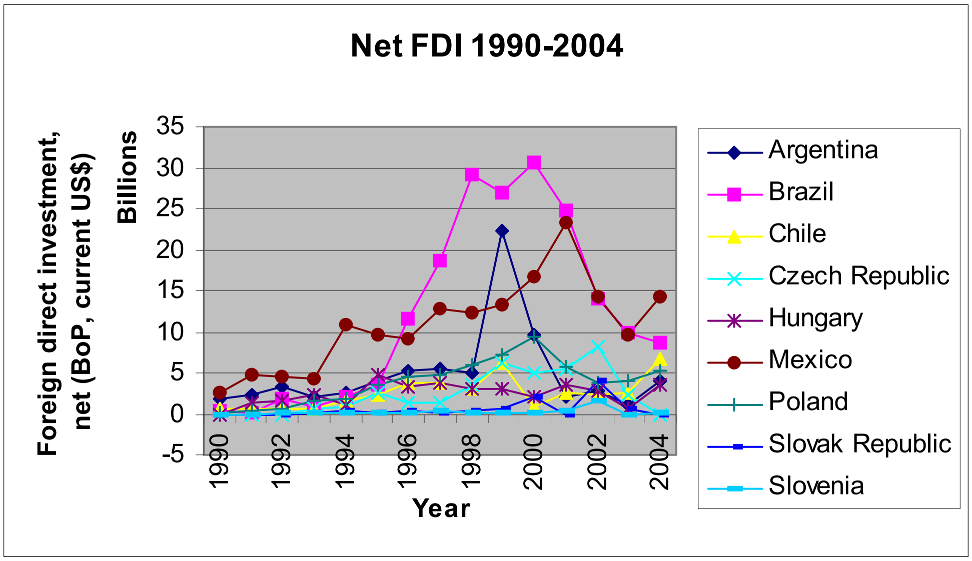
NAFTA meets criteria 1 and 3

MERCOSUR meets criteria 1-3

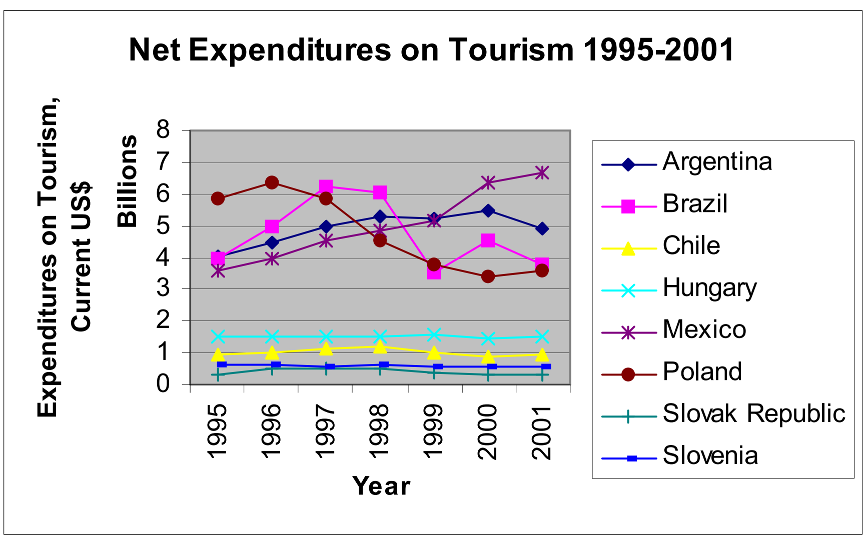
Clearly, the political incentives are strongest for Eastern Europe. The accession process provides more comprehensive integration opportunities than the NAFTA, and among these opportunities, the common currency and free movement of labor are particularly attractive. Though one might assume that this is also the case for economic incentives, a closer look provides contrary evidence: Mexico is undoubtedly more economically integrated with the US than the CEE-5 are with the EU in terms of current accounts.



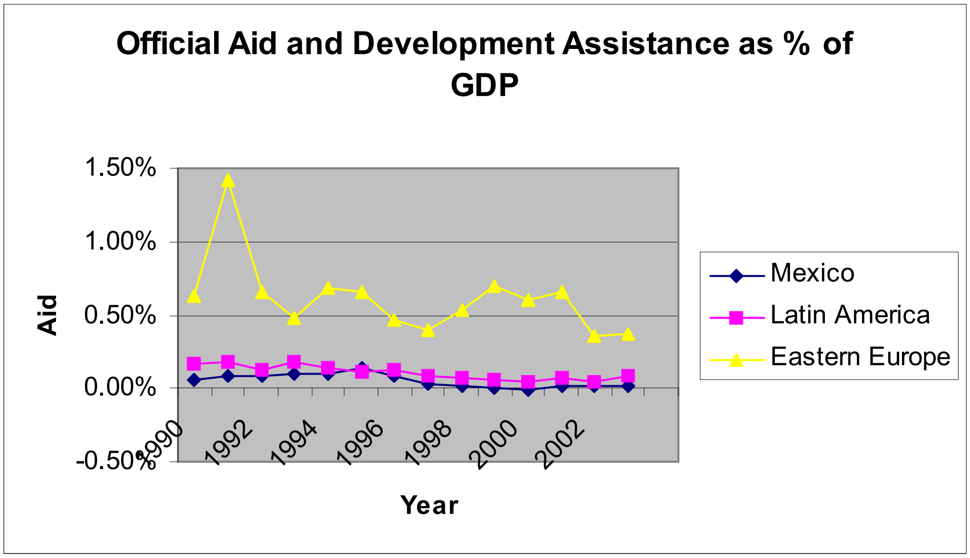
Mexico both starts out and ends up with a larger percentage of more integrated with the US than Eastern European integration with the EU. Latin American countries have also experienced more FDI than their Eastern counterparts as shown by figure 2.



The amount of money received through tourism in Latin America is only matched by Poland. However, it is still clear that the economic incentives for Latin America to converge with the West are greater than those for Eastern Europe.



According to the neofunctionalist/functionalist school of thought, then, Latin America's governance scores should have been higher than those of the CEE-5 even though this has obviously not been the case. The political school of thought explains this outcome by attributing institutional development to the stronger political incentives presented to the CEE-5; as can be seen in figure 3, vehicles for reform such as foreign aid have been much higher for Eastern Europe than Latin America.



However, the answer cannot simply lie in the amount of foreign aid received and policy harmonization poor countries implement. If this were the case, Latin America and other poor regions should have been developed by now with one of the IMF or World Bank's myriad of development programs. The only way to explain and understand this puzzle is to see in what ways the neofunctionalist/functionalist account has or has not played out in Mexico, and to what extent the political incentive story and conditionality mechanisms have come true for the CEE-5.

Case #1: The NAFTA

<u>**Economic elites and institutional development: the race to the bottom meets the market-preserving state**</u>

Policy anchoring, or issue linkage, was seen as one of the major benefits that a free trade agreement with the United States was believed to confer upon Mexico. NAFTA would help justify necessary economic reforms and tie the hands of the government in favor of improving investor confidence in the political and business environment.[7] This was because the agreement gave economic reforms the status of national law.[8] As demonstrated by the graphs from the previous section, NAFTA has enabled economic reforms to the extent that Mexico has seen remarkable export and FDI. Palma supports this idea that a NAFTA-led FDI increase has fueled the expansion of Mexico's successful maquila sector in manufacturing.[9] This would "give consumers of all three nations a wider variety of goods at lower prices and to make North American industry more competitive by enlarging its markets.[10]" This market enlargement is seen to be directly linked to the de-statization of enterprises and de-regulation while at the same time making sure that the pricing mechanisms in markets can operate freely without government interference.[11] This frees up the market for the creation of regulations and institutions which take a less interfering and more effective approach to monitoring markets. It would also generate the wealth necessary to produce a critical mass of economic elites who would pressure for state reform.

According to the economic school of thought, what should have happened in Mexico after NAFTA is the following: as liberalization and integration increased among NAFTA partners, the new domestic actors benefiting from liberalization and integration would pressure the Mexican state to establish institutions to enforce disputes, correct international market failures and coordinate policy to increase integration. This prediction has only proved correct on a very minimal level. Firstly, across-the-board improvements in institutional quality have not materialized from 1996-2004, as shown by Kaufmann et al's institutional indicators. Moreover, a 2003 World Bank report on NAFTA shows that the treaty has not been able to help Mexico become an innovator or leader; rather, Mexico has fallen behind as a "follower." The report concludes that "the income gap between the U.S. and Mexico can be largely explained by the institutional gap plus geographic variables…there is not evidence that Mexico's institutions improved more than others from Latin America in the post NAFTA period."

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[7] Interpreting NAFTA
[8] Royo, p.15
[9] Palma, p.4
[10] Royo, p.10
[11] Laszlo, p.128

The only institutional arrangement triggered by NAFTA was the result of political lobbying on the part of mainly US-based environmental and labor interest groups, not economic elites benefiting from the treaty. The continuation of this program was also upheld by national institutional initiatives rather than economic elites' pressure on states. This sole developmental NAFTA initiative called the Border XXI program was established to accomplish goals geared towards 10 general principles outlining environmental concerns along the US-Mexico border. These projects were coordinated by three regional institutions specially created from NAFTA: the North American Commission for Environmental Cooperation (CEC), the Border Environment Cooperation Commission (BECC) and the North American Development Bank. Projects were supported and coordinated on a localized level along with the backing of national and regional institutions in both the US and Mexico. The management and preservation of resources were not directly addressed by Border 2012; rather, project implementation mobilized the help of "workgroups" which consisted of a mix of representatives from local communities on both sides of the border, the three NAFTA-created bi-national institutions, NGOs, community-based organizations, academics and different levels of government from Mexico and the US. Under Border XXI, nine such workgroups focused on particular border-wide environmental issues. Under the follow-up Border 2012 program, four such workgroups continued these tasks. [12] This was in line with the expectation that NAFTA would encourage greater environmental cooperation between the US and Mexico as a side effect now that the economic incentive to locate industrialization only along the border was reduced.[13] However, programs for Border 2012 were targeted mostly at directly improving

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[12] 2012 US-Mex border report
[13] Interpreting NAFTA, pp. 221,222

environmental indicators and businesses' self-regulation and compliance rather than enhancing the capacity of Mexican institutions to do so. Monitoring mechanisms for these projects were also fairly weak: enforcement mechanisms entailed status reports once every two years plus a 5-year report. National coordinators such as the SEMARNAT (in Mexico) and the EPA (in the US) were selected to discuss and agree upon evaluation metrics and occasionally monitor projects according to these metrics. Funding from national sources depended upon requests to the legislatures of each country and varied from year to year. The accountability issues created by such diverse workforces and general principles were partially offset by fairly clear and measurable goals outlined in the Border 2012 report. However, a summary report indicates that these specifications were not enough:

"In carrying out their mission, the BECC and NADB face the following fundamental challenges on both sides of the border:

- Lack of comprehensive master plans and inadequate preparation of proposed projects
- Limited financial, administrative and operating capabilities of some local agencies responsible for providing water, sewage and sanitation services
- High cost of projects and insufficient community sources
- Inadequate revenue for the sound operation and maintenance of existing systems, coupled with resistance to user fee increases
- Insufficient interest and limited success with private sector participation"

In an attempt to resolve these problems, a reformed charter for the BECC-NADB was created in 2004; whether or not the expanded jurisdiction, new 10-member board of directors and increased grants from NADB's paid-in capital will be enough to revamp the program is yet to be seen.[14]

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[14] BECC/COCEF Join Status Report

Labor is the other sector in which NAFTA negotiations attempted to go beyond mere rules of origin and tariff specifications. However, no institutional initiatives similar to Border 2012 were created to address labor concerns. The result of the fierce negotiations and lobbying by US labor interest groups and Mexican businesses was the establishment of a minimum wage pegged to productivity for Mexican workers and the subjection of certain labor disputes to stricter punishment standards than normal treaty violations.[15] Nothing about institutional development for the labor sector was specified in the treaty. Although the World Bank report on NAFTA argues that "cautious optimism" is warranted in this sector due to a slight wage increase, the report also singles out that the agreement did not spur significant changes in Mexican labor codes or institutions to enhance the capacity of labor markets to adjust to changes in a more open labor market.

With the exception of environmental sector issues, it seems that the NAFTA has produced more of a "race to the bottom" effect that any other prediction associated with the economic school of thought. In the one sector where this has not been the case, it was political interest groups, not economic elites, which took the initiative to pressure the state to develop institutions. Moreover, the Border 2012 program still faces significant challenges related to the implementation and enforcement necessary in order to make the program successful.

The Market-Preserving State- NAFTA's minimalist design

At the time of NAFTA's creation, Mexico was a democratic one-party state. While there were no preconditions specifying the need for a politically competitive or open system in order to participate in the treaty, the dispute resolution mechanisms established by the treaty indicate that the signatories had the market preserving state in mind. The political system in Mexico was irrelevant to institutional convergence as long as certain minimum standards upholding the rule of law, patent protection and CVD/AD measures would be honored. NAFTA created a regional dispute settlement mechanism (DSM) in an attempt to ensure that these standards would be upheld. Yarborough and Yarborough identify the majority of NAFTA monitoring and compliance mechanisms as DSM II. This

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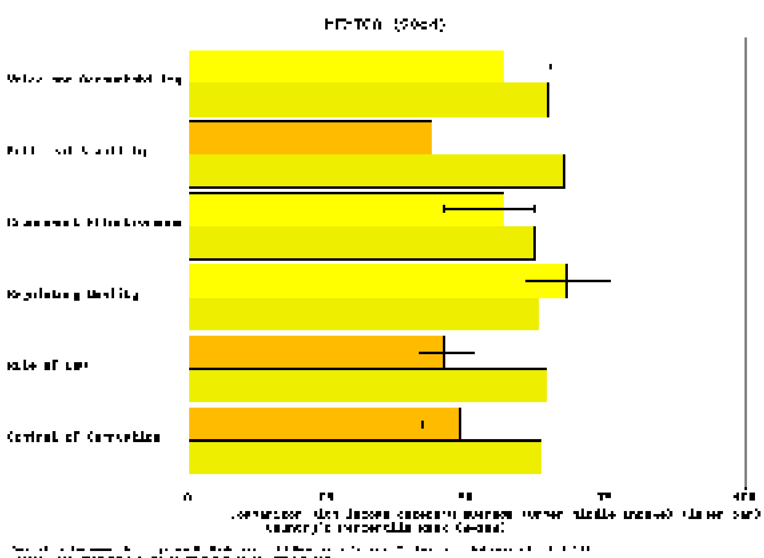
[15] Interpreting NAFTA

is an arrangement where all disputes except for dumping, countervailing duty, and investment cases are monitored and identified by a third-party mechanism which recommends the resolution details but leaves enforcement up to each party. Noncompliance can result in sanctions retaliation by the relevant party, potentially expanding the conflict. Only NAFTA's chapter 19 on antidumping and countervailing duty investigations employs DSM-III, where third party adjucation is binding and retaliation is not possible after a not-guilty finding, with an appeals process substituting the sanctions process in the event of non-compliance.

Neofuncitonalists/functionalists might argue that DSM mechanisms should serve as a stimulus for improvements in Mexican court systems to harmonize their legislation and improve their capacity. Indeed, the only institutional indicator for which Mexico showed a gradual, consistent increase was "voice and accountability," suggesting that perhaps there has been a slight "market preserving-state" effect. Anti-dumping and countervailing duty judgments have been generally complied with despite the ambiguity of national laws on this subject and despite NAFTA's lenience in allowing for evaluation standards to be set by each country's national AD/CVD standards. However, the "rule of law" under this arrangement is fairly weak, as panels can make judgments but cannot enforce them, resulting in a large, unresolved trade dispute between Canada and the US.[16] This is echoed by Mexico's poor scores on "rule of law" and "control of corruption" in Kaufman's indicators relative to its income category in 2004.



[16] WB report, p.104

If these indicators are tracked for Mexico over time, Regulatory Quality and Rule of Law scores show a decrease from 1996-2004. Consequently, the best way to describe the outcome of NAFTA is a hybrid mix of the benefits and downsides of the economic school of thought, with most elements taken from the race to the bottom and a few from the market-preserving state. This is hardly the development story which economists and political scientists had expected for Mexico at the outset of the 1990s.

Case #2: The CEE-5

Incentives, conditions and compliance "a la Copenhagen": a path of institutional development

An extremely political model since its inception, accession to the EU was considered to be a "return to European roots" by Eastern European countries. However, if one looks a bit further, it becomes clear that the EU is more than just an exclusive "club."
At the beginning of the EU accession process, the EU regional integration regime actually resembled that of Mexico and NAFTA. In 1990 the EU did not have a set plan for admitting less developed countries in the East; it simply used trade agreements (called the Europe Agreements) as a way to establish bilateral economic ties and political relationships. Though the Europe Agreements' more general goal was to prepare Eastern European countries for eventual accession, these agreements focused on tariff reductions, subsidy allowances, and other details regarding bilateral trade. Countries participating in these agreements included Hungary, Poland, Estonia, Czechoslovakia, Latvia, Lithuania, Romania and Slovenia. Within the framework of the committees established under these treaties, the terms and implementation of EU accession were explained to Eastern countries; however, this did not in any way constitute a concrete plan for entry into the EU.[17]

In addition to the trade agreements, the European Community established the PHARE programme in 1989. At the moment of its inception, the PHARE program was

[17] EU agriculture and enlargement summary

designed to provide financial support to Hungary and Poland so that they could rebuild and reform their economies. Their application was general and used for the overall goal of economic reform.[18] Granting of the funds was demand-driven, creating fragmented and difficult to manage projects.[19] To assist with this difficult task of both enabling and implementing widespread and lasting reforms, a joint program between the OECD and the European union in 1992 was established to help countries modernize their public management systems. Known as the Sigma program, it used the EU accession process as a basis from which to assess the progress of country reform and worked exclusively with national administrations in candidate countries. PHARE funds were used to finance the Sigma program as OECD and EU officers published Regular Reports, Comprehensive Monitoring Reports, and helped decision-makers in public and administrative positions set up organizations and procedures consistent with European values and standards. The partnership with the OECD was meant to bring in experts and a comparative perspective to help with project designs meant to reform government administration.[20] The Sigma program was limited in scope, however, and up until 1993 the Europe Agreements had been the basis of a relationship between Eastern and Western Europe which was more diplomatic and geopolitical than conditional and developmental. With the Europe Agreements and PHARE, the EU accession process was nothing more than a trade and aid regime.

Political Incentives:

It was at the Copenhagen European Council in 1993 that the accession process began to include political conditionality and began following the predictions of the political incentives theory. At a conference in Denmark, the Union took a decisive step by declaring that "the associated countries in Central and Eastern Europe that so desire shall become members of the European Union." As a result of this declaration, the European Council also stated:

[18] Twinnings paper p.8
[19] EU paper of accession instruments, p.9
[20] (EU website summary)specifically for the areas of: public service and administrative reform, legal framework for public administration, public sector financial control and external audit, public expenditure management, public procurement and concessions, management and taxation of international trade, policy capacities and regulatory management (report paper PDF)

> "Accession will take place as soon as an associated country is able to assume the obligations of membership by satisfying the economic and political conditions required."

Now the European Union had turned the question of Eastern European accession into a question of *when* accession would occur rather than *if* accession would occur. This strengthened the political incentives for the CEE-5 to implement reforms since admission was now virtually guaranteed; moreover, the EU had finally committed itself to specifying the conditions under which this admission would occur. [21] The subsequent criteria specified by the EU were the following:

Political criteria: the applicant country must have achieved stability of its institutions guaranteeing democracy, the rule of law, human rights and respect for and protection of minorities.

Economic criteria: It must have a functioning market economy, as well as the capacity to cope with competitive pressure and market forces within the EU.

Criteria of the adoption of the acquis: It must have the ability to take on the obligations related to membership, including adherence to the aims of political, economic and monetary union.[22]

The political incentives provided by entry into the union, along with the political leverage the EU employed for the CEE-5 to meet this criteria, resulted in an opening up of Eastern European political systems. Vachudova provides a thorough account of how democratization and competitivization of the political system in Slovakia, Romania and Bulgaria occurred as a result of the EU's leverage and conditionality. The EU's Copenhagen political criteria did this by providing a common political platform around which otherwise fractionalized opposition groups could cohere in order to put in place a new, democratically competitive political system. Without military threats or pressure, the Copenhagen guarantee and conditions were enough to trigger amazing political changes in post-soviet countries.[23]

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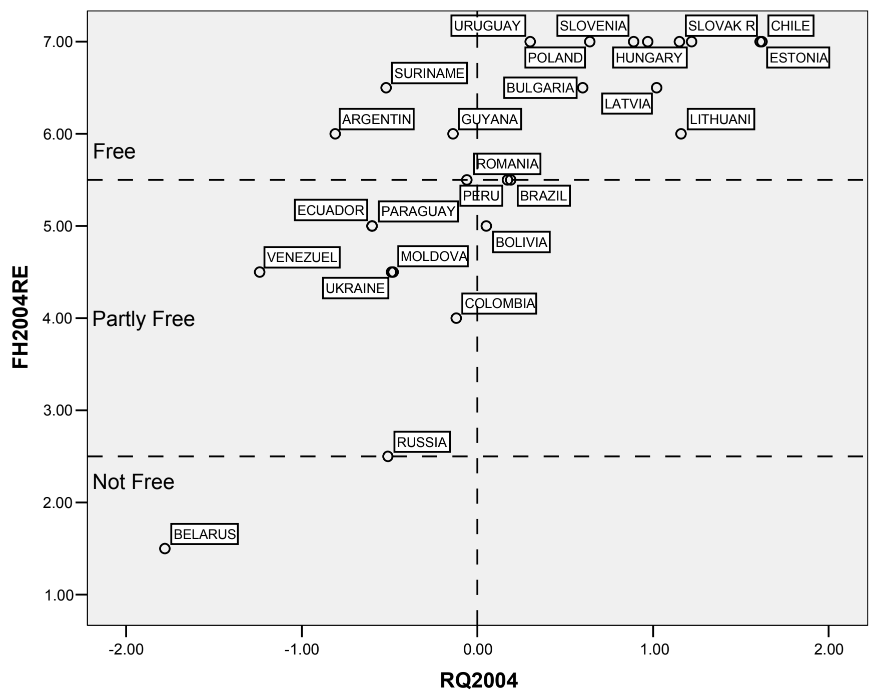
[21] http://europa.eu.int/comm/enlargement/intro/criteria.htm#cooperation
[22] www.europa.eu
[23] Vachudova

The effects of the democratic precondition for institutional development have shown themselves to be positive; the graph below shows the relationship between regulatory quality and the Freedom House political freedom ratings of each country. Countries' regulatory quality clearly increases with increases in political quality, helping to explain the success of CEE-5 efforts to reform their institutions.



Sources: Laszlo Bruszt: The Freedom House Ratings 2004, www.freedomhouse.org and "Governance Matters IV: Governance Indicators for 1996–2004", Kaufmann, Kraay and Mastruzzi (2005). Note that the FH-ratings have been recoded so that 1=7, 1.5=6.5 and so forth until 7=1.

By demanding politically competitive systems the EU therefore increased the likelihood that subsequent institutional reform efforts would be successful. Once an Eastern European country was deemed to satisfy the economic and political Copenhagen criteria however, the criteria of the adoption of the acquis still had to be satisfied before accession could occur. Whereas other Southern European states were required to put in place the acquis communaitaire *after* being admitted, the EU mandated that the Eastern countries satisfy the acquis *before* joining. The acquis communataire, an 80,000 page portfolio of European Union laws, regulations, and principles, became the backbone of the EU accession process. Divided into 31 chapters, the global application of the lengthy portfolio of EU norms and standards redefined the level of development expected by the

EU for each country in terms of economics, institutions, laws and society. TAIEX[24] was established in 1996 to provide demand-driven, short-term technical assistance to candidate countries' civil and political actors with writing, adapting and enforcing acquis legislation. TAIEX provided this assistance by advice, trainings, database tools for facilitating and monitoring the approximation process, and acting as an information broker for information on the acquis.[25] The EU accession process was now a program whose main components were trade, aid, and conditionality.

Compliance

Seven years after the creation of PHARE, three years after the Copenhagen declaration and one year after TAIEX, the European Commission realized that the political incentives the EU provided would not be enough to ensure compliance with the conditions required of the CEE-5. The traditional formula of "trade and aid" was not enough to solve enormous problems related to the CEE-5's lack of capacity and the EU's inability to properly monitor reforms due to their distance from and unfamiliarity with CEE-5 domestic conditions. In order to resolve this dilemma, the EU created a revolutionary new version of PHARE which established clear accountability structures, created a joint monitoring and learning system, and offered a wonderful assistance package to teach the CEE-5 how to go about their reforms. This new version of PHARE is the driving force behind the CEE-5 performance on the World Bank institutional development indicators, and it is what has turned the EU accession process from a simple political incentives story into a comprehensive development model.

Step 1: Accountability

The first step to reorienting PHARE was to solve accountability gaps so as to pave the way for an effective monitoring system. This was accomplished by streamlining the distribution of aid funds in each country. Firstly, candidate countries had to establish

[24] TAIEX is an acronym for Technical Assistance and Information Exchange Instrument of the Institution-building unit of the directorate general of enlargement of the European Union
[25] EU website: http://taiex.cec.eu.int

administrative agencies with which to manage funds. For PHARE, which provided the largest grants to candidates, a national fund set up within the ministry of finance in each country served as a conduit for money to reach their final destination after their approval.[26] This was called the Contracting/Financing Unit (CUFU). Clear and explicit responsibilities for fund management were outlined to administrators in the ministry of finance and accountability was placed on specific people within this ministry. All subsequent aid funds from other programs such as ISPA and SAPARD would be obtained from this national fund. To establish the agency, domestic administrators also had to undergo a complex application process before they could receive any aid. This ensured the soundness of the administration and also served as a practice run for future fund administration. Once the SAPARD program became more decentralized, SAPARD agencies also had to be accredited by the EU commission. Only SAPARD provides a fully decentralized process, with a conferral of management of funds on agencies within the applicant countries, usually in the National Ministry of Agriculture.[27] Moreover, the PHARE projects themselves were always carried out and overseen by government officials in CEE-5 administrations; responsibility for project management was never placed on private or community actors.

Step 2: Monitoring for Innovation and Reform

Next, the EU designed a system of joint monitoring and learning in a style which mimics the monitoring and learning setup proposed by Charles Sabel. This enabled the EU to revise criteria appropriately, define what metrics they would use to evaluate projects, and ensure the most accurate and consistent monitoring possible for CEE-5 reform efforts. Through reports drafted by the EU commission itself, the candidate countries and negotiations, the discussion about what the candidate countries need to do and whether or not they were doing it became intertwined and inseparable. For example, every step of reform was accompanied by negotiations; from the Europe Agreements to closing acquis chapters to using aid funds. Beginning in 1998, the European Commission published

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[26] (p.2 EU gen report of pre-accession assistance, p.9 of EU Instruments paper).
[27] p.17, 18 EU instruments).

regular, yearly reports assessing the steps taken over the past year towards implementing the acquis and providing an evaluation of how far along in the accession process the country was. The commission also began requiring that the country governments themselves provide a complimentary report called the National Accession Partnerships, 250-600 pages in length, detailing the progress made over the past year as well as the steps needed to be taken in the medium-term to implement the acquis. This enhanced both the learning capacity and criteria revision capacity of the big brother with regards to the little brother. Phare funds were refocused entirely on the pre-accession priorities highlighted in thee Road Maps and the Accession Partnerships. Western European Twinnings advisors working in CEE-5 countries were also required to submit reports back to the Commission to help provide a better picture of reform progress and needs. In a study of Twinnings projects, Berennsztein and Bohmer provide a glimpse into the information provision function of Twinnings project advisors:

> "in general, priority areas are where there are technical and administrative difficulties whose solution requires specific expertise. In some cases, there are political complications owing to the sensitive nature of the issues involved (human rights, migration), so receiving external cooperation helps diffuse potential conflicts with other political and social actors. In sum, in view of the challenge of developing state and institutional capacity, Twinning emerged as the best alternative, as it can steer clear of the risks inherent to efforts to develop institutional capacity endogenously by turning to the kind of external assistance that does not produce xenophobic reactions nor rejection for fear of excessive influence on the part of foreign powers." (p.14)

Berennsztein and Bohmer make several important points with this description of Twinnings partnerships. Firstly, while the goal of the Twinnings program was tailored to the needs of each particular country and provided human resource investment for national governments, Twinnings projects had clearly defined outcomes and goals which were meant to be measured objectively as part of project proposals and design. The experience and monitoring which this program created was the facilitating factor for revision and adaptation of the PHARE program; for example, a new "Twinnings light" was later added to address needs which should be satisfied by visits from EU experts but whose implementation only required a month or two of advising. While the EU as a more developed "big brother" could have simply told Eastern European political elites how to change their institutions, Wade Jacoby shows in his study of institutional reforms in the CEE-5 that domestic governments did not always have the preexisting institutional capacity to follow EU demands word for word, and sometimes political elites did not have the strength to oppose strong, oppositional interest groups on their own. Moreover, although Twinnings projects had specific goals and were not explicitly meant to foster binational relationship-building, they did foster understanding and cooperation between the two countries involved; hosting a Twinnings advisor from Spain for a year or two years helped humanize the face of the EU "big brother" and also helped sensitivize administrators from the more developed West to the needs and challenges facing their more "backwards eastern little brothers." As Berensztein and Bohmer point out many of the post communist states had flawed regulatory mechanisms which integrated ethnic, gender, or elitist biases. This required a more sensitive handling in terms of conditionality while suggesting the need for stronger monitoring and enforcement to ensure the elimination of such biases. [28]

Step #3: Assistance and learning for the "little brother"

The third and final component of the new PHARE program was an assistance package designed to help fund, equip and train CEE-5 political elites in institutional management and development. This component of PHARE accounted for the need for "little brothers" to learn and recognizes the need for access to resources in order for learning to take place. Equipment and supplies were provided to all projects, as were service contracts in order to show CEE-5 government staff how to use new technologies and equipment. After one year this assistance component was expanded; in June of 1999, additional areas of financial need were identified in infrastructure/environmental investments and agricultural reform. This was the origin of SAPARD and ISPA programs.[29] These funds were decentralized to address local concerns and take the stress off of EU supranational institutions. However, the EU demands on national administrations for project applications, project reporting and evaluation remain very high and demand a significant amount of administrative effort so as to prevent a decrease in

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[28] **(p.16). (http://europa.eu.int/comm/enlargement/pas/phare/index.htm).**

[29] pp.2-7 Agro summary 2002

quality or rigor of projects. The emphasis on environmental, infrastructure and agricultural reforms were not the only areas in which reforms took place however; the 31 chapters of the EU process were each addressed under PHARE at the same time from 1998-2004 in an effort to create a version of Bruzt's regulative, modern state.

The assistance component of the PHARE program also recognized the need for access to expertise and technocratic knowledge through the creation of the Twinnings program. Thirty percent of PHARE funds were set aside specifically for the purpose of institution building efforts under Twinnings to directly train government agencies and upgrade both their capacity, organization and regulatory implementation skills. According to the EU website, the primary goal of this program was to " help the candidate countries in their development of modern and efficient administrations, with the structures, human resources and management skills needed to implement the acquis communautaire to the same standards as Member States."

Incorporated into the design of this joint monitored, continuous and self-revising program of yearly projects, there is a special type of socio-political incentive specific to monitoring which according to Vachudova enhances the learning capacity of CEE-5 elites. She refers to this as "meritocracy." The logic of this argument is that if reforming political elites feel that their evaluation is fair, they are more likely to put such reforms in place. How does one design a fair process while keeping conditionality intact? One way is to allow countries to move forwards and backwards in the evaluation process rather than being kicked out if they do not immediately meet expectations. Another way is to make future qualification for funds contingent upon good management of current funds. For example, the importance of the National Development Plans is increased by its transformation into a pre-requisite for qualifying for future participation in the structural funds in the event that a country is admitted to the union. ISPA is also seen as a precursor indicating a country's ability to manage cohesion funds as well.[30] Performance in one area is therefore evaluated not only for the sake of accomplishing the tasks at hand but is also seen as a predictor of future success in other projects, increasing the pressure on CEE-5 political elites.

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[30] p.11,12 EU instruments

Moreover, the specificity of the acquis provided a more precise idea of what to monitor and learn, making evaluation and expectations more "fair": 80,000 pages of legislation, principles and regulations which form the core of the European Community were the standard by which candidate countries were held. It follows that if the EU is not clear about its standards and then condemns Eastern European countries for not meeting them, applicant countries will become frustrated and lose motivation to continue to put in place costly and lengthy reforms. Wade Jacoby shows that part of the meritocracy and fairness of EU conditionality is linked to the clarity of EU standards and demands. The more generally the EU defined the standards desired for healthcare policy and services or regional development institutions, the more difficult and less likely it is that political elites in applicant countries will effectively emulate Western institutions. This makes sense, since national political elites in Eastern Europe may not have the same conceptions about consumer protection, the relationship between the state and private or civil actors, or standards as Western Europe.

All of these monitoring, learning and resource distribution processes are coordinated by the EU Directorate General for enlargement. This department focuses solely on continuing accession negotiations, ensuring the sound use of PHARE funds, monitoring and reporting on acceding countries, and developing accountability in the use of funds so as to enhance local evaluation capacity. While many of the staff of the DG are temporary or part-time, the centralization of information and planning provided by the DG coordination efforts contribute to the accountability and monitoring aspects of the reform process in each CEE-5 country. [31] As of 2005, there are approximately 30 people in charge of 5 categories related to accession: acceding countries, candidate countries, other western Balkans, financial instruments and general matters and resources.[32]

As shown by Kaufmann et al.'s indicators, the EU's comprehensive enlargement process has produced marked improvements for the CEE-5 in terms of economic and institutional development indicators; another proof of their success is their admission into

[31] DG 2003 annual enlargement plan
[32] Directorate General Flowchart, 01.12.2005

the EU in 2004. Finally, it seems that the development that has occurred is indeed similar to the regulative state, indicating that the CEE-5 have been able to not only upgrade institutions but also modernize their economies and society.

Conclusion:

The EU accession process started out as a regular trade and aid arrangement. After the establishment of the Copenhagen Agreement in 1993, the accession process turned into an integration regime involving trade, aid, conditions and incentives. This was enough to trigger the democratization of political systems across the CEE-5. However, in order to create institutional development the EU had to reengineer PHARE so as to create new supra-national systems of monitoring, learning and compliance. It is this novel design of PHARE and the pre-accession democratic pre-condition not seen in other integration regimes which sets the EU accession apart from NAFTA and other trade regimes today. NAFTA was a one-shot deal with weak conditionality and weak enforcement mechanisms. Moreover, the preconditions of competitive, political democratization was not imposed by NAFTA. As the EU example suggests, this provides a crucial step towards meeting conditions related to regulatory quality, an opportunity which was completely passed by in the Latin American case. [33]

Section IV: Understanding Institutional Development on a Micro Level through the Phytosanitary Sector

In order to better understand and explain institutional outcomes in Mexico under NAFTA and the CEE-5 entering the EU, this paper will now look at a specific policy area and track the effects of each integration regime on institutional development. The policy area chosen for study is food health and safety because of the key role that food health and safety plays in maintaining good relations between trade partners. Enforcement of

[33] Appendix I provides a timeline of the accession process and its evolution through the 90s; it also provides tables which compare NAFTA and EU institution-building efforts.

standards is exceptionally important in this policy area, providing a prime example through which to make observations about monitoring and compliance.

International Agricultural Markets- an overview

Since the 1980s and 1990s, international agricultural trade has become increasingly liberalized. As a result, production and processing markets on domestic and international levels have been transformed. What were once homogeneous markets have now become competitive, differentiated markets with a more standards and process-oriented focus. In a discussion of non-tariff barriers to trade presented by the agricultural sector, Leonardo Iacovone concludes that "Among technical regulations and standards, sanitary and phytosanitary (SPS) regulations occupy a particularly relevant place in the regulators' agenda, because of their primary aim of protecting citizens from everyday food hazards. …These increasing concerns about food safety problems are both real because of the new potential food borne risks and perceived, especially in developed countries where demand for health and safety is fuelled by increasing income levels and recent food scares." In this context, several important issues come to the forefront. Firstly, agricultural institutions must possess considerable monitoring capacity and resources in order to ensure that all the different producers and sellers comply with their respective production processes and standards. The ability to coordinate along the food supply chain to ensure that standards have been upheld from a product's origin all the way to the sales outlet is a difficult task. Secondly, communicating changes in food standards to domestic consumers and to international markets imposes significant costs. This means that an institution must have the sufficient resources in order to be able to certify producers and assist with labeling and marketing efforts to communicate producer standards and quality to the public. Thirdly, implementing the standards themselves requires knowledge, technology and money from producers and processors. In the absence of regulatory institutions to enforce compliance, the implications of this in a differentiated market are that of a zero-sum game. Firms will either not want to comply due to the costs they have to absorb; or, if they can afford to pay for these upgrades, they will try to prevent other producers from benefiting from their efforts so as to maximize their market share and keep others out. As a result, institutions must have both enough political power and will to enforce compliance from producers.

This means that institutions need to have both innovative policy-developing abilities and implementation capacities. Underpinning all of this is the question of institutional capacity and competence- agricultural regulators are assumed to have the equipment required and also have enough technical expertise to carry out regulatory reforms. Furthermore, even if the economic and political incentives for reform are in place, national governments may not want to upgrade their phytosanitary departments because of the cost and energy that such reforms require.

Mexico, NAFTA and Food Health Safety:

Under the economic incentives theory, a hazy picture emerges as to what institutional development would look like. It is disproportionately easier for large producers to implement and address food health standards than small or middle-sized producers, either through collective efforts or through private provision. Large producers are more likely to have the disposable income to pay for private certification, are more likely to have the capacity to coordinate with other suppliers and have the market share and access to communicate with consumers. Given that they have to internalize all the costs of coordination and upgrading and that this upgrading allows them to become more competitive in a differentiated market, firms are incentivized to prevent other firms from benefiting from their improvements and new knowledge. This increases the income and inequality gap between poor producers and large agribusiness firms, suggesting that economic elites in the phytosanitary sector are unlikely to pressure the government to create better institutions.

Reardon et. al's answer to this dilemma is that the small and middle income producers will lobby the government to strengthen institutions and public-private partnerships. Consumer groups, environmental groups and labor groups could all lobby for government action as well. However, the strength and number of these types of organizations tends to be limited in developing countries, and the quantity of medium-sized enterprises present in this sector may not be very numerous. Moreover, small and medium-sized producers may or may not find governments to be responsive to their demands depending on the level of democracy and the agenda of the government.

National administrations may be perfectly happy allowing large firms to adjust to shifts in international demand through private means, collecting tax or patronage revenues from the increasingly rich economic elite. In this case, then, one can see the weakness of the economic school of thought in accounting for institutional development. The ability and motivation of economic actors to pressure the government and regional institutions in this situation is highly dependent upon the existence of robust lobby groups, a large middle class of producers, and an openly democratic and competitive government; such groups are often inexistent in developing nations.

Indeed, NAFTA's model functions mainly on the assumption that institutional development will occur as a result of incentives created by market access in specific import/export areas, direct pressure through treaty elaboration, sanction mechanisms and indirect normative pressures. NAFTA provided for the creation of a committee on agricultural trade to monitor, report and provide a forum for agricultural trade issues, while Article 722 established a committee on Sanitary and Phytosanitary matters. This committee was meant to encourage standards improvements in the territories of the parties, encourage technical cooperation, provide consultation on phytosanitary matters and help monitor phytosanitary issues.[34]

How effective has the economic incentives approach and the Sanitary and Phytosanitary Committee been in promoting institutional development? Both before and after NAFTA, phytosanitary regulations and standards in Mexico have remained poor and fragmented. Before NAFTA, phystosanitary standards were monitored and implemented by the Ministry of Agriculture, Livestock and Rural Development (SAGAR) and the Ministry of the Environment, Natural Resources and Fisheries (SEMERNAD). Minimal coordination and communication between these two departments, as well as a business culture which put profits before standards, were some of the main problems which needed to be addressed.[35] The agricultural trade committee and phytosanitary committee do not seem to have created much improvements on this front however. This can be seen through ongoing difficulties Mexican producers have with complying to US standards and the inability to reconcile food-related policy differences. Although NAFTA gave US market

[34] NAFTA secretariat online
[35] Berkley

access to Mexican avocadoes for the first time since 1914, producers were only allowed access to the Northeastern American market under a "systems approach" in 1997. This "systems approach" was designed as a scientifically supported process and is both costly and complicated to implement. Individual Mexican producers were left to pay the cost, acquire the knowledge and self-regulate in order to comply with these standards to gain market access. While NAFTA did specify that parties could request technical assistance, the treaty provided no aid or regular training projects for the SEMARNAT or SSA. Thus, trade opening through NAFTA did not equally guarantee market access to all Michoacan avocado growers.[36]

Despite an increase in agricultural trade and an improvement in the design of Mexico's unilateral agriculture subsidies,[37] a number of food health derogations have been documented since NAFTA. These derogations indicate the inability of the NAFTA setup to encourage an improvement in phytosanitary standards. In 1996 at least 200 Michigan students and teachers fell ill from Hepatitis-A infected strawberries imported from Mexico. FDA investigators identified the origins of the contaminated fruit in San Quentin and Baja California Norte areas where workers were cultivating fruit under unsanitary conditions. Open-pit latrines and nonexistent hand-washing facilities were singled out as part of the problem's cause, producing a significant negative impact on domestic Mexican strawberry farmers in 1997 from negative publicity.[38] Nor have the agriculture or phytosanitary committees been able to coordinate national policies and stances on genetically modified corn in between the US and Mexico; while the US is in favor of more lenient standards, a non-GMO stance allows Mexico to maintain more control over the structure of its agro-food system and source of its food supply. The disputes arising from these differences have created a large public debate in which a more zero-sum outlook on agricultural policy seems to prevail.[39] This is a far cry from the standardization and harmonization expected of phytosanitary institutions in Mexico under the economic incentives theory.

The EU Phytosanitary Model

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[36] Bredahl and Holleran, Section: "the US-Mexico avocado dispute"
[37] PROCAMPO program de-linked the amount of income support from production decisions (WB 2003 report)
[38] John Henkel, "Food Firm Gets Huge Fine for Tainted Strawberry Harvest"
[39] McAfee, p.10

In contrast to the NAFTA case, the PHARE program's design has proven itself to be well suited for developing institutions in the food health safety policy area. Accountability structures have improved the effectiveness of reforms, while monitoring and learning have allowed the EU to revise its criteria and expectations appropriately. Monetary and technical assistance have also facilitated the institutional upgrading necessary for compliance with the standards of the acquis, complementing the first two components of the program very nicely.

Accountability for phytosanitary reforms have been maintained during PHARE phytosanitary projects through clear delineations of the government agencies involved in each aid contract. On the first page of each project contract the "location" of the project is always specified; for phytosanitary regulations, the "location" is typically the Ministry of Agriculture, Ministry of Health or another related institution. Each PHARE project specifies goals for the project which are either linked to the acquis or problem areas identified by the NPAA or previous European Commission studies. This enables project evaluations and responsibility to be as objective, clear and consistent as possible. In addition, numerous projects under this category sought to reorganize or create new phytosanitary institutions in order to improve the transparency, accountability and capacity of domestic institutions. For example, a 1998 PHARE project in the Czech Republic established an agricultural payment agency, and in 2002 a project was carried out to reorganize the Czech Agriculture and Food Inspectorate through a Twinnings project.[40]

The monitoring and learning methods which allow the EU to revise and set criteria for the CEE-5 have also fared well in the phytosanitary sector. This is because the complexity of regulatory monitoring in this policy area increases the need to revise criteria to adapt them to local conditions. CEE-5 governments could simply borrow policies from neighboring countries or other developed nations, but the disparity and differences across regions, products, testing methods, and understanding of consumer demands and behavior varies enough that simply copying institutional structures and policies may not be enough to ensure effective reforms. As a result, the PHARE program arranged for studies evaluating market functionality and sector competitiveness to get a better picture of the issues on the ground; for example, in 1999 a project was commissioned with the express

[40] CZ fite fiche II 2002

purpose of assessing the capital and technical needs to be met in order for the Czech State Phytosanitary Administration to reach full conformity with the acquis regarding plant health diagnostics.[41] An example of the revision capacity provided by the PHARE program can be seen in the transitional period granted to smaller food producers and providers in candidate countries so as to help them make the necessary changes to sell their products on the common market. Producers who could not meet regulations were still allowed to sell their product to domestic markets even though they would not be allowed to access the European market so as to protect the diversity of products offered on the European market and allow for a certain amount of self-regulation.[42]

The EU also established a supra-national committee in charge of monitoring food health safety called the Food and Veterinary Committee. Its responsibility was to monitor the standards and procedures of new members through peer reviews, workshops, technical meetings, seminars and questionnaires. Missions to the candidate countries started in 2001 and were the trop priority for 2002 and 2003.[43] Commissioned on a yearly basis, each project which employed a Twinnings advisor also used that advisor as someone who would report back to the European Commission along with their national CEE-5 partner. In the event that a project did not measure up to expectations, it could be cancelled and the money would be reabsorbed and reused for the following year's projects. Projects could also build on work from the previous year to maximize efforts: for example, in 2000 a project was commissioned to compliment other projects meant to strengthen the regulatory capacity of the SPA (state phytosanitary administration) started in 1999 for plant registration and quarantines.[44] In this manner, food health and safety institutional reform becomes a joint process between the EU and the CEE-5 where the monitoring process is intermeshed with efforts to learn more about Eastern European administrations so as to better set targets, evaluations and conditions.

3) Finally, significant resources were dedicated to this sector both in terms of Twinnings advisors and equipment. Multiple Twinnings visits to reorganize government structures

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[41] fito fiche 1999, I
[42] Press releases
[43] Eu enlargement: memo/03/88
[44] Czech 2000 fite fiche III

and TAIEX or short-term Twinnings visits to provide trainings to government staff were only a few of the projects carried out with the help of Western European government officials under PHARE. PHARE also provided funds to supply computers, data software, laboratory equipment to test for microbes and bacteria, even construct new buildings for border inspection posts. This ensured that CEE-5 regulatory institutions would not come short of acquis expectations due to a lack of resources. After all, the available income at the disposal of post-communist, Eastern European elites would most likely not have been spent on such equipment given the state of poverty out of which these countries were emerging at the time.

Although there do not exist institutional indicators for agricultural sectors analogous to those provided by Kauffman and the world bank, the information on EU accession indicate that the program has been effective. An EU press release cited the flexibility and revisional nature of the accession process produced by the criteria revision process as in integral part of setting up the EU internal market and while also maintaining the diversity of European agricultural products.[45] According to an EU press release on the 15th of April 2004, only 1006 food processing establishments had to be granted transition periods, representing 8% of the food processing establishments in the concerned countries. . Moreover, the new Border Inspection Posts established in the CEE-5 were deemed satisfactory enough to replace those in Western European countries as part of the communal market border, and "the Commission **approved 22 BIPs** in the new Member States as meeting EU standards. The Commission intends to approve a further lists of BIPs in time for accession bringing the total number of new BIPs up to 37." [46]

Conclusion:

[45] Commissioner Byrne: promoting food safety and diversity throughout an enlarged EU, (13 May 2003) http://europa.eu/rapid/pressReleasesAction.do?reference=IP/03/700&format=HTML&aged=0&language=EN&guiLanguage=en.

[46] EU press release, (Brussels April 14 2004) http://europa.eu/rapid/pressReleasesAction.do?reference=IP/04/485&format=HTML&aged=0&language=EN&guiLanguage=en

This paper has provided a review of the literature on institutional development to highlight a missing link in conceptions about the ways in which institutional reforms are brought about by international integration regimes. This missing link lies in the different mechanisms of monitoring, learning and compliance which "big brothers" use with regards to "little brother" members. The EU and NAFTA case studies provide valuable insights about the nature and effects of these mechanisms. The EU-NAFTA comparison shows that while political and economic incentives play a role in institutional development, they are only sufficient to lay the groundwork for this development. Specifically, economic and political incentives establish the democratically competitive political system and functioning market economy necessary to begin reform processes. Institutional reforms only come about once these systems are put in place and once additional, extensive conditionality specifying institutional standards along with compliance and monitoring systems are established. Given that institutional development occurs through a specialized process of monitoring and learning, the EU development model could potentially be recreated for Latin America. The challenge lies in the strain that such a development model places on existing institutional capacity and financial resources in advanced country members, making makes the question of political commitment a central issue. However, the first step is to recognize how this mechanism is created and acknowledge the possibility of replicating it; with the plethora of international aid organizations and associations in the world today, hopefully someone will take the lead and be able to help Latin America experience the same institutional growth that the CEE-5 has been able to achieve.

APPENDIX I:

EU timeline

•1990: creation of PHARE and Europe Agreements. Demand driven: meant to help create market economy and establish bilateral relations. "Trade and aid"
•1994 criteria: market economy, political liberalization, ability to implement acquis BEFORE joining. Conditions and political incentives.
•1996 creation of TAIEX
•1998 Re-engineering of PHARE *for 31 areas of the acquis*: trade, aid, conditions, incentives, compliance
•2000 ISPA, SAPARD
•2004 ACCESSION

NAFTA timeline

- 1994 NAFTA signed: trade, dispute resolution and economic incentives
- 1994 creation of NAD Bank , BECC *for environmental issues only*
- 1996 Renewal of NAD Bank and BECC by EPA and SEMARNAT

NAFTA Border Program funding:
(source: Border 2012 summary document)

Capacity Building Needs & Solid Waste Technical Assistance Program.

The total funding amounts, projects and communities benefited in both countries under both programs are summarized below.

Country	Communities*	Projects	Amount (US$)	Percent
Mexico	64	132	$11,132,394	36%
United States	71	105	$19,440,549	64%
Total	135	237	$30,572,943	100%

* A community may have several projects; communities are not duplicated in total count

Public Participation	Mexico	U.S.
Citizen committees formed	52	74
Local organizations contacted (estimated)	499	582
Public meetings held (required & others)	170	201
Project videos produced	17	26
Total projects certified	**36**	**69**

NADB Financing as of December 31, 2005
(Millions of dollars)

	Total	U.S.	Mexico
Projects requiring NADB financing	91	61	30
Projects with approved financing	90	61	29
Total project costs	$2,347.9	$1,024.1	$1,323.8
Total NADB participation	$703.8	$360.4	$343.4
Total financing contracted	$658.0	$324.6	$333.4
Total financing disbursed	$378.6	$180.4	$198.2

BECC Project Certifications as of December 31, 2005

Projects	Total	U.S.	Mexico
Water and wastewater	67	45	22
Solid waste	13	4	9
Air quality	4	0	4
Water conservation	21	20	1
Total	**105**	**69**	**36**

EU chart
Source: Phare Brochure 0503

Program	***Date***	***Countries***	***$$***	***Goals***
PHARE I	1990	Poland, Hungary, 10 CEE	EBRD takes on 10 CEE between 92 and 93	Functioning market economy
TAIEX	1996	Cyprus, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovak Republic, Slovenia		Technical assistance for adopting legislation from acquis
PHARE II	1998	All countries undergoing accession	Approx. 1.6 billion euro annually	Capacity to implement acquis ***in 31 different policy areas***
Twinnings	1998	All	30% of PHARE funds set aside, 475 projects from 98-01	Institution-building through increased human capital and knowledge-sharing
SAPARD	2000	All	Approx. 0.5 billion euro/yr	Agricultural competitiveness, CAP
ISPA (EC)	2000	All	Approx. 1 billion euro/yr	Environmental and transport infrastructure