

# NAFTA and the U.S.-Mexican Trucking Dispute

Robert J. Carbaugh\*

Central Washington University

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**Abstract** Although the charter of the North American Free Trade Agreement established a schedule that would have opened the border states of the United States to competition from Mexican trucking companies in 1995, and all of the United States to this competition in 2000, the full implementation of these provisions has been delayed due to concerns about the safety of Mexican trucks and drivers. This delay has resulted in much frustration for Mexico, which, in 2009 implemented retaliatory tariffs on products imported from the United States. In March, 2011 the two countries unveiled a deal to resolve this dispute which could help ease tense relations between the two neighbors. This paper discusses the nature and significance of the trucking dispute between Mexico and the United States.

*Keywords:* Transportation, trucking, NAFTA

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## 1. Introduction

The economic ties between Mexico and the United States are of importance to policymakers because Mexico borders the United States and because of the significant economic links connecting the two countries. It is also of strategic importance for the United States to have a prosperous, democratic, and friendly Mexico as a neighbor. Mexico is the United States' third largest trading partner, after Canada and China, while the United States is Mexico's largest trading partner. Trucks carry about 80 percent of the cargo, by value, from the United States to Mexico, and vice versa.

The United States and Mexico have had substantial economic connections through the North American Free Trade Agreement (NAFTA), which began in 1994. Before NAFTA, Mexico used the economic policy of import substitution, in which it attempted to grow certain domestic industries through trade protection. An example is Mexico's automobile industry, which was heavily regulated by the Mexican government from the 1960s to 1990. The government imposed import tariffs up to 25 percent on automotive products and levied restrictions on foreign automobile production in Mexico. However, Mexico's protectionist policies did not yield the expected positive results on economic growth, and so the country moved toward a policy of economic deregulation.

The enactment of NAFTA was an important step in Mexico's adopting freer trade policies, as were its efforts to privatize some of its state industries. Since the early 1990s, Mexico's trade policy has been among the most open in the world. By early 2011, Mexico had entered into a

total of twelve free trade agreements involving forty-two countries. Most studies conclude that the overall economic effects of NAFTA on Mexico (and the United States) have been small but positive, although some sectors in both countries have encountered adjustment burdens. (Lederman, et. al, 2002)

Prior to NAFTA, the United States used two different trucking policies when dealing with Canada and Mexico. The United States allowed Canadian cargo trucks to enter through its borders, largely because U.S. truckers were allowed to deliver cargo to Canada. Yet the United States prevented Mexican truckers from obtaining operating licenses in the United States. However, Mexican trucks destined for Canada were allowed to travel through the United States as long as they adhered to U.S. safety regulations and insurance requirements. The United States essentially maintained an open trucking policy for Canada and a closed trucking policy for Mexico. In similar fashion, the government of Mexico prevented U.S. trucks from delivering cargo into that country.

Although NAFTA was primarily intended to abolish barriers on the trade of goods and services between the United States, Mexico, and Canada, it was also intended to open the signatories to cross-border trucking competition. This implies that Mexican trucks and drivers can compete on various routes against U.S. trucks and drivers. To achieve this goal, NAFTA adopted the principles of nondiscrimination and Most-Favored-Nation Treatment which mean that the contracting parties shall not treat domestic market participants more favorably than foreign market participants. These principles apply to all types of governmental trade obstacles, such as border measures and internal regulations (e.g., taxes and product standards). In the case of trucking, the principles mean that the United States should hold Canadian and Mexican trucks and drivers to the same inspection, safety, and financial standards that apply to its own drivers, thus promoting cross-border competition. Simply put, by removing restrictions on cross border trucking operations, NAFTA was supposed to move the signatories to an environment of open competition in trucking. (MacDonald, 2009)

NAFTA established a two-stage schedule that would have opened the United States to cross-border trucking competition. In the first stage, which was to begin in 1995, the United States would allow Mexican trucks into the four U.S. bordering states--Texas, New Mexico, Arizona, and California--and Mexico would allow U.S. trucks into its six border states. The second stage was to begin in 2000, whereupon trucks from the United States would be permitted to travel throughout Mexico, and Mexican trucks would be permitted to travel throughout the United States.

However, trucks did not cross the borders according to NAFTA's timeline. On the day before the first stage of the cross-border trucking was to begin, President Bill Clinton placed a moratorium that blocked cross-border trucking with Mexico. Clinton's official reason was that Mexico's trucks and drivers were not as safe as U.S. trucks and drivers, and additional time was necessary to study the situation. Clinton also expressed concerns about illegal drugs and immigrants being transported into the United States by the Mexican trucks. However, critics felt that Clinton's delay was primarily intended to appease the U.S. trucking industry, notably the Teamsters Union (International Brotherhood of Teamsters), which felt threatened about losing jobs to lower paid Mexican drivers.

The Teamsters Union's concerns about job losses for its members was supported by data showing that Mexican truck drivers on average earn from one third to one half the wages of U.S. truck drivers, thus providing Mexican trucking firms a competitive advantage. However, the majority of the cost advantage due to lower wages can be offset on any job without a revenue-earning backhaul--the pick up and making a domestic U.S. delivery on the way back to Mexico. Also, truck-driver wages in the United States are only about one-half of operating costs. Other factors that work against the lower costs of Mexican trucking firms' lower wages include: higher equipment costs in Mexico; fewer financing options in Mexico; and relatively high maintenance costs in Mexico due to poor road conditions. (Case, 2002)

U.S. policies that have prevented Mexican trucks from delivering cargo to U.S. customers have resulted in much frustration for the Mexican government. The cross-border trucking dispute reached a climax in 2009, when Mexico imposed retaliatory tariffs on U.S. imports. However, in March, 2011, the two countries unveiled a deal to resolve this dispute, which could help ease tense relations between the two neighbors. This paper discusses the nature and significance of the trucking dispute between Mexico and the United States.

## **2. The U.S.-Mexican Trucking System**

For decades, the safety of the trucking system has been of concern to Americans as well as people of other countries. The United States has laws on its books that limit the number of consecutive hours a trucker can be on the road. We periodically test our drivers for drug or alcohol use. We inspect every vehicle. We have a computerized database to check the validity of licenses and the prior violations of anyone licensed to operate a tractor-trailer. We require thorough training for every U.S. trucker on the road.

When the NAFTA agreement was negotiated, analysts noted that Mexico did not maintain as stringent trucking regulations as the United States. These analysts maintained that Mexican drivers were not subject to roadside inspection and drug testing, the requirement of logbooks or weighing stations for trucks, mandatory labeling of hazardous or toxic cargo, or a system to verify drivers' licenses. Also, Mexican trucks were not required to have front brakes and were permitted a gross vehicle weight 17,000 pounds heavier than permitted on U.S. roads. According to the U.S. Teamsters Union, Mexico's unsafe trucks and drivers should not be allowed to compete with Teamsters Union truckers along the highway trade corridors within the United States.

The ratification of NAFTA resulted in the agreement of the United States, Mexico, and Canada to open their roads to each other's trucks according to the time schedule mentioned above. Largely because of fears about the safety of Mexican trucks and drivers, in 1995 President Bill Clinton delayed the implementation of an open trucking policy by imposing restrictions on Mexican trucks, confining them to commercial areas within 25 miles of the Mexican border. Mexican goods traveling beyond this zone, deeper into the United States, had to be loaded onto American trucks, a practice that pleased the Teamsters Union.

Despite bilateral meetings intended to bring Mexican truckers up to U.S. safety requirements, no agreement was reached on implementation. Therefore, Mexico imposed a border ban against U.S. truckers: U.S. rigs could cross the Mexican border but could not leave a commercial zone that extends no more than 25 miles. Like Mexican drivers on the other side, American truckers drop loads at transfer points, from which Mexican truckers complete the delivery.

In Mexico, as in the United States, two trucking businesses evolved: long-haul companies that use newer, better-maintained vehicles, and short-haulers with older fleets that travel just short distances. For example, Mexican products rolling into the United States arrive at a Mexican border depot on long-haul trucks. They are loaded onto short-haulers. (These go back and forth over the border between depots on both sides.) Finally, an American long-haul trucker takes the cargo from the American border depot to its U.S. destination. This requires three to five trucks to cross one line. A similar system applies to the transport of goods from the United States to Mexico. Indeed, the movement of goods across the border of the two countries was quite inefficient and costly.

Not only was NAFTA intended to yield free trade in goods and services for the signatories, it was also meant to decrease transportation costs through competition in trucking. By allowing Mexican long-haul trucks to transport goods directly into the United States (beyond the 25-mile commercial zone) and likewise for U.S. long-haul trucks to go deep into Mexico, the need for storage and warehousing would decline. The reduction in short-haul truckers would cut costs to shippers and, because they normally do not back haul, the traffic and congestion on the border would be reduced due to fewer empty trucks. Therefore, economic efficiencies created by free trade in goods and services would also yield efficiencies in cross-border transportation of these products.

### **3. Arbitration Panel Rules in Favor of Mexico**

Despite the advantages of NAFTA, the United States refused to comply with NAFTA's regulations providing an open border policy in ground transportation of goods across the U.S.-Mexican border. Mexico's dissatisfaction regarding this issue resulted in its submission of the dispute to the NAFTA resolution panel in the year 2000. Also, Canada intervened in the conflict on behalf of Mexico, maintaining that NAFTA required the equal treatment of foreign and domestic truckers. However, the United States justified its position on the grounds of safety of trucks and drivers.

In 2001, the NAFTA resolution panel unanimously supported Mexico's position by determining that the blanket refusal of the United States to process applications of Mexican truckers for entry into the United States was in violation of its NAFTA obligations. Moreover, the alleged shortcomings of Mexico's regulations of commercial trucking did not free the United States from its NAFTA obligations. However, the panel did determine that the United States could apply more stringent standards to Mexican truckers than are applied to U.S. and Canadian truckers, as long as the Mexican truckers are reviewed on an individual, case by case basis. When the resolution panel made its ruling, it authorized Mexico to issue retaliatory tariffs against the United States if compliance did not take place. It turned out that Mexico patiently gave the

United States eight years to comply with NAFTA before resorting to retaliatory tariffs.

Although President George W. Bush indicated a willingness to comply with NAFTA's cross-border provisions, he was opposed by labor and environmental groups who did not want Mexican cargo trucks to travel throughout the United States. Also, in 2002 the U.S. Congress mandated 22 conditions for opening the border beyond the commercial zone to Mexican cargo trucks. These requirements were in addition to the previous conditions that Mexican truckers had to meet for entry into the United States--alcohol and drug tests, hours-of-service limitations and logbook rules, insurance requirements, and so on. Examples of these additional requirements included:

- All Mexican trucks are subject to U.S. Department of Transportation safety examinations before being granted operating authority.
- Mexican truckers applying to operate beyond the 25 mile commercial zone must have a distinctive company identification number.
- Mexican trucks may enter the United States only where a certified safety inspector is on duty.
- Weigh scales must be installed at the ten highest-volume border crossings.
- Safety inspectors must verify the validity of the license of each Mexican driver carrying hazardous materials, as well as 50 percent of the licenses of all other drivers.

These additional requirements were in excess of the requirements that applied to U.S. and Canadian truckers operating in the United States. (Frittelli, 2010)

#### **4. The Cross-Border Demonstration Project**

The official reason that the Bush administration did not respond immediately to the 2001 ruling of the NAFTA resolution panel was that Congress remained skeptical about the safety of Mexican trucks. However, there also was increasing concern in the United States about drug-related violence in Mexico and human smuggling along the U.S.-Mexico border. The Mexican government threatened to levy tariffs in retaliation for the prolonged inaction of the Bush administration. Mexico's President, Vicente Fox, even threatened to totally close the border to American cargo trucks. Meanwhile, Mexican trucks were limited to the 25-mile commercial zone in U.S. border states, while a similar program existed for U.S. cargo trucks going to Mexico. From 2001 to 2006, Congress passed several pieces of legislation that made NAFTA's cross-border provision unachievable.

In 2007, the Bush Administration announced a pilot program to determine if the NAFTA cross-border provision would work. Known as the Demonstration Project, it allowed approved Mexican trucks from 100 trucking firms full access to U.S. highways, with a similar program allowing U.S. trucks to travel beyond Mexico's commercial zone. Although the pilot program did not fulfill all of NAFTA's cross-border trucking provision, which would have allowed all Mexican trucks to operate within the United States, it provided a compromise in the heated controversy between Mexico and the United States. During 2007-2009, 29 trucking firms from Mexico were granted operating authority throughout the United States. In total, 103 Mexican

cargo trucks were used by these firms as part of the program, and they crossed the border about 12,500 times to make U.S. deliveries. During the same period, 10 U.S. trucking firms participated in the reciprocal project, and they operated 55 trucks making about 2,200 trips into Mexico.

The record of the pilot program provided considerable support for the improving safety of Mexico's trucks and drivers. According to the Secretary of the U.S. Department of Transportation, the safety of Mexican trucks had improved from the previous decade and was now comparable to U.S. trucks, and Mexican drivers were generally safer than U.S. drivers. This conclusion applied to Mexican trucks operating within and beyond the U.S. commercial zone. (Peters, 2008) Also, there was no evidence to suggest that human smuggling or drug trafficking activities had increased during the pilot project.

Although only a small number of Mexican trucks entered the United States under the pilot program, there was substantial concern about the program and its potential for many additional trucks and drivers to be on U.S. highways. Also, the Teamsters Union continued to insist that permitting Mexican trucks in the United States would confiscate jobs from U.S. truck drivers. Despite the success of the pilot program, in March, 2009 President Barack Obama signed legislation that eliminated funding, thus killing the program. All of the progress that the United States and Mexico had made on the issue of cross-border trucking came to an abrupt halt, and Mexican trucks could no longer travel beyond the commercial zones along the border. Given the favorable safety statistics produced by the pilot program, it appears that this unilateral move was more politically motivated than safety-minded.

## **5. United States and Mexico Tentatively Agree to Settle Trucking Dispute**

In response to the termination of the pilot program, the Mexican government in March, 2009 increased tariffs on 89 products, with a value of \$2.4 billion, that were imported from the United States. Calibrated to make U.S. products uncompetitive in Mexico's market, the tariffs ranged from 10 to 45 percent and covered a variety of products that included paper, home appliances, vegetables, fruit, Christmas trees, suntan lotion, and other consumer goods. Among the states hit hardest by Mexico's tariffs were California, Oregon, and Washington, which exported these products to Mexico.

To add to political pressure, in August, 2010 the Mexican government announced a new list of retaliatory tariffs on imports from the United States. This list added 26 products to, and removed 16 products from, the original list of 89, bringing the new total to 99 products from 43 states, with a total export value of \$2.6 billion. However, the new retaliatory tariffs were less than the original tariffs and ranged from 5 to 25 percent.

The effect on U.S. exporters was magnified beyond the retaliatory tariffs themselves because the Mexican government randomly rotated the target of the duties. For instance, one month pork bellies would be hard hit, but wine would be adversely taxed the next month. This random application of tariffs across a broad range of U.S. goods made it impossible to make appropriate business plans, such as pricing and investment, and the cost to U.S. producers was far greater

than the tariffs themselves. Mexico's tariff rotation strategy obviously was designed to apply maximum pressure on American producers, their powerful lobbies, and also influential lawmakers from states seeking a settlement of the trucking conflict.

On a bipartisan basis, members of Congress increasingly complained that Mexico's retaliatory tariffs were having substantial adverse impacts on economies in states like California and on local industries, notably agriculture. For example, it was estimated that U.S. potato exports to Mexico had decreased by 50 percent in value since the tariffs had been adopted, and that U.S. exporters were losing market share to their Canadian competitors. (Tsui, 2010) Clearly, the retaliatory tariffs added friction between the Obama administration, seeking to expand trade opportunities that would result in increased American jobs, and Congressional Democrats allied with unions and independent truck drivers, who supported the trucking restrictions. Among the groups who supported Obama on this issue was a coalition of agriculture and industry interests that were led by the U.S. Chamber of Commerce.

In March 2011, President Obama and President Felipe Calderon of Mexico unveiled a deal to resolve the dispute that kept Mexican trucks off American roads and resulted in billions of dollars in tariffs on U.S. exports to Mexico. Under the plan, in exchange for giving Mexican trucks access to U.S. roadways, the Mexican government will eliminate its \$2.6 billion in tariffs targeted at 99 products. The first half of the tariffs will be removed after both governments sign the agreement. The remaining tariffs will be eliminated after the first Mexican truck is certified under a series of new standards, including English-language, drug, and safety tests, which are monitored by the U.S. Department of Transportation. The proposed project will not be a pilot program but an initial stage that will include several thousand trucks and eventually bring as many vehicles as needed into the United States.

The proposed requirements for Mexican trucks are more stringent than those previously established in NAFTA and somewhat tougher than those currently in force for American truckers. For example, Mexican trucks will have to carry electronic recorders to ensure that they make only cargo trips across the border and to track compliance with U.S. hours-of-service laws. This means that Mexican trucks will be prohibited from hauling freight between destinations within the United States. The agreement, by simplifying the border crossing process, would boost Mexico's ability to compete in international trade by decreasing transport costs. The Obama-Calderon agreement is subject to ratification by the governments of Mexico and the United States, which could occur later in 2011.

The American Trucking Association praised the announcement, saying it will promote two-way trade between the United States and Mexico. However, the Teamsters Union and certain trucking companies oppose the deal, saying it sacrifices American jobs when unemployment is high so that big business can save money partly by hiring cheaper drivers.

## **6. Conclusion**

Whether or not the United States should fulfill its NAFTA commitment and allow Mexican cargo trucks to travel throughout the United States is a controversial issue. On one hand, free

traders have favored an open transportation policy on the grounds that it will lead to greater economic efficiency and benefits to consumers in the form of lower prices. They also note that the world opinion of the United States has deteriorated as the U.S. has maintained its refusal to grant access to Mexican cargo trucks. However, the Teamsters and other unions have officially opposed an open transportation policy on the grounds of truck safety, although job preservation for their members appears to be an important part of their motivation.

Indeed, strong political forces have served as a barrier to an open trucking policy. During his campaign for the presidency, Barack Obama maintained that an open transportation policy should not be applied to Mexican drivers and that the United States should renegotiate NAFTA. Since Obama became president, he has slowly moved in the direction of granting access to Mexican truckers, as seen in his March, 2011 announcement of a trucking deal with Mexico. Nevertheless, a skeptical Congress has dragged its feet on forming free trade and transportation deals not only with Mexico, but with other countries such as South Korea and Colombia. At the writing of this paper, it remains to be seen if President Obama can convince Congress to ratify his trucking deal with Mexico.

What will be the effects for commercial trucking under the Obama-Calderon deal? It is likely that the opening of the Mexico-U.S. border will be based on gradualism, and therefore the effects will be modest. That is, there will not be an immediate surge of U.S. long-haul trucks into Mexico during the first several years after enactment, nor a surge of Mexican long-haul trucks into the United States (Fritelli, 2010). Why is this so?

Mexican cargo trucks operating in the United States will continue to encounter several disadvantages. Increased border delays since the September 11 terrorist attack against the United States have added to the time that Mexican trucks and drivers are not operating, resulting in increased costs that burden long-haul cargo companies and discourage them from making commitments to trade with the United States. Moreover, Mexican trucks will be handicapped by relatively high costs of insurance, an English language requirement that restricts the number of Mexican trucks that can operate legally in the United States, and relatively higher interest rates due to less access to financial resources than their American competitors.

Another disadvantage to Mexican trucking companies operating in the United States is that the profitability of trucking declines with an increase in the distance that empty trailers are hauled. For a Mexican trucking company, lower wages of Mexican drivers increase its competitiveness. However, this advantage can be significantly offset by the lack of a revenue-earning backhaul, since it is illegal for a Mexican truck to pick up and make a domestic U.S. delivery on the way back to Mexico. Therefore, it is likely that only the U.S.-Mexico border states will initially serve as the major zone of competition; that is, only a few Mexican trucking firms that develop business relationships with American customers will be able to benefit from backhaul loads from deep in the United States to Mexico.

The likelihood of substantial numbers of U.S. trucking companies' immediately providing cargo service deep into Mexico also appears to be low. Once an American truck and driver enter Mexico, they encounter a labor cost disadvantage relative to their Mexican competitors. Also, many U.S. drivers do not speak fluent Spanish, and they may also believe that Mexico is

becoming an increasingly dangerous place to operate, in view of the violence of Mexican drug cartels. These factors will continue to discourage long-haul U.S. cargo truckers from traveling very far into Mexico. Most of the access will likely be near the border, where Mexican trucking firms will face increasing competition from American companies serving the industrial parks' (maquiladora) trade.

Over the longer run, the ability of Mexican truck companies to extend their range into the United States, or U.S. trucking companies to penetrate Mexico, will become less dependent on government rules applied to commercial activities and more dependent on the economics of global trucking. The major determinant of the growth of border truck crossings has been the growth in trade between the two countries, which determines the amount of freight that must be transported across the border. It is unlikely that the Obama-Calderon plan to open transportation networks will, by itself, result in a substantial increase in the amount of cargo transported across the border.

The economic relationship with Mexico is strategic to the United States because of the implications it has for bilateral trade, economic conditions in both countries, economic competitiveness, and border security. President Calderon and President Obama have reaffirmed their shared values and the need for increased cooperation in North America to promote economic growth and competitiveness. If the United States is to deepen economic integration with Mexico, it is necessary that the long-standing trucking dispute between these countries be put to an end.

## Endnote

\* Department of Economics, Central Washington University, 400 E. University Way, Ellensburg WA 98926. Email: [carbaugh@cwu.edu](mailto:carbaugh@cwu.edu).

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